

# Regulatory Notice

## 12-39

## Trade Reporting and Compliance Engine (TRACE)

### FINRA Requests Comment on TRACE Dissemination Issues

**Comment Period Expires: October 10, 2012**

#### Executive Summary

FINRA requests comment on two issues relating to the dissemination of information on TRACE-eligible securities transactions.

First, FINRA seeks input on whether it should maintain or modify current TRACE dissemination caps, under which the actual size (volume) of a transaction over a certain par value is not displayed in disseminated real-time TRACE transaction data. Second, FINRA requests comment on whether transactions in TRACE-eligible securities effected pursuant to Securities Act Rule 144A<sup>1</sup> (Rule 144A transactions) should be disseminated, and if so, the scope and manner of such dissemination.

Questions regarding this *Notice* should be directed to:

- ▶ Elliot R. Levine, Associate Vice President and Counsel, Transparency Services, at (202) 728-8405; or
- ▶ Sharon Zackula, Associate Vice President and Associate General Counsel, Office of General Counsel, at (202) 728-8985.

#### Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by October 10, 2012.

Member firms and other interested parties can submit their comments using the following methods:

- ▶ Emailing comments to [pubcom@finra.org](mailto:pubcom@finra.org); or

#### September 2012

##### Notice Type

- ▶ Request for Comment

##### Suggested Routing

- ▶ Compliance
- ▶ Fixed Income
- ▶ Legal
- ▶ Trading

##### Key Topics

- ▶ Dissemination Caps
- ▶ Rule 144A Transactions
- ▶ TRACE Dissemination
- ▶ TRACE-Eligible Security

##### Referenced Rules & Notices

- ▶ FINRA Rule 6710
- ▶ FINRA Rule 6750
- ▶ Securities Act Section 3
- ▶ Securities Act Section 5
- ▶ Securities Act Rule 144A

- ▶ Mailing comments in hard copy to:  
 Marcia E. Asquith  
 Office of the Corporate Secretary  
 FINRA  
 1735 K Street, N.W.  
 Washington, D.C. 20006-1506

To help FINRA process and review comments more efficiently, persons should only use one method to comment on the proposal.

**Important Notes:** The only comments FINRA will consider are those submitted using the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA website. Generally, FINRA will post comments as they are received.<sup>2</sup>

## Background & Discussion

### Dissemination Caps

As part of the initial TRACE implementation in July 2002, FINRA established dissemination protocols that included certain caps. Disseminated TRACE transaction data includes price, time of execution, size and other information. The size disseminated is the total par value of the trade, subject to the limits of the applicable dissemination cap.

- ▶ For investment grade TRACE-eligible securities and agency debt securities, the current dissemination cap is \$5 million, and a transaction in excess of \$5 million is disseminated as "\$5MM+."<sup>3</sup>
- ▶ For non-investment grade TRACE-eligible securities, the current dissemination cap is \$1 million, and a transaction in excess of \$1 million is disseminated as "\$1MM+."<sup>4</sup>

FINRA recently announced additional caps as part of the dissemination of transaction information on agency pass-through mortgage-backed securities traded to be announced (TBA transactions).<sup>5</sup> FINRA will begin disseminating TBA transactions on November 5, 2012.

- ▶ For TBA transactions eligible "for good delivery," the dissemination cap is \$25 million, and a transaction in excess of \$25 million will be disseminated as "\$25MM+."
- ▶ For TBA transactions "not for good delivery," the dissemination cap is \$10 million, and a transaction in excess of \$10 million will be disseminated as "\$10MM+."<sup>6</sup>

## Discussion

FINRA periodically evaluates current practices and seeks input on modifications that may be beneficial. FINRA seeks comment as to whether to modify, leave unchanged or eliminate the \$1 million and \$5 million TRACE volume dissemination caps, which have been in place since TRACE began operating on July 1, 2002. As part of a broader effort to review dissemination practices, FINRA also seeks comment on the caps for TBA transactions that become effective on November 5, 2012.

Most firms have comprehensive policies and procedures for TRACE compliance, and regularly use TRACE data for pricing purposes, as well as for internal supervisory purposes. Providing transaction data showing the actual trade size may assist all market participants in determining the quality of their executions and member firms in complying with their best execution obligations. In addition, the dissemination of transaction data showing actual trade size may have a positive impact on the quality of pricing for valuation purposes.

The following tables show the percentage of transactions in TRACE-eligible securities reported to TRACE—excluding asset-backed securities—by total par value and trade count, that are effected at various sizes, and the impact of the \$5 million dissemination cap (for investment grade and agency debt securities) and \$1 million dissemination cap (for non-investment grade securities) on the percentage of par value and trades for which actual size is above the indicated cap level and therefore not displayed in disseminated data. The tables also show the impact of dissemination caps if set at alternative levels.<sup>7</sup>

INVESTMENT GRADE CORPORATE BONDS		NON-INVESTMENT GRADE CORPORATE BONDS		AGENCY DEBT SECURITIES	
Percentage of Par Value Traded Above Cap Level		Percentage of Par Value Traded Above Cap Level		Percentage of Par Value Traded Above Cap Level	
Cap Level	Percentage	Cap Level	Percentage	Cap Level	Percentage
\$1 million +	83.17%	\$1 million +	79.49%	\$1 million +	94.14%
\$5 million + <i>Current Level</i>	48.91%	<i>Current Level</i>		\$5 million + <i>Current Level</i>	77.20%
\$10 million +	30.49%	\$5 million +	36.39%	\$10 million +	66.01%
\$15 million +	22.99%	\$10 million +	23.03%	\$15 million +	60.07%
\$20 million +	17.84%	\$15 million +	18.39%	\$20 million +	54.99%
\$25 million +	14.10%	\$20 million +	15.22%	\$25 million +	47.42%
\$50 million +	7.23%	\$25 million +	12.89%	\$50 million +	31.50%
\$75 million +	5.19%	\$50 million +	8.06%	\$75 million +	26.93%
\$100 million +	3.90%	\$75 million +	6.59%	\$100 million +	20.36%
\$100 million +	3.90%	\$100 million +	5.49%		
Percentage of Trades Above Cap Level		Percentage of Trades Above Cap Level		Percentage of Trades Above Cap Level	
Cap Level	Percentage	Cap Level	Percentage	Cap Level	Percentage
\$1 million +	8.08%	\$1 million +	10.85%	\$1 million +	23.90%
\$5 million + <i>Current Level</i>	1.81%	<i>Current Level</i>		\$5 million + <i>Current Level</i>	8.34%
\$10 million +	0.64%	\$5 million +	1.43%	\$10 million +	4.65%
\$15 million +	0.35%	\$10 million +	0.46%	\$15 million +	3.40%
\$20 million +	0.21%	\$15 million +	0.26%	\$20 million +	2.64%
\$25 million +	0.13%	\$20 million +	0.16%	\$25 million +	1.76%
\$50 million +	0.03%	\$25 million +	0.11%	\$50 million +	0.63%
\$75 million +	0.02%	\$50 million +	0.03%	\$75 million +	0.43%
\$100 million +	0.0080%	\$75 million +	0.02%	\$100 million +	0.23%
		\$100 million +	0.0105%		

The following tables show the percentage of TBA transactions reported to TRACE, by total par value and trade count, that are effected at various sizes, and the impact the \$25 million dissemination cap (for TBA transactions eligible "for good delivery") and the \$10 million dissemination cap (for TBA transactions "not for good delivery") (based on historical transaction data) would have had on the percentage of par value traded and trades for which the actual size would not have been displayed (if such transactions had been disseminated during that period).<sup>8</sup> The tables also show the impact of dissemination caps if set at alternative levels.

<b>TBA GOOD DELIVERY</b>	
Percentage of Par Value Traded Above Cap Level	
Cap Level	Percentage
\$10 million +	92.40%
\$25 million + <i>Current Level</i>	84.17%
\$50 million +	74.20%
\$75 million +	69.37%
\$100 million +	57.70%
\$250 million +	33.82%
\$500 million +	17.40%
Percentage of Trades Above Cap Level	
Cap Level	Percentage
\$10 million +	32.79%
\$25 million + <i>Current Level</i>	20.13%
\$50 million +	12.45%
\$75 million +	10.04%
\$100 million +	6.19%
\$250 million +	1.87%
\$500 million +	0.51%

<b>TBA NOT GOOD DELIVERY</b>	
Percentage of Par Value Traded Above Cap Level	
Cap Level	Percentage
\$10 million + <i>Current Level</i>	84.53%
\$25 million +	54.71%
\$50 million +	23.52%
\$75 million +	15.50%
\$100 million +	10.11%
\$250 million +	2.68%
\$500 million +	0.00%
Percentage of Trades Above Cap Level	
Cap Level	Percentage
\$10 million + <i>Current Level</i>	41.47%
\$25 million +	15.98%
\$50 million +	3.80%
\$75 million +	1.80%
\$100 million +	0.90%
\$250 million +	0.12%
\$500 million +	0.00%

### Rule 144A Transactions

Securities Act Rule 144A is a safe harbor exemption from the registration requirements of Securities Act Section 5 for certain offers and sales of qualifying securities by certain persons other than the issuer of the securities. The exemption applies to the re-sale of securities to qualified institutional buyers (QIBs).<sup>9</sup> Rule 144A transactions have been subject to TRACE reporting requirements since TRACE inception. Unlike transactions in publicly traded bonds, Rule 144A transactions are not subject to dissemination because of the private nature of the transactions.<sup>10</sup> However, this approach results in limited or no price transparency in the market in Rule 144A TRACE-eligible securities. Without any disseminated data, it may be difficult for market participants to assess the quality of the executions of their orders and for firms to determine if they have complied with their best execution obligations. In addition, the lack of disseminated data in Rule 144A transactions may have an adverse impact on the accurate valuation of positions in such securities.

FINRA seeks comment on the current approach and whether Rule 144A transactions should be subject to dissemination. FINRA notes that Rule 144A transactions account for approximately 4 percent of trades and 18 percent of par value in corporate debt securities reported to TRACE. The table below summarizes the percentage of all TRACE corporate debt trades, all TRACE non-investment grade corporate debt trades and all TRACE investment grade corporate debt trades that are Rule 144A trades.<sup>11</sup>

	July 2011 Through June 2012
Rule 144A trades as a percentage of total TRACE corporate trades	4.37%
Rule 144A non-investment grade trades as a percentage of all TRACE non-investment grade trades	8.09%
Rule 144A investment grade trades as a percentage of all TRACE investment grade corporate trades	2.50%
Rule 144A par value traded as a percentage of total TRACE corporate par value traded	17.53%
Rule 144A non-investment grade par value traded as a percentage of all TRACE non-investment grade corporate par value traded	20.59%
Rule 144A investment grade par value traded as a percentage of all TRACE investment grade corporate par value traded	14.89%

If Rule 144A transactions were disseminated and dissemination caps were applied, the following tables show the percentages of Rule 144A transactions (and par value traded) that would be subject to various dissemination cap levels.

July 2011 Through June 2012	
INVESTMENT GRADE RULE 144A	
Percentage of Par Value Traded Above Cap Level	
Cap Level	Percentage
\$1 million +	94.02%
\$5 million +	64.30%
\$10 million +	47.22%
\$15 million +	39.48%
\$20 million +	33.58%
\$25 million +	28.40%
\$50 million +	18.01%
\$75 million +	14.70%
\$100 million +	12.48%
Percentage of Trades Above Cap Level	
Cap Level	Percentage
\$1 million +	50.68%
\$5 million +	13.28%
\$10 million +	5.52%
\$15 million +	3.38%
\$20 million +	2.23%
\$25 million +	1.44%
\$50 million +	0.42%
\$75 million +	0.23%
\$100 million +	0.15%

July 2011 Through June 2012	
NON-INVESTMENT GRADE RULE 144A	
Percentage of Par Value Traded Above Cap Level	
Cap Level	Percentage
\$1 million +	89.41%
\$5 million +	44.63%
\$10 million +	30.57%
\$15 million +	25.07%
\$20 million +	21.20%
\$25 million +	18.42%
\$50 million +	12.22%
\$75 million +	9.93%
\$100 million +	8.01%
Percentage of Trades Above Cap Level	
Cap Level	Percentage
\$1 million +	51.47%
\$5 million +	7.35%
\$10 million +	2.61%
\$15 million +	1.51%
\$20 million +	0.96%
\$25 million +	0.66%
\$50 million +	0.21%
\$75 million +	0.12%
\$100 million +	0.06%

## Request for Comment

FINRA welcomes all comments on the use of dissemination caps and the dissemination of Rule 144A transactions. FINRA also specifically requests comment on the issues identified below.

### Dissemination Caps for Investment Grade and Non-Investment Grade Debt Securities

1. What would be the impact of raising the dissemination caps for:
  - a. investment grade TRACE-eligible securities transactions to \$10 million, \$15 million, \$20 million or higher; and
  - b. non-investment grade TRACE-eligible securities transactions to \$5 million, \$10 million, \$20 million or higher?
2. Should FINRA set a dissemination cap applicable solely to agency debt securities in light of the larger size of many transactions in such securities?
  - a. If so, should it be set at \$25 million, \$50 million, \$100 million or higher?
3. Should there continue to be different dissemination caps for investment grade and non-investment grade debt securities?
4. Should the dissemination caps for investment grade and non-investment grade debt securities be eliminated entirely?
5. Would the information available as a result of higher dissemination caps allow broker-dealers and institutional investors to better value positions?
6. Could alternative ways of determining dissemination caps—for example, by dollar value<sup>12</sup> of transaction rather than par value—provide meaningful trade volume exposure while still limiting the transaction sizes displayed through the caps?

### Dissemination Caps for TBA Transactions

1. Should there be a dissemination cap for TBA transactions?
  - a. If yes, are the levels appropriate or should higher or lower caps be considered?

### Rule 144A Transactions

1. Should Rule 144A transactions—private re-sales of securities to QIBs—be subject to dissemination?
2. If yes, should Rule 144A transactions be subject to dissemination in the same manner as other disseminated transactions in TRACE-eligible securities?
  - a. If yes, should they be disseminated subject to a dissemination cap?
  - b. If yes, what is the appropriate size (volume) at which to set the dissemination cap?

- c. If yes, should FINRA distinguish between investment grade and non-investment grade securities, and set a higher dissemination cap for Rule 144A transactions in investment grade securities and a lower dissemination cap for Rule 144A transactions in non-investment grade securities?
3. Would dissemination of Rule 144A transaction information impact investment decisions and price negotiations, and, if yes, how?
4. If information on Rule 144A TRACE-eligible securities transactions should be disseminated, should the transaction information be disseminated publicly without limitation or on a more limited basis?

## Endnotes

1. 17 CFR 239.144A.
2. FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. See [Notice to Members 03-73](#) (November 2003) (NASD Announces Online Availability of Comments) for more information.
3. The term investment grade is defined in FINRA Rule 6710(h). In most cases, an agency debt security that is not rated is traded and priced as an investment grade security. Thus, for purposes of TRACE, in most cases, such securities are classified as investment grade debt and subject to the \$5MM+ dissemination cap. The term agency debt security is defined in FINRA Rule 6710(l).
4. The term non-investment grade is defined in FINRA Rule 6710(i). For purposes of TRACE, most unrated corporate bonds are considered non-investment grade debt and are subject to the \$1MM+ dissemination cap.
5. The terms agency pass-through mortgage-backed security and to be announced are defined in, respectively, FINRA Rule 6710(v) and FINRA Rule 6710(u). See Securities Exchange Act Release No. 66829 (April 18, 2012), 77 FR 24748 (April 25, 2012) (SEC Approval Order Relating to Post-Trade Transparency of Agency Pass-Through Mortgage-Backed Securities Traded TBA) (TBA Dissemination Approval Order); [Regulatory Notice 12-26](#) (May 2012) (announcing November 5, 2012, as the effective date for the dissemination of TBA transactions, dissemination caps for such TBA transactions, and related rule changes).
6. See FINRA Rule 6710(u) (as effective on November 5, 2012) for reference to the terms "for good delivery" and "not for good delivery." See also [Regulatory Notice 12-26](#) and TBA Dissemination Approval Order.
7. FINRA calculated the percentages based on the 12-month period from July 1, 2011, to June 30, 2012.
8. See *supra* note 5.

9. Qualified institutional buyer is defined in Securities Act Rule 144A(a)(1). 17 CFR 239.144A(a)(1).
10. See FINRA Rule 6750(b)(1).
11. FINRA calculated the percentages based on the 12-month period from July 1, 2011, to June 30, 2012.
12. For this discussion, the dollar value of the transaction means the par value multiplied by the execution price of the transaction.

EXHIBIT 2b

**Alphabetical List of Written Comments to Regulatory Notice 12-39 (September 2012) with respect to dissemination of transactions in TRACE-Eligible Securities effected pursuant to Securities Act Rule 144A**

1. Dorothy Donohue, The Investment Company Institute (November 12, 2012).
2. Mark Hepsworth, Interactive Data Corporation (November 19, 2012).
3. David A. Hodges, Integra Wealth, LLC (November 15, 2012).
4. Chris Killian, Securities Industry and Financial Markets Association (November 16, 2012).
5. Beth N. Lawson, The Nelson Law Firm, LLC (October 9, 2012).
6. Chris Melton, Coastal Securities (November 19, 2012).
7. Michael Nicholas, Bond Dealers of America (November 19, 2012).
8. Bill O'Neill, Income Research & Management (September 17, 2012).
9. Scott Oswald, Bristlecone Advisors, LLC (November 9, 2012).
10. Lyn Perlmuth, The Credit Roundtable (November 7, 2012).
11. E.A. Repetto, Dimensional Fund Advisors LP (November 6, 2012).
12. Jim Toffey, Benchmark Solutions, Inc. (October 4, 2012).



1401 H Street, NW, Washington, DC 20005-2148, USA  
202/326-5800 [www.ici.org](http://www.ici.org)

November 12, 2012

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: FINRA Request for Comment on Trade Reporting and Compliance Engine ("TRACE") (Regulatory Notice 12-39)

Dear Ms. Asquith:

The Investment Company Institute<sup>1</sup> is pleased to respond to the Financial Industry Regulatory Authority's ("FINRA") request for comment on issues related to the dissemination of information on securities transactions eligible for reporting on the Trade Reporting and Compliance Engine ("TRACE").<sup>2</sup> Registered investment companies ("funds") are significant investors in the fixed-income markets.<sup>3</sup> As such, funds and their shareholders benefit from fixed-income markets characterized by transparency and liquidity. Our letter reflects the views of a majority of ICI members as to the effect that the contemplated changes to the TRACE system will have on the functioning of the fixed-income markets at this time. These views are not representative of all ICI members, some of which take opposing views.

FINRA currently requires its members to report to TRACE all secondary transactions in certain fixed-income securities within fifteen minutes of the time of execution.<sup>4</sup> The transaction

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<sup>1</sup> The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$13.8 trillion and serve over 90 million shareholders.

<sup>2</sup> Regulatory Notice 12-39 (September 2012) ("Notice"), which is available at <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p163711.pdf>.

<sup>3</sup> At year-end 2011, investment companies held 15 percent of the total of United States and international corporate bonds. See 2012 Investment Company Fact Book, *A Review of Trends and Activity in the U.S. Investment Company Industry*, Investment Company Institute, at p. 12, which is available at [www.icifactbook.org](http://www.icifactbook.org).

<sup>4</sup> See FINRA Rule 6730.

Ms. Marcia Asquith  
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information for investment grade corporate debt securities and agency debt securities disseminated from TRACE includes the exact par value on all transactions with a par value of \$5 million (“\$5M”) or less and includes an indicator of “5MM+” in place of the exact par value on transactions where the par value is greater than \$5M.<sup>5</sup> With respect to non-investment grade TRACE-eligible securities, the exact par value on all transactions with a par value of \$1 million (“\$1M”) or less is disseminated and any transaction in excess of \$1M is disseminated as “1MM+.” (The \$1M and \$5M thresholds are referred to collectively in this letter as “dissemination caps.”)

TRACE was first established to increase transparency in the corporate debt market and dissemination caps were intended to respond to industry concerns about the potential negative impact that immediate dissemination of transaction data could have on liquidity.<sup>6</sup> The Notice explains that as part of FINRA’s periodic evaluation of current practices, it is seeking input on whether to modify, leave unchanged, or eliminate the \$5M investment grade and \$1M non-investment grade dissemination caps for corporate debt securities. The Notice also seeks comment on whether to modify the \$5M dissemination cap for agency debt securities and whether information regarding Rule 144A transactions should be disseminated in the same manner as publicly traded corporate debt securities.

**Corporate Debt Transactions.** The current \$1M and \$5M dissemination caps are considered round lot transaction amounts, and we believe, at this time, that these thresholds provide adequate transparency regarding transaction prices in the corporate debt market. At the same time, we are concerned that increasing or eliminating the current dissemination caps will negatively affect liquidity for corporate debt securities. Secondary market liquidity for investors in the fixed-income market, such as funds, is provided by dealers that are willing to risk their capital pending the location of customers who are willing to purchase a block of bonds. Revealing the exact par value of large trades (especially for certain infrequently traded issues) would allow other dealers to identify the dealer, including information about a dealer’s inventory and investors involved in the trade. This information could then be used to trade against the dealer’s position and reduce the incentive for a dealer to take large positions in these circumstances. This in turn could have unintended consequences for all market participants (retail and institutional) by impairing liquidity (*e.g.*, caused by the unwillingness of dealers to continue their active role in the fixed-income market).

We are particularly wary of modifying dissemination of TRACE information in ways that might negatively affect liquidity at this time given that liquidity in the corporate bond markets has declined since the financial crisis in 2008, and other pending regulatory changes have potentially negative, as yet unknown, implications for liquidity in the fixed-income market. In particular, we are concerned that the proposed rule to implement Section 619 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, commonly known as the Volcker Rule, could restrict banks from playing their

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<sup>5</sup> Disseminated TRACE transaction data includes, among other information, price, time of execution, and size.

<sup>6</sup> See SEC Release No. 34-42201 (December 3, 1999), which is available at <http://www.sec.gov/rules/sro/nd9965n.htm>.

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historic role as market makers buying and selling securities. If banks could not provide these services, particularly in the less liquid fixed income market, funds likely would face wider bid-ask spreads, higher transaction costs and diminished returns.<sup>7</sup> Similarly, the federal banking agencies have issued proposed rules that would substantially revise the capital framework for U.S. banking organizations. The proposals would, for example, remove the Accumulated Other Comprehensive Income (“AOCI”) filter from existing bank regulatory capital rules, which would result in short-term gains and losses on available-for-sale securities portfolios “flowing through” to banking organizations’ regulatory capital, thereby increasing capital volatility. In response, banking organizations may reduce their holdings of fixed-income securities, which would decrease overall market liquidity.<sup>8</sup> We therefore recommend that FINRA retain the current dissemination caps. We would not object, however, to FINRA again seeking comment on modifying the dissemination caps after the market implications of the regulatory changes discussed above are fully understood by market participants.

***Agency Debt Transactions.*** The Notice seeks comment on whether to modify the \$5M dissemination cap for agency debt securities. In response to the financial crisis, significant changes have occurred in the agency debt market that have resulted in diminished liquidity. For example, the Federal National Mortgage Association and Federal Home Loan Mortgage Corporation each have been required to reduce the size of its portfolio of mortgage loans. Reducing their debt outstanding has led to diminished liquidity in the market for agency debt securities. To avoid further reducing the liquidity in that market, we recommend leaving unchanged at this time the current dissemination cap of \$5M for agency debt securities. As with corporate debt transactions, we would not object to FINRA again seeking comment on modifying the dissemination cap for agency debt securities after some period of time has passed to allow market participants to better understand the long-term implications of the recent changes in the market.

***Rule 144A Transactions.*** Unlike transactions in publicly traded debt securities, Rule 144A transaction information currently is not disseminated.<sup>9</sup> Therefore, under the current approach, there is limited or no price transparency for Rule 144A transactions. The Notice seeks comment on whether

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<sup>7</sup> For a more detailed explanation of our concerns, *see* Letter from Paul Schott Stevens, President & CEO, Investment Company Institute, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission; Robert E. Feldman, Executive Secretary, Federal Deposit Insurance Corporation; Jennifer M. Johnson, Secretary, Board of Governors of the Federal Reserve; John G. Walsh, Acting Comptroller of the Currency, Office of the Comptroller of the Currency; and David A. Stawick, Secretary, Commodity Futures Trading Commission, dated February 13, 2012, which is available at <http://www.ici.org/pdf/25909.pdf>.

<sup>8</sup> *See* Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action, 77 Fed. Reg. 52,792 (Aug. 30, 2012); Regulatory Capital Rules: Standardized Approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements, 77 Fed. Reg. 52,888 (Aug. 30, 2012); and Regulatory Capital Rules: Advanced Approaches Risk-Based Capital Rule, Market Risk Capital Rule, 77 Fed. Reg. 52,978 (Aug. 30, 2012).

<sup>9</sup> *See* FINRA Rule 6750(b)(1).

Ms. Marcia Asquith  
November 12, 2012  
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information regarding Rule 144A transactions should be disseminated in the same manner as transactions in publicly traded corporate debt securities.

Funds are qualified institutional buyers that participate in the Rule 144A market. As with the publicly traded bond market, funds and their shareholders benefit from being able to participate in a Rule 144A market that is sufficiently transparent and liquid. The Rule 144A market has, over time, become a more mature and liquid market with no corresponding enhancement in its transparency. We therefore recommend that information regarding Rule 144A transactions be disseminated to the same extent as comparable non-Rule 144A transactions.<sup>10</sup>

\* \* \* \*

We look forward to working with FINRA as it continues to examine this issue. In the meantime, if you have any questions, please feel free to contact me at (202) 218-3563.

Sincerely,

/s/ Dorothy Donohue

Dorothy Donohue  
Deputy General Counsel—Securities Regulation

cc: Sharon Zackula, Associate Vice President and Associate General Counsel  
Office of General Counsel  
FINRA

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<sup>10</sup> In particular, we recommend that the transaction information for investment grade corporate debt securities and agency debt securities sold in Rule 144A transactions disseminated from TRACE include the exact par value on all transactions with a par value of \$5M or less and include an indicator of "5MM+" in place of the exact par value on transactions where the par value is greater than \$5M. With respect to non-investment grade corporate debt securities sold in Rule 144A transactions, we recommend that the exact par value on all transactions with a par value of \$1M or less be disseminated and an indicator of "1MM+" be used to describe any transaction in excess of \$1M.



November 19, 2012

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, N.W.  
Washington, D.C. 20006-1506

Dear Ms. Asquith:

Interactive Data is pleased to provide comments to FINRA's notice on TRACE dissemination issues. We continue to be strong supporters of FINRA's efforts to provide investors with greater transparency of the fixed income marketplace, particularly as it relates to the timeliness, depth, breadth and overall accessibility of fixed income trading information. We also recognize the importance of achieving transparency through prudent regulation that protects trading in the marketplace.

**Background on Interactive Data Corporation:**

Interactive Data Corporation is a trusted leader in financial information. Thousands of financial institutions, including many of the world's leading investment companies, subscribe to our fixed income evaluations, reference data, real-time market data, trading infrastructure services, fixed income analytics, desktop solutions and hosted, web-based solutions. The Company's Pricing and Reference Data business has established itself as a leading provider of evaluated pricing for 2.8 million fixed income securities, international equities and other hard-to-value instruments including OTC derivatives. These offerings are complemented by a comprehensive range of reference data for more than 10 million securities that encompasses listed markets pricing, identification information, corporate actions, and terms and conditions for current and historical fixed income securities. In recent years, we have invested considerable resources to provide our clients with solutions, such as our Vantage<sup>SM</sup> web application, that provide clients with greater insight and transparency into the fixed income markets and our evaluations. Related to these efforts, we continue to work collaboratively with FINRA to jointly support the FINRA-Interactive Data Structured Trading Aggregate Reports, which are designed to provide transparency into market activity related to U.S. structured securities on a daily basis.



**Interactive Data's Views on Issues Relating to the Dissemination of Information on TRACE-eligible securities transactions:**

Interactive Data subscribes to and utilizes FINRA's TRACE transaction data. This data provides us with important, timely insight into daily transaction activity, thereby serving as a valuable input into our evaluation methodologies and models along with other market color that we obtain from a broad range of sources. Many market participants also contend that the current dissemination caps help to support liquidity in what is generally regarded as an illiquid asset class (compared with equities) by preserving the anonymity of buyers and sellers, masking dealer inventories and reducing the potential for volatility following a very large trade of a particular security that is executed outside of recent trading patterns.

Nevertheless, we believe that the valuation activities of broker-dealers and institutional investors may benefit by raising the current dissemination caps. Given the concerns of market participants regarding liquidity risk, we believe it may be more prudent to take a measured approach to raising the current caps. Applying smaller, incremental increases for investment grade corporate bonds and agency debt securities, non-investment grade corporate bonds and To Be Announced (TBA) agency pass-through mortgage-backed securities) would further improve transparency while affording FINRA the flexibility to assess the impact of those changes. Based on its assessment, FINRA could then phase in additional increases to, or elimination of, dissemination caps, at some point in the future.

In addition, we believe that having different dissemination caps for different security types would be valuable based on the trading data presented by FINRA. We also generally support disseminating 144A transactions, distinguishing between 144A transactions in investment and non-investment grade securities. Related to this, we advocate for implementing dissemination caps for 144A transactions that are consistent with the broader dissemination caps for that specific security type.

**Summary**

Interactive Data appreciates the opportunity to comment on FINRA's notice on current TRACE dissemination caps and the dissemination of transactions in TRACE-eligible securities effected pursuant to Rule 144A under the Securities Act. Since the current caps already provide both direct and indirect benefits to the marketplace, we recognize that the benefits of increasing or eliminating current dissemination caps must be balanced against the potential risks to liquidity. Nevertheless, we believe that an incremental increase to the current caps could enhance the valuation practices of vendors and market participants while preserving the indirect benefits that the current caps afford.



# Interactive Data

In closing, we are generally supportive of regulatory initiatives aimed at improving both pre- and post-trade transparency in the fixed income markets as these activities can help strengthen the valuation process for vendors and all market participants. With that in mind, we would welcome consideration of additional transparency measures to further inform the fixed income marketplace, such as identifying "paired trades" that match dealer-client trades with equivalent inter-dealer trades typically executed at the same time and stratifying primary and secondary market trading for structured products.

We would be happy to meet with FINRA's staff to discuss our comments. We look forward to continuing to work with FINRA to promote transparency in the fixed income markets.

Sincerely,



Mark Hepsworth  
President, Pricing and Reference Data  
Interactive Data Corporation

Dear FINRA,

Please accept the following as my position of where I stand on the *Trade Reporting and Compliance Engine*:

I believe that the public dissemination of information regarding all trades, regardless of size or amount, would increase transparency and reduce costs for investors. I am of the opinion that FINRA should eliminate all dissemination caps and/or at least increase the current caps for post-trade data to further move toward a world of full transparency as it relates to transactions costs in the securities markets. I also recommend that information regarding Rule 144A transactions should be disseminated just as any other transactions for TRACE eligible securities. Thank you.

Sincerely,

**David A. Hodges, CFP®**  
Principal | INTEGRA WEALTH, LLC  
Ph: 423.664.0344 | Mobile: 423.827.3611  
871 McCallie Ave., Chattanooga, TN 37403  
[www.IntegraWealth.com](http://www.IntegraWealth.com)



November 16, 2012

Submitted Via Email to [pubcom@finra.org](mailto:pubcom@finra.org)

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street N.W.  
Washington D.C. 20006-1506

**Re: FINRA request for comments on TRACE Dissemination Issues**

Ladies and Gentlemen,

The Securities Industry and Financial Markets Association (“SIFMA”) is pleased to respond to FINRA’s request for comments on issues relating to the dissemination of TRACE-eligible securities transactions.<sup>1</sup> SIFMA’s comments on this proposal focus on the general question of whether current dissemination practices should be altered for investment grade and non-investment grade debt securities, Agency mortgage-backed securities traded on a to-be-announced (“TBA”) basis, and Rule 144A transactions.

***Summary of the Requests***

FINRA has requested comment on the general appropriateness of its current dissemination protocols for investment grade and non-investment grade debt securities, TBA transactions, and Rule 144A transactions. Regarding investment grade and non-investment grade debt securities, FINRA requests feedback on whether the TRACE dissemination volume caps should be raised from \$5mm and \$1mm. FINRA also seeks comment on the appropriateness of the soon to be implemented TBA dissemination caps. Finally, FINRA requests comments on whether Rule 144A transactions should be subject to dissemination.

***Summary of SIFMA Views***

- FINRA should not increase dissemination caps for investment grade TRACE-eligible securities or non-investment grade TRACE-eligible securities at this time. The steady reduction in market liquidity that has occurred over the last few years, which is expected to be amplified by market structure changes and recently implemented and proposed financial regulations, will be exacerbated by increases to dissemination caps.
- Since dissemination of TBA transaction data did not take effect until November 12, 2012, any recalibration of dissemination caps for TBA transactions should be postponed until the market impact is known.
- Public dissemination of Rule 144A transactions is not appropriate or necessary at this time.

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<sup>1</sup> See <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p126487.pdf>

## ***DISSEMINATION CAPS FOR INVESTMENT GRADE AND NON-INVESTMENT GRADE DEBT SECURITIES***

### ***Liquidity Concerns Remain***

SIFMA members do not believe now is the appropriate time to increase dissemination caps. Market dynamics do not appear to be necessitating any changes, liquidity has generally declined in recent years, and our members believe that an increase to dissemination caps would most likely further harm liquidity and large trade execution. Markets benefit from increased liquidity, and transparency initiatives should be developed with the intended effect of increasing liquidity (or, at least not harming it). As we have stated in past letters<sup>2</sup>, market participants, including investors, value the ability to keep their strategies and activities confidential for competitive and other reasons. Broad knowledge of specific sizes and timing of trades is therefore very sensitive information, as is the ability to reverse engineer net flows to or from customers or market makers. Our members believe that an increase to dissemination caps will make such specific knowledge more widespread by increasing the proportion of trades where exact sizes will be made public. This will decrease confidentiality of positions, strategies, and flows, and lead to a decrease in market activity and liquidity instead of an increase.

### ***Ultimately, Issuers will be Negatively Impacted by Diminished Liquidity***

Issuers face the ultimate risk from decreases to market liquidity since the public dissemination of trade information, as a general matter, makes broker-dealers less willing to take risk on large size trades. A reduction in liquidity will cause institutional investors to demand greater yield from issuers (to compensate for the reduced liquidity), or to simply refuse to buy new issues in meaningful size. Therefore, a careful balance between transparency and the preservation of liquidity must be struck. Data shows that dealers have recently chosen to (or been forced to, in the case of rules like the Volcker Rule) put capital to work elsewhere. This means that institutional investors will face greater difficulty selling a larger sized amount of an issue. Pre-TRACE, and pre-financial crisis, dealers provided a much larger outlet where they would take the risk temporarily while they worked to uncover a buyer. This outlet has been much reduced in recent years, due to a combination of regulation and other market structure issues. The real liquidity differential for larger vs. smaller “on the run” amounts has been meaningfully amplified, and eliminating caps on disseminated volumes would exacerbate this problem. At a much more specific level, it is more difficult to issue securities in smaller sizes when participant’s transactions are immediately made public and expose exact amounts taken down by particular investors. An increase in the dissemination caps will increase the threshold where these securities issuances are somewhat more challenging, and disproportionately harm smaller issuers. In each case, the macro and the granular, the result is a higher cost of capital for issuers.

### ***Regulatory Reform is Expected to Significantly Impair Liquidity***

When the current dissemination caps were instituted ten years ago, financial markets and the world economy were very different than they are today. Importantly, due to reforms instituted during and after the financial crisis, trading is more capital intensive than ever before. Several factors have impacted market liquidity, including but not limited to: Basel 2.5 and Basel III, which will significantly impact capital requirements for various asset classes and trading activities; the Volcker Rule, which has

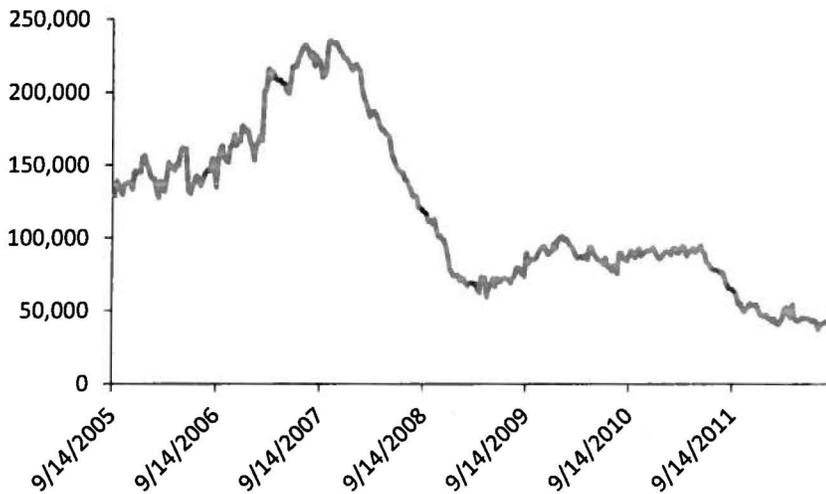
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<sup>2</sup> See, e.g., SIFMA’s May 10, 2012 letter on FINRA’s proposal to implement dissemination for MBS specified pools, here: <http://www.sifma.org/issues/item.aspx?id=8589938683>; SIFMA’s December 22, 2011 comment letter on FINRA’s proposal to implement dissemination for Agency MBS securities traded TBA, here: <http://www.sifma.org/issues/item.aspx?id=8589938683>

and will continue to reduce proprietary trading by banking entities as a source of liquidity in the markets (and in our view, due to the overbroad nature of the proposal, reduce liquidity far beyond what was intended due to the elimination of activity beyond true proprietary trading); and the consolidation of many large financial market participants (i.e., reductions in the number of large market makers). Each of these factors serves to reduce liquidity on its own; when combined, it is likely they will have an impact that is greater than the sum of their parts. In any case, granular economic analysis of the impact of these rules has not been performed, and rules have not been issued in final form and implemented such that markets have any experience with them. SIFMA does not believe it is appropriate to implement yet another significant change, on top of all of the others, without a better idea of combined impact of all of these regulatory initiatives.

An increase to TRACE dissemination caps coupled with these impediments to liquidity provision would serve to further decrease the ease of transacting in fixed-income markets, at a time when it has already significantly decreased. For example, dealer inventories have significantly decreased from their levels in 2007, and remain in steady decline, as shown below. Anecdotal evidence from our members supports the data. The ability and willingness of dealers to hold securities in inventory, that is, to take on the risk of price movements in securities to facilitate customer activity, is clearly reduced. While one may argue that dealer inventories have simply returned to the levels present in the early 2000s, and therefore all we have seen is a wringing out of the excesses of the crisis, we believe this argument omits one key factor. Financial markets have significantly grown in size over the last decade, and when dealer inventories are viewed proportionally to the size of the markets they serve, they are far smaller now than in the past. As a general matter, we believe that further decreasing the confidentiality of dealer and investor activities will only serve to further decrease the incentive to hold inventory and support market liquidity.

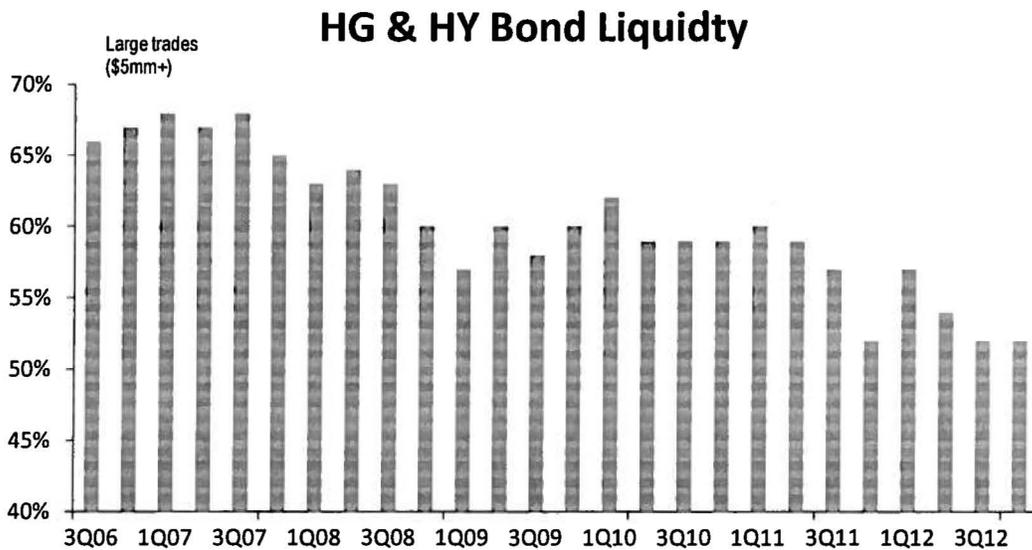
### Dealer Inventories



Source: Bloomberg

***Trade Sizes have been Decreasing, Execution is More Challenging, and Raising the Volume Caps will Enhance that Trend***

Another indicator of market liquidity is the ease with which market participants are able to execute large trades of blocks of securities. In an examination of TRACE data, it is clear that the trend for larger trades is following that of dealer inventories. Larger trades (defined as \$5mm+) in corporate markets have been steadily decreasing since 2007, as shown in the chart below. The steady decrease is the product of the regulatory and liquidity concerns highlighted above. Our members believe this downward trend will be amplified with an increase to dissemination caps. If these volumes were increasing or at least steady, one could make an argument to increase caps, but the data shows that the opposite trend is in progress - and we view this as a signal for the continued need for consistency and stability in rule making initiatives.



Source: TRACE

***DISSEMINATION CAPS FOR TBA TRANSACTIONS***

***Impact Analysis Needed before any Changes to Agency MBS TBA Dissemination Protocols***

SIFMA provided feedback on FINRA’s proposal to implement dissemination for Agency MBS traded TBA in 2011, and was generally supportive of the final rules. Given that dissemination of TBA transactions took effect on November 12, 2012, there has been no market experience with the initial dissemination regime. We believe it is premature to discuss amendments to that regime until we better know the impact of the proposed regime on the markets. Discussion of the appropriateness of and possible changes to TBA dissemination should be delayed until the market impact of the initially proposed dissemination is known.

**144A TRANSACTIONS**

***Changes to the TRACE Regime are not Warranted at this Time***

While the 144A market shares some similarities with that of publicly-issued debt, we believe that its unique characteristics merit its separate treatment by FINRA. As a threshold matter, the 144A market is a private market. Buyers in this market must meet certain thresholds, known as Qualified Institutional Buyer (QIB) standards, and the market is not open to typical individual investors. Offering documents are not publicly available on a system like the SEC's Edgar, and in many cases are locked behind password protected websites if they are even posted on the internet at all. Offering and other documentation is often only provided to holders of securities, and is not available to the general public.<sup>3</sup> What all of this means for TRACE is that data disseminated on 144A transactions is not relevant to purchasers of public offerings, as those involved in public transactions may or may not be QIBs, may or may not have access to essential offering documents and disclosure documents, and may end up confused by, or draw incorrect conclusions from, the irrelevant data. On the other hand, the potential market-based downsides are the same as we see in public markets – potential for liquidity disruptions. Here we also incorporate by reference our previously discussed concerns around changes in market liquidity and the impact of many regulatory changes – those concerns are identical in 144a markets.

In the end, the cost-benefit calculation is weighted differently than it is in public markets, and FINRA has correctly designed TRACE with regulatory reporting and dissemination for public transactions, and regulatory reporting for 144A. We do not believe that FINRA should implement dissemination for trades of 144A securities.

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SIFMA appreciates the opportunity to comment and hopes our comments are helpful and we would be pleased to discuss any questions or comments with this submission. Please contact Chris Killian at 212-313-1126 or [ckillian@sifma.org](mailto:ckillian@sifma.org) with any questions or comments.

Sincerely,



Chris Killian  
Managing Director

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<sup>3</sup> We recognize that the JOBS Act reduced the general solicitation restrictions on 144A and other private offerings of securities. We note, however, that just because these restrictions have been reduced does not imply that securities issuers will necessarily begin to make offering documents publicly available. Indeed we do not think this will happen on any large scale. We also note that the SEC, in the case of asset-backed securities, has proposed to align some of the disclosure requirements of 144A and public transactions. This proposal has not been finalized, in any case would *not* require posting of such disclosure on Edgar (aside from a public notice of the offering containing summary data).

**About Sifma**

SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit [www.sifma.org](http://www.sifma.org).

THE NELSON LAW FIRM, LLC

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October 9, 2012

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Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, N.W.  
Washington, DC 20006-1506

**Subject: Comments on Regulatory Notice 12-39 (TRACE Dissemination Issues)**

Ladies and Gentlemen,

On behalf of our clients—value-oriented broker-dealers, investment advisers and investors—The Nelson Law Firm, LLC respectfully submits these comments on the proposal of the Financial Industry Regulatory Authority, Inc. (“FINRA”) to eliminate or modify the dissemination caps on TRACE volume information, as described in the above-referenced Regulatory Notice (the “Proposal”). We have, on several other occasions, made public comment on this issue,<sup>1</sup> and we are grateful to have to opportunity to comment on this issue again.

We strongly support FINRA’s proposal to eliminate the dissemination caps. We believe that all dissemination caps, regardless of type of security, should be eliminated, because any limitation on the dissemination of trade information is an impediment to a competitive, free and open market. We would support an increase in the level of the dissemination caps, as we believe that any increase in the quantity and quality of transaction information that is disseminated would be a step in the right direction. However, unless FINRA eliminates all dissemination caps, this effort will fall short of creating the complete transparency that is essential to efficient competition among broker-dealers and the proper functioning of our

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<sup>1</sup> See Comments of The Nelson Law Firm (i) dated March 31, 2009, relating to File No. SR-FINRA-2009-004, (ii) dated May 5, 2009 relating to File No. SR-FINRA-2009-010, (iii) dated November 13, 2009 relating to SEC Release No. 34-60726, File No. SR-FINRA-2009-010, and (iv) dated November 13, 2009 relating to File No. SR-FINRA-2009-010.

securities markets. We do not believe that there is any valid reason for withholding volume information from public dissemination on trades of any size.

We also strongly support FINRA's proposal to disseminate Rule 144A transaction data. We believe that the dissemination of Rule 144A transaction trade data would be a desired enhancement to TRACE. There are many instances when registered bonds trade alongside Rule 144A bonds and full real-time dissemination of trade data for each of these types of securities is essential to price discovery and would provide market participants the tools to make more informed and better investment decisions.

### **Elimination of Dissemination Caps is the Next Logical Development for Bond Markets**

FINRA and the Securities and Exchange Commission ("SEC") have long acknowledged the benefits to the investing public from the dissemination of real-time trade and volume data during market hours. For example, in 1992, in its comments to the proposed penny stock rules, FINRA's predecessor (NASD) stated that the "dissemination of real-time trade and volume data during market hours will significantly benefit investors by providing the same high degree of market visibility and more efficient price discovery . . ."<sup>2</sup> In 1997, in the context of trading foreign equity securities, the SEC stressed the value of real-time dissemination of market data when it noted that dissemination of trade reports has the potential "to better enable investors to monitor the executions they receive in foreign securities."<sup>3</sup>

TRACE was introduced in 2002 in order to "increase price transparency in the U.S. corporate debt market." Since that time, FINRA and the SEC have made several enhancements to the system in order to promote market transparency and competition, including the following:

- The TRACE dissemination protocols were expanded to publicly disseminate the buy/sell and dealer/customer data elements. This improvement enhanced "market transparency by allowing TRACE users to better understand what a reported price actually represents." (SEC Release 34-58115, Jul. 7, 2008)
- The scope of securities subject to reporting and dissemination through TRACE was expanded to include non-registered and Rule 144A transactions. (SEC Release 34-59768, Apr. 14, 2009)
- TRACE was expanded to include agency debt securities and primary market transactions, because "[t]he expansion of TRACE will create consolidated post-trade transparency in Agency Debt Securities, and the dissemination of transaction information will assist in price discovery and valuation processes for all market

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<sup>2</sup> SEC Release No. 34-30608 (Apr. 20, 1992).

<sup>3</sup> SEC Release No. 34-38456 (Mar. 31, 1997).

participants and provide retail investors access to price information current not readily available to non-professionals.” (SEC Release 34-60726, Sept. 28, 2009)

- Asset-backed, mortgage-backed and similar securities were made subject to TRACE reporting (SEC Release 34-61566, Feb. 22, 2010) and dissemination (but still subject to dissemination caps) (SEC Release No. 34-66829, SR-2012-020, Apr. 18, 2012; see also proposal to disseminate additional information, SEC Release 34-67798, SR-2012-042, Sept. 7, 2012).

FINRA’s protocol of capping dissemination of volume information (which was never instituted through the formal rulemaking process) runs contrary to the general trend in rulemaking to enhance transparency in debt and equity reporting and dissemination. The elimination of the dissemination cap protocol would be a logical and essential next step.

### **Dissemination Caps Inhibit a Free and Open Market in Debt Securities**

Section 15A(b)(6) of the Securities Exchange Act of 1934 requires, among other things, that FINRA rules must be designed to “remove impediments to and perfect the mechanism of a free and open market.” Competition is an essential component of a free and open market in securities. In turn, the wide dissemination of information about securities prices and transactions costs is necessary for the creation and maintenance of free, open and competitive markets.

The SEC and FINRA have long followed this guiding principle in designing a system of regulation to ensure that securities markets are transparent and competitive. Regulation should require accurate and complete information be made available to the public. This information places competitors on an equal footing, resulting in a free and open market, and thereby ensuring that resources are properly allocated to their most valued use.

Dissemination caps are an impediment to free and open markets. Without the benefit of complete information about trades, investors are unable to accurately gauge the quality of executions received from bond dealers and end up paying higher execution costs than competitive markets would allow.

FINRA’s rules have long required most TRACE-eligible securities to be disseminated pursuant to FINRA Rule 6750.<sup>4</sup> Nonetheless, the TRACE system has, since 2002, followed

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<sup>4</sup> FINRA Rule 6750 on Dissemination of Transaction Information provides that “FINRA will disseminate information on all transactions in TRACE-eligible securities immediately upon receipt of the transaction report, except as provided below.” The only information that is currently not required to be disseminated is (i) information on a transaction effected pursuant to Rule 144A under the Securities Act, (ii) transfers of certain proprietary positions effected in connection with broker-dealer mergers or consolidations, (iii) List or Fixed Offering Price Transactions or Takedown Transactions, or (iv) information relating to transactions in Asset-Backed Securities.

an internal protocol<sup>5</sup> of implementing dissemination caps. For investment grade TRACE-eligible debt transactions with a par value above \$5,000,000, the disseminated volume is capped at \$5,000,000, and for non-investment grade debt transactions with a par value greater than \$1,000,000, the disseminated volume is capped at \$1,000,000. Agency debt securities have a dissemination cap of \$5,000,000, agency pass-through mortgage-backed securities traded to be announced (“TBA transactions”) (for good delivery) are capped at \$25,000,000, and TBA transactions (not for good delivery) are capped at \$10,000,000.

The dissemination protocol is inconsistent with the terms of FINRA’s Rule 6750 and the regulatory goals of TRACE. For TRACE to perfect the mechanism of a free and open market in debt securities, protect investors and enhance competition, FINRA must abandon this protocol in its entirety and disseminate all trade data information for all reported trades to the public. Otherwise, TRACE data, and particularly TRACE data relating to non-investment grade debt transactions, will continue to be of limited utility to many investors and there will continue to be an unnecessarily flawed market in debt securities.

One particularly egregious flaw in the current dissemination cap protocol turns cap limits on their heads. Investment grade debt, which generally trades consistently at or around par, and for which there is little price difference regardless of volume levels, is capped by FINRA at \$5,000,000. However, non-investment grade debt, which frequently trades at deep discounts to par, and for which prices can vary significantly at different volume levels, is capped by FINRA at \$1,000,000. The protocol would make more sense if the size of these caps were reversed.

Nonetheless, the primary problem is that dissemination caps withhold vital information regarding trades from the investing public, which inhibits competition. Our clients manage large portfolios, frequently trade in debt, and often purchase non-investment grade bonds that trade at significant deep discounts to par. Real-time information relating to the exact number of bonds traded is vital to the interpretation of trade data and trade execution costs. Our clients have a duty to evaluate the quality of their executions, and they generally use TRACE reports to make a best execution determination. Orders will flow to bond dealers providing better executions at lower costs, as suggested by the TRACE data. Thus, it is essential for investment managers to have complete transparency in trade information in order to properly evaluate whether they have received best execution with respect to any debt transaction in which they are participants, and to determine whether orders should be directed to market participants that provide better executions at lower costs.

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<sup>5</sup> This protocol was never proposed or approved as a FINRA rule through the formal rulemaking process. The protocol was previously disclosed only in FINRA’s TRACE User Guides and mentioned in certain recent rule proposals (SEC Release No. 34-66829, SR-2012-020, Apr. 18, 2012, and SEC Release 34-67798, SR-2012-042, Sept. 7, 2012). Currently, the protocol does not appear to be disclosed in any publicly-available TRACE manuals.

For example, suppose that two institutional investors have each submitted an order to different broker-dealers to purchase 50,000 non-investment grade bonds. The first investor receives an execution for 2,000 non-investment grade bonds at ½ of par. The TRACE report submitted to FINRA would show a par value of \$2,000,000 and a purchase price of ½ of par. However, due to the dissemination caps, the public report would show the par value to be \$1,000,000+ with a purchase price of ½ of par. Now suppose that the second investor in a contemporaneous transaction receives an execution for 50,000 of the same bonds at ½ of par, thereby receiving a complete fill on its order. The TRACE report submitted to FINRA would show a par value of \$50,000,000 and a purchase price of ½ of par, but the public report would again show a par value of \$1,000,000+ with a purchase price of ½ of par. The public dissemination appears to show that each investor purchased the same number of bonds, since both transactions report the same par value, \$1,000,000+, but in fact the second investor received twenty-five times as many bonds.

Clearly, the investor in the second example, all other things being equal, received a much better execution than the first investor. The first investor is subject to market risk on the remainder of its order and the order may never be filled at a reasonable price. But, nothing in the TRACE report disseminated to the public would alert the first investor to the fact that the second investor's broker did a much better job of filling its order than her broker did. In a free and open market, the first investor would know this information and would be able to immediately complain of this execution failure to the firm that made the trade on her behalf. If that complaint failed to produce a satisfying result, the investor would likely shift her business to the other firm.

Eliminating the dissemination caps will enable sophisticated investors to compare, in real-time, the executions received by different broker-dealers. In the securities industry as well as other industries, consumers (investors) seek the best execution of their orders. Disclosure allows customers to understand how they are being treated, and if they are repeatedly allocated inferior executions, will take their business elsewhere. Competition forces suppliers to provide better service at lower prices. A higher-priced market participant providing inferior service that wishes to retain its business will be forced to improve service and lower its rates. Enhanced competition in the bond market will result in better executions for customers and a narrowing of the differences in execution rates and prices as investors seek the best executions available. By removing the dissemination caps, the bond market will become more competitive, execution prices will be driven to fair prices by customer choice, best execution obligations will be satisfied and capital will end up being allocated to its most efficient use.<sup>6</sup>

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<sup>6</sup> It is important to note that FINRA and the SEC are required to consider the effect on competition of every rule or rule change that it proposes. See the SEC's Current Guidance on Economic Analysis in SEC Rulemaking (Mar. 16, 2012) ("Rulemaking Guidance"). In the Rulemaking Guidance, the SEC reiterated that it is required "to consider the impact that any rule promulgated under [the Exchange] Act would have on competition and to include in the rule's statement of basis and purpose 'the reasons for the Commission's...determination that any burden on competition imposed by such rule or regulation is necessary or appropriate in furtherance of the purposes of [the Exchange Act.]'" See Rulemaking Guidance,

**The Lack of Liquidity Argument in Favor of Dissemination Caps Is Not Valid**

We believe that FINRA instituted this protocol of withholding volume information from the investing public not because of any systems limitations or technical reasons, but because FINRA-member firms participating in the debt market resisted the complete dissemination of trade information that was required under Rule 6750 in order to avoid competitive pressure. The affected broker-dealers claimed (and will likely continue to claim) that dissemination would impair debt market liquidity.

We do not believe the lack of liquidity argument is valid. Bond investors are the source of liquidity in the bond markets, not broker-dealers, who are the source of transactions costs. Broker-dealers arguing for dissemination caps essentially are saying that they cannot be profitable in a competitive market.

We reject the concept of roadblocks to competition in almost every sphere of life; why should we give it validity in the securities markets? Competition inspires innovation, as competitors seek to find lower cost methods to deliver services. We are all richer as a result. Roadblocks to competition discourage innovation and impoverish us. The proponents of dissemination caps confuse their own interests with the public interest and the inability to compete with a lack of liquidity.

It has been argued that the original intent of the dissemination caps was to protect a broker-dealer's capital commitment. This is simply another expression of the fear that some broker-dealers would not survive in a more competitive market. There is no valid reason to continue the practice of protecting bond dealers from competition. History informs us that efforts to protect some industry sub-group from competition are doomed to failure. While anti-competitive practices continue, the investing public is made to suffer. It is time to remove the dissemination caps and allow the cleansing power of the market to sweep away firms than are unable or unwilling to compete.

This is not the first time that investors have heard complaints from the industry that transparency would hurt liquidity. In the early 1990's, broker-dealers in equity markets resisted similar disclosures. But time has proven such claims to be false, even for thinly-traded securities. The dissemination of information about equity transactions resulted in astounding systems competition and extremely low transactions costs; yet markets, if anything, are more liquid than ever. Experience has taught us that transparency and competition benefit investors and improve markets. Regulatory roadblocks to competition hinder capital formation and the free flow of invested capital.

We do not believe there is any valid justification (statutory or otherwise) for the imposition of the TRACE dissemination caps. The SEC and FINRA exist to protect the investor and perfect the mechanism of free and open market, not broker-dealer profits. It is contrary to the public interest to keep the public in the dark regarding the actual quantities of bonds traded.

Moreover, there is no justification for the disparate treatment provided to different grades of corporate bonds (or to other types of debt securities) with respect to these dissemination caps. Since there is more fluctuation in prices in the non-investment grade bond market, dissemination caps permit uncompetitive bond dealers to provide poorer executions, resulting in higher uncompetitive mark-ups if trade information is kept from the public eye.

### **Rule Enforcement is a Poor Alternative to Competition**

Faced with the competitive pressure resulting from full dissemination, bond dealers would be forced to provide better service and maintain competitive prices. Furnishing a trade report to FINRA so that FINRA may observe patterns of trading and otherwise conduct surveillance of the market at levels above the dissemination cap is not sufficient to protect the investing public. FINRA cannot cause orders to be sent to bond dealers providing the best executions. The information contained on the trade report, regardless of the size of the trade, and regardless of the percentage of trades affected, must also be disseminated so that the investing public can monitor the behavior of their brokers and direct orders to those brokers who best represent their interests. We submit that competitive pressures are much more effective than enforcement procedures when it comes to ensuring best execution. We strongly believe that the failure to disseminate complete volume information on debt transactions is detrimental to the investing public and the marketplace for debt securities. This failure to disseminate provides large bond dealers an unfair advantage over the smaller investor and the marketplace in general. Removal of the dissemination caps would expose very valuable information and would put investors in a position to know who is charging the best price. The transparency that would be provided by complete dissemination of trade information would greatly enhance the ability of investors to monitor the debt markets, and the resulting competitive marketplace would lead to more precise valuations, better pricing, and reduced investor costs. As investors gravitate towards the dealers providing the best executions, all other bond dealers will be forced to reduce their prices or improve their service to compete. The transparency provided by removal of the dissemination caps will inspire innovation, level the playing field among broker-dealers with respect to executions, and enhance best execution practices in the industry.

We respectfully request that the FINRA eliminate its policy of capping the trade volume information that is disseminated in its TRACE system, for all debt securities. The dissemination caps are inconsistent with FINRA Rule 6750 and impede free and open markets in debt securities. Dissemination will not create any additional burden on FINRA members from a reporting standpoint, as this information is already being reported to

FINRA. Accordingly, FINRA should amend its protocol and disseminate complete volume information on debt transactions (including 144A transactions) to the investing public.

We greatly appreciate the opportunity to comment. I can be reached at (914) 220-1919 or via email at [bnlowson@nelsonlf.com](mailto:bnlowson@nelsonlf.com) if you have any questions.

Respectfully submitted,

A handwritten signature in black ink, reading "Beth N. Lawson". The signature is written in a cursive, flowing style.

Beth N. Lawson

Thank you for providing me with the opportunity to comment on the proposed expansion of TRACE reporting dissemination to include 144A issues and an increase in the volume cap for reported trades on other TRACE issues. I begin by stating the obvious. No market can be truly "transparent" when only FINRA members are required to report transactions and bank dealers are free to conduct business in TRACE eligible securities free from the obligation to report. It seems that bowing at the altar of "transparency" only appeals to regulators when non-bank dealers are to be proscribed. The current proposal to expand trade size reporting will only tilt the playing field further and may actually achieve the tipping point where bank affiliated member firms begin shifting their business in TRACE eligible securities to their bank affiliates. The unintended result would be less, rather than more, transparency. If the regulators are truly interested in a transparent market, rather than the appearance thereof, they should beware of the law of unintended consequences as it may pertain to this expansion of TRACE reporting.

I do not know the affect that reporting of 144A issue transactions will have on the market; however, by definition it can have no effect on any client that is not a Qualified Institutional Buyer. These are supposedly private securities transactions trading in a very limited market. Public dissemination may result in a hue and cry for expanded availability of the product for clients that do not have the sophistication to properly evaluate the investments without the protection of Securities Act registration. It could be argued that is unlikely; however, the little that is to be gained by disseminating 144A trade information surely cannot outweigh the potential Pandora's Box that may be opened by "publicizing" a private market.

Sincerely,

Chris Melton  
Executive Vice President  
Coastal Securities



21 Dupont Circle, NW • Suite 750  
Washington, DC 20036  
202.204.7900  
www.bdamerica.org

November 19, 2012

VIA ELECTRONIC MAIL (send to: pubcom@finra.org)

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, N.W.  
Washington, D.C. 20006-1506

RE: FINRA Requests Comment on TRACE Dissemination Issues  
(Regulatory Notice 12-39)

Dear Ms. Asquith:

The Bond Dealers of America (BDA) is pleased to submit this letter in response to Regulatory Notice 12-39, the Financial Industry Regulatory Authority (FINRA)'s request for comment on TRACE Dissemination Issues. The BDA is the only DC based group representing the interests of securities dealers and banks focused on the U.S. fixed income markets and we welcome this opportunity to state our position.

The BDA is pleased to supply comment on two issues relating to the dissemination of information on TRACE-eligible securities transactions and we will address each one separately.

*First, FINRA seeks input on whether it should maintain or modify current TRACE dissemination caps, under which the actual size (volume) of a transaction over a certain par value is not displayed in disseminated realtime TRACE transaction data:*

The BDA believes that FINRA should not increase the \$1 million and \$5 million TRACE volume dissemination caps, which have been in place since TRACE began operating on July 1, 2002. The BDA fully supports the use of the TRACE system as a mechanism for greater transparency in the marketplace, and especially as it relates to the retail investor, who is often examining for valuable pricing information. But we do not believe that raising dissemination caps above the current caps of the \$1 million and \$5 million thresholds will provide any additional protections to the retail investor and will potentially harm institutional investors. By the very fact that the trades would need to be in excess of the current caps in order to benefit retail investors and given the fact that very few retail investors trade securities at these par amounts, we believe that it is highly unlikely that increasing these caps will meaningfully benefit retail investors. In contrast, we believe that institutional investors will be meaningfully harmed.

As we have stated before in previous comments letters to FINRA and the SEC, institutional investors take their anonymity very seriously. Any research done internally, by and for themselves, is less beneficial if opportunistic investors are afforded the information they need to take advantage of this valuable research by reverse engineering their trading activity. As the potential for their internal research to be pilfered by others increases, so does the likelihood that this will suppress their trading activity. Worse, the capacity for these opportunistic investors to pilfer valuable research may discourage investors from conducting this kind of research at all and may lead them to abstain from investing in securities that they will only invest in with such research. This, we believe, could materially suppress liquidity in markets that need as much liquidity as they can get. Therefore, we believe that FINRA should not raise these dissemination caps.

Second, FINRA requests comment on whether transactions in TRACE-eligible securities effected pursuant to Securities Act Rule 144A1 (Rule 144A transactions) should be disseminated, and if so, the scope and manner of such dissemination:

The BDA believes the current approach for Rule 144A transactions should remain unchanged and that Rule 144A transactions should not subject to dissemination.

Rule 144A transactions are inherently private transactions in nature and are traded almost exclusively among institutions. FINRA even points out in its Notice, that Rule 144A safe harbor exemption from registration applies only to the re-sale of securities to qualified institutional buyers (QIBs), a very small section of the market in these transactions. These institutions are capable of assessing and negotiating for the kind of information they need to make their investment decisions. It is neither an area that invites nor needs this kind of regulation. Therefore, we do not support the potential dissemination of Rule 144A transactions.

We thank you for this opportunity to submit these comments.

Sincerely,



Michael Nicholas  
CEO  
Bond Dealers of America



## CELEBRATING 25 YEARS

Income Research & Management (“IR+M”) is a fixed income asset management firm with approximately \$34 billion in assets under management as of August 31<sup>st</sup>, 2012. IR+M manages portfolios on behalf of individual and institutional investors including private and public pension plans, insurance entities, healthcare providers, universities, foundations, and corporations and has been an active participant in the U.S. credit markets since its inception in 1987.

We are writing in response to FINRA’s request for comment on TRACE dissemination issues. Comments are as follows:

### **Dissemination Caps for Investment Grade and Non-Investment Grade Debt Securities**

1. What would be the impact of raising the dissemination caps for:
  - a. investment grade TRACE-eligible securities transactions to \$10 million, \$15 million, \$20 million or higher; and
  - b. non-investment grade TRACE-eligible securities transactions to \$5 million, \$10 million, \$20 million or higher?

*A \$5-\$10 million cap increase for investment grade securities would allow for better overall market volume reporting as well as increase transparency into the pricing of standard large blocks (~\$10 million). Similarly, a cap increase for non-investment grade to \$5 million would allow for a more sufficient analysis of the market relative to the current \$1 million cap.*

2. Should FINRA set a dissemination cap applicable solely to agency debt securities in light of the larger size of many transactions in such securities?
  - a. If so, should it be set at \$25 million, \$50 million, \$100 million or higher?

*Yes - \$50 million*

3. Should there continue to be different dissemination caps for investment grade and non-investment grade debt securities?

*Yes*

4. Should the dissemination caps for investment grade and non-investment grade debt securities be eliminated entirely?

*No – An elimination of dissemination caps would likely result in less capital committed by broker/dealers as trading margins would likely fall.*

5. Would the information available as a result of higher dissemination caps allow broker/dealers and institutional investors to better value positions?

*Yes, marginally*

6. Could alternative ways of determining dissemination caps—for example, by dollar value of transaction rather than par value—provide meaningful trade volume exposure while still limiting the transaction sizes displayed through the caps?

*More information is preferable to less though there is likely diminishing marginal utility as stated in the response to point #4.*

### **Dissemination Caps for TBA Transactions**

1. Should there be a dissemination cap for TBA transactions?

a. If yes, are the levels appropriate or should higher or lower caps be considered?

*Yes - \$250 million. A \$250 million cap would cover ~70% of the market which is consistent with our desires expressed above.*

**Rule 144A Transactions**

1. Should Rule 144A transactions—private re-sales of securities to QIBs—be subject to dissemination?

*Yes*

2. If yes, should Rule 144A transactions be subject to dissemination in the same manner as other disseminated transactions in TRACE-eligible securities?

a. If yes, should they be disseminated subject to a dissemination cap?

b. If yes, what is the appropriate size (volume) at which to set the dissemination cap?

*Would prefer that dissemination mirrored that of comparable non 144A securities.*

**Bill O'Neill, CFA**

Sr. Portfolio Manager

INCOME RESEARCH + MANAGEMENT

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CELEBRATING 25 YEARS

I support increasing the reporting caps on bond trades reported to TRACE. This would increase transparency, information flow, and potentially reduce costs to investors.

In reading the comment papers posted to the website, I'd agree with the suggestions made by Income Research & Management's letter dated September 17, 2012.

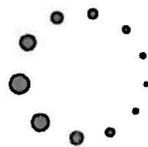
Regards,  
Scott Oswald

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Scott Oswald, CFA, CAIA  
Senior Associate, Research  
Bristlecone Advisors, LLC

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 **The Credit Roundtable**  
In association with the Fixed Income Forum

November 7, 2012

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 12-39 on TRACE Dissemination Issues

Dear Ms. Asquith:

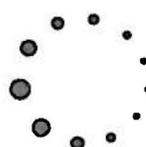
The Credit Roundtable welcomes the opportunity to comment on FINRA's two proposals, first to potentially modify current TRACE dissemination caps, and second, to potentially disseminate information on transactions involving Rule 144A transactions. Formed in 2007, The Credit Roundtable, organized in association with the Fixed Income Forum, is a group of large institutional fixed income managers including investment advisors, insurance companies, pension funds, and mutual fund firms, responsible for investing more than \$3.8 trillion of assets. The Credit Roundtable seeks to enhance investment grade bondholder protection and was formed in response to events such as leveraged buyouts, leveraged recapitalizations and other corporate actions that adversely affected the credit quality and valuations of a significant number of existing investment grade bond issues. Its mission includes education, outreach, and advocacy. It hopes to benefit all bond market participants through increased transparency and improved market efficiency and liquidity.

In order to evaluate making any changes in the corporate bond trade information disseminated by TRACE, it is first important to understand the current nature of trading in the corporate bond market. The attached graphs chart the state of liquidity and trading in the investment grade corporate bond market over approximately the last decade. Graph 1 shows that the overall size of the investment grade corporate bond market has grown substantially, particularly in the years following the financial crisis as many corporations issued debt to extend the maturity of their liabilities and take advantage of the lower interest rate environment. Contrast that with how primary dealers (security dealers who can deal directly with the Federal Reserve, and who do the vast majority of trading in corporate bonds) have changed their holdings of corporate bonds available for facilitating customer transactions. As Graph 2 points out, their absolute dollar value grew steadily through 2007 and then plummeted back down to levels last seen in 2002. This decline is even more striking when one looks at the drop of dealer positions relative to the large increase in the corporate bond market, as Graph 3 does. The amount of dealer positions on a relative basis to the size of the market is only approximately one-sixth of its peak in 2007.

Let's turn to another perspective on the market, trading. Graph 4 shows that trading volumes have grown somewhat since 2005; however, when adjusted on a relative basis to the large growth in the size of the overall market, they have dropped. In particular, as Graph 6 indicates, it

**Institutional Investor**

225 Park Avenue South, 7th Floor, New York, NY 10003, Tel: (212) 224-3074, Fax: (212) 224-3838



# The Credit Roundtable

In association with the Fixed Income Forum

now takes about 335 business days for the investment grade corporate market to turn over, a substantial increase from approximately 200 business days back in 2005. It is also important to realize that this drop in liquidity occurred before the formal imposition of the Volcker Rule, which in its current proposed formulation could have a substantial negative impact on bond market liquidity.

## TRACE Investment Grade and Non-investment Grade Dissemination Cap Proposal

In order to analyze if it is appropriate to change TRACE dissemination caps, it is important to understand how the bond market works. Bonds trade very differently than stocks. Investors do not trade directly with each other in the vast majority of cases; they use bank dealers as intermediaries. In addition, outside of U. S. Treasuries and mortgage-backed securities, most corporate bonds trade infrequently. For example, Ford Motor Company and Ford Motor Credit have more than 30 issues whose size are \$100 million par value or larger. If, hypothetically, a portfolio manager needs to meet investor redemptions and decides to sell a specific Ford bond, it is unlikely that there will be a buyer at that immediate point in time that needs that exact combination of issuer, maturity, and coupon. Such a trade will often require the dealer to hold the bond on its balance sheet for some period of time before it finds a buyer. Any analysis to change the caps must look at whether a potential increase in price transparency will be bought at a decrease in liquidity. The current caps for investment grade corporate bonds of \$5 million and non-investment grade bonds of \$1 million are considered “round lot” transaction amounts and provide good information about transaction prices. Against a backdrop of substantially decreased liquidity as discussed earlier, it is our view that increased size transparency of trades accomplished by raising the dissemination caps will make the dealer community even more reluctant to position bonds on their balance sheet, particularly those issued by smaller companies. We, therefore, recommend that there be no change to the dissemination caps for investment grade and non-investment grade TRACE-eligible securities.

## Rule 144A Securities Dissemination Proposal

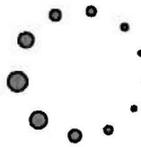
Over time, as the Rule 144A market has matured, the size and liquidity of the securities have grown substantially. In many cases, their trading rivals public registered securities. We therefore agree with the proposal to disseminate information on transactions in Rule 144A securities. The TRACE dissemination caps should be exactly the same as for publicly registered investment grade and non-investment grade corporate securities.

## U. S. Government Agency Dissemination Proposal

As a direct result of the financial crisis, there have been structural changes in the government agency debt market that resulted in less liquidity. As Graph 7 indicates, the amount of debt outstanding from the three largest government agencies has declined sharply over the last several years. In the case of the Federal National Mortgage Association (FNMA) and the Federal Home Loan Mortgage Corporation (FHLMC), their regulator has mandated that they reduce the size of the mortgage portfolio that they hold on their own balance sheets. With regards to the Federal

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 **The Credit Roundtable**  
In association with the Fixed Income Forum

Home Loan Banks (FHLB), their advances (loans) to their constituent members have decreased as their members have increased their holdings of time and demand deposits. This decline in debt outstandings due to a decrease in new issuance has brought with it a fall off in liquidity in trading of these securities. For these reasons, we would recommend not changing the dissemination cap for these instruments.

The Credit Roundtable looks forward to working with FINRA on this issue. If you have any questions, please contact me at 212-224-3074 or [lperlmut@iimemberships.com](mailto:lperlmut@iimemberships.com).

Sincerely,



Lyn Perlmuth  
Director, Fixed Income Forum  
On Behalf of the Credit Roundtable

**Institutional Investor**

225 Park Avenue South, 7th Floor, New York, NY 10003, Tel: (212) 224-3074, Fax: (212) 224-3838



Eduardo Repetto  
Chief Executive Officer  
Chief Investment Officer

November 6, 2012

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

**Re: FINRA Request for Comment on Trade Reporting and Compliance Engine  
("TRACE") (FINRA Notice 12-39)**

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Dear Ms. Asquith:

Dimensional Fund Advisors LP ("Dimensional") appreciates the opportunity to provide the Financial Industry Regulatory Authority ("FINRA") with our views on the TRACE dissemination issues discussed in Regulatory Notice 12-39.<sup>1</sup> As a registered investment adviser that provides investment management services to mutual funds, institutional and financial adviser clients, Dimensional is in full support of efforts to provide and improve post-trade transparency to market participants.

At the time TRACE was created, FINRA implemented a phase-in approach that limited public dissemination of TRACE information to certain types of fixed income securities. In addition, TRACE-eligible securities were subject to specified dissemination caps, under which the actual size of a transaction over a certain par value is not included in disseminated TRACE data. This approach was largely in response to concerns that transparency could cause reduced liquidity in the marketplace. Now that TRACE has been in operation for some time, FINRA is seeking input on: (i) whether it should maintain or modify current TRACE dissemination caps and (ii) whether transactions in TRACE-eligible securities effected pursuant to Securities Act Rule 144A ("Rule 144A Transactions") should be disseminated.

**Increased transparency benefits investors**

Since the introduction of TRACE, there have been measurable benefits to investors, primarily in the form of lower transaction costs due to increased transparency. There are multiple studies of the impact of increased transparency in the corporate bond market. Despite the use of different methodologies and samples, the consistent finding across these studies is that

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<sup>1</sup> FINRA Regulatory Notice 12-39 (September 2012) ("Notice"), available online at: <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p163711.pdf>.



the introduction of TRACE was associated with a decline in trading costs.<sup>2</sup> Armed with more information, investors have an enhanced ability to negotiate terms for bond trades. We also believe that increased transparency inherently boosts investor confidence in the market.

The impact of increased transparency has been particularly striking on more actively traded bonds. Importantly, these studies have had considerable success in separating causation from correlation; the evidence indicates that increased transparency resulted in *subsequent* decreases in trading costs. Edwards, Harris and Piwowar, report that transparency decreases customer transaction costs by roughly five basis points.<sup>3</sup> Similarly, Bessembinder et. al. indicate an approximately 50% reduction in trade execution costs for bonds eligible for TRACE transaction reporting.<sup>4</sup> Given these observations, we believe that increased transparency would be to the benefit of our clients and all investors in the corporate debt market.

Separately, a reduction in trading costs will also reduce borrowing costs for issuers. Such reductions may entice more borrowers to the marketplace and could further enhance the bond market.

#### **No observed adverse liquidity impact**

When FINRA first proposed the introduction of TRACE, many commenters expressed concern that the immediate dissemination of bond transaction data could have a potential adverse impact on liquidity.<sup>5</sup> However, the previously cited research shows no negative impact on liquidity from TRACE eligible securities. Quite the contrary, these studies show substantial reductions in trading costs. Even the most conservative estimates in Goldstein and Sirri (2006) indicate that increased transparency has either a neutral or a positive effect on market liquidity, depending on the trade size.<sup>6</sup>

It is possible, however, that commenters may again raise the concern that eliminating or increasing the level of dissemination caps could adversely impact market liquidity. In particular, we are aware that some industry members are concerned that if dissemination caps are removed then dealer inventory could be identified in a way that could be used against dealers. The argument they make is that dealers could become disincentivized from providing liquidity. It is important to recognize that the disseminated data under TRACE does not reveal which dealer

<sup>2</sup> See Michael A. Goldstein et. al. *Transparency and Liquidity: A Controlled Experiment on Corporate Bonds*, Oxford University Press (2006); Amy K. Edwards et. al. *Corporate Bond Market Transaction Costs and Transparency*, *The Journal of Finance* (June 2007); and Hendrik Bessembinder et. al. *Market Transparency, liquidity externalities, and institutional trading costs in corporate bonds*, *Journal of Financial Economics* (2006).

<sup>3</sup> See Edwards (2007).

<sup>4</sup> See Bessembinder (2006); it was also observed that trade execution costs for bonds not eligible for TRACE reporting also decreased by approximately 20% since the introduction of TRACE, which implied a liquidity externality where better pricing information reduced execution costs for related bonds.

<sup>5</sup> See Edwards (2007), at p. 1422, stating that the trade association for bond dealers, the Bond Market Association, had concerns that transparency will hurt liquidity; see also "Corporate Bond Market Transparency and Debt Mark-Up Regulation," Morgan, Lewis & Bockius LLP (2002), stating that over half of the commenters on the TRACE proposal in 1999 expressed concern over possible adverse effect on liquidity.

<sup>6</sup> See Goldstein (2006).



participated in a transaction, just that a dealer was involved. Based on that information alone, it is not clear that the inventory of any specific dealer could be gleaned from the TRACE data. Furthermore, because dealers can pass inventory between them and have those recorded as inter-dealer trades, it would be difficult for market participants to reverse engineer dealer inventory based on the data disseminated via TRACE. It is for these reasons that we believe this argument to be flawed.

**Response to FINRA requests for comment**

We wanted to respond to the two principal issues that FINRA was seeking comment on: (i) whether it should maintain or modify current TRACE dissemination caps and (ii) whether transactions in TRACE-eligible securities effected via Rule 144A Transactions should be disseminated.

First, based on the evidence that TRACE data has been beneficial to investors, we support the elimination of dissemination caps. If FINRA decides to maintain dissemination caps, however, then we would support increasing the caps since any increase in the amount of post-trade data available to market participants would be, in our view, in the best interests of investors. An incremental increase in the dissemination caps<sup>7</sup> may be a reasonable middle ground approach that takes into consideration the clear benefits of increased transparency along with any other commenters' concerns regarding a potential reduction in liquidity. Such an approach would allow time for additional studies on the effect of the incremental increases in the caps to address concerns regarding liquidity and would also appear consistent with the approach taken thus far in implementing TRACE in phases.

Second, on the question of Rule 144A Transactions, we believe that information regarding Rule 144A transactions should be disseminated just as other transactions for TRACE-eligible securities. For the same reasons, investors such as our clients that participate in Rule 144A transactions would benefit from increased transparency.

We appreciate FINRA's efforts in continuing to examine these issues and are grateful for this opportunity to provide our comments.

Sincerely,

A handwritten signature in black ink, appearing to read 'E. A. Repetto', written over a horizontal line.

E. A. Repetto

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<sup>7</sup> For example, increasing the par value cap level from \$5 million to \$10 million for short and intermediate-term investment grade bonds and agency debt securities and increasing the par value cap level from \$1 million to \$5 million for short and intermediate-term non-investment grade corporate bonds. We also believe that the par value cap levels should be set higher for long-term bonds across all categories.



October 4, 2012

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, N.W.  
Washington, D.C. 20006-1506

**Re: FINRA Notice 12-39: FINRA Requests Comment on TRACE Dissemination Issues**

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Dear Ms. Asquith:

Benchmark Solutions<sup>1</sup> appreciates this opportunity to respond to Regulatory Notice 12-39<sup>2</sup> (the "Notice") issued by the Financial Industry Regulatory Association ("FINRA") in which FINRA is seeking comment on two TRACE dissemination issues. The first, on whether it should maintain or modify current TRACE dissemination caps, under which the actual size (volume) of a transaction over a certain par value is not displayed in disseminated real-time TRACE transaction data. And second, on whether transactions in TRACE eligible securities effected pursuant to Securities Act Rule 144A should be disseminated, and if so, the scope and manner of such dissemination.

**Feedback Loop:**

In general, Benchmark Solutions is fully supportive of regulatory efforts to provide full post-trade transparency to all market participants in the timeliest and most complete manner possible. We believe that there is a strong feedback loop where post-trade information is a valuable input to determining pre-trade price discovery. Therefore, any delay in either reporting (timeliness) or transparency (data) inhibits the ability of the market to provide pre-trade price discovery which may ultimately affect market liquidity.

**Size assists in determining market impact:**

Full disclosure of trade size will help market participants make more informed trading and risk management decisions. In most asset classes, trading activity is a closely watched indicator of market sentiment. Heavy buying or selling activity helps investors interpret news reports and other forms of market research and commentary. Based upon the information currently available through TRACE, it is not possible to accurately assess the level of intraday activity in specific bonds.

FINRA publishes lists of the 10 Most Active investment grade and high yield issues on its investor website, with a one-day lag. Attempts to replicate this list using the information reported on the TRACE feed are fruitless. For example, on 9/18/12, the Sun America 5.6's '97 was the 5<sup>th</sup> most active investment grade issue according to FINRA. The TRACE feed that day reported a single trade with a capped amount of \$5MM+. The same day, the Citigroup 1.875's of Oct'12 was the 9<sup>th</sup>

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<sup>1</sup> Benchmark Solutions is a privately owned corporation focused on providing real-time price transparency in the Fixed Income Markets.

<sup>2</sup> FINRA Regulatory Notice 12-39 Issued September 2012.

most active bond but traded only 3 times, with just 1 capped volume trade report. Any most active list produced solely from the publicly available information provided by FINRA would never include either of these issues.

The absence of fully disclosed trade sizes also complicates the adoption of important management tools, such as Transaction Cost Analysis, in the corporate bond sector. Any attempt to compare one's trades to trades of similar size suffers from the same inability to accurately assess activity levels. Therefore, full disclosure of the actual trade size at a time nearest to the true execution time should be the norm for reporting. Valid arguments should be made as to why timely and complete reporting is not made to the investing public.

**FINRA Specific Request for Comment:**

Dissemination Caps for Investment Grade and Non-Investment Grade Debt Securities

1. What would be the impact of raising the dissemination caps for:

a. investment grade TRACE-eligible securities transactions to \$10 million, \$15 million, \$20 million or higher; and

b. non-investment grade TRACE-eligible securities transactions to \$5 million, \$10 million, \$20 million or higher?

**Benchmark Solutions Response: In general, we feel that there should not be dissemination caps for either investment grade or non-investment grade securities and that all trades should be reported and disseminated within seconds after execution.**

2. Should FINRA set a dissemination cap applicable solely to agency debt securities in light of the larger size of many transactions in such securities?

**Benchmark Solutions Response: As stated above we feel that it is best for the market participants to have full visibility to market transactions. Therefore, there should not be a cap for agency securities.**

a. If so, should it be set at \$25 million, \$50 million, \$100 million or higher?

3. Should there continue to be different dissemination caps for investment grade and non-investment grade debt securities?

**Benchmark Solutions Response: We firmly believe that there should not be any dissemination caps. Based on the information provided from FINRA we do not believe there is a material difference between how investment grade and non-investment grade trade or as to their bond structures to warrant caps in general or unique caps specifically. If FINRA feels that caps are in the best interest marketplace then we would ask FINRA to consider consistent caps and a much shorter embargo timeframe.**

4. Should the dissemination caps for investment grade and non-investment grade debt securities be eliminated entirely?

**Benchmark Solutions Response: Yes, based on our response to question 3.**

5. Would the information available as a result of higher dissemination caps allow broker dealers and institutional investors to better value positions?

**Benchmark Solutions Response: We firmly believe this to be the case. Additionally, many Institutional Investors utilize TRACE data as an input in performing Transaction Cost Analysis. Delayed reporting of trades along with capped volumes inhibits their ability to perform an accurate analysis.**

6. Could alternative ways of determining dissemination caps—for example, by dollar value of transaction rather than par value—provide meaningful trade volume exposure while still limiting the transaction sizes displayed through the caps?

**Benchmark Solutions Response: We're generally not in favor of this particular idea.**

#### Dissemination Caps for TBA Transactions

1. Should there be a dissemination cap for TBA transactions?

**Benchmark Solutions Response: No. The TBA market is an OTC version of a futures market. The futures market doesn't have any caps associated with its trade reporting and dissemination.**

- a. If yes, are the levels appropriate or should higher or lower caps be considered?

#### Rule 144A Transactions

1. Should Rule 144A transactions—private re-sales of securities to QIBs—be subject to dissemination?

**Benchmark Solutions Response: Yes.**

If yes, should Rule 144A transactions be subject to dissemination in the same manner as other disseminated transactions in TRACE-eligible securities?

**Benchmark Solutions Response: In the case of 144A securities, while their market size is smaller than the overall Trace disseminated market the amount traded is significant(17.53%) even though the actual number of trades is relatively low (4.37%). Given the materiality of the volume associated with this market we feel that trades in these instruments should be disseminated to the marketplace in the same manner and timeframe as their registered security counterparts.**

- a. If yes, should they be disseminated subject to a dissemination cap?
  - b. If yes, what is the appropriate size (volume) at which to set the dissemination cap?

#### **Areas of Improvement to Existing TRACE Data:**

Although we were not specifically asked to comment on areas of improvement we'd like to take this opportunity to do so.

1. **Time of Execution-** We suggest that FINRA consider redefining the time of execution (FINRA Rule 6710 (d)) to reflect the time at which investment risk is transferred between the parties in the transaction. Prices reported on the TRACE feed provide an estimate of an asset's value at a moment in time. The current rule allows trade participants to agree on the "spread" at which a transaction will be valued but defer the setting of the transaction yield until some later time,

which is then reported as the execution time. As a result, consumers of the TRACE feed are unable to reconcile the value represented by prices derived for spread-based transactions with the market conditions that existed at the time the value judgment was made. Without this improvement, there will always be transactions that appear to be off-market.

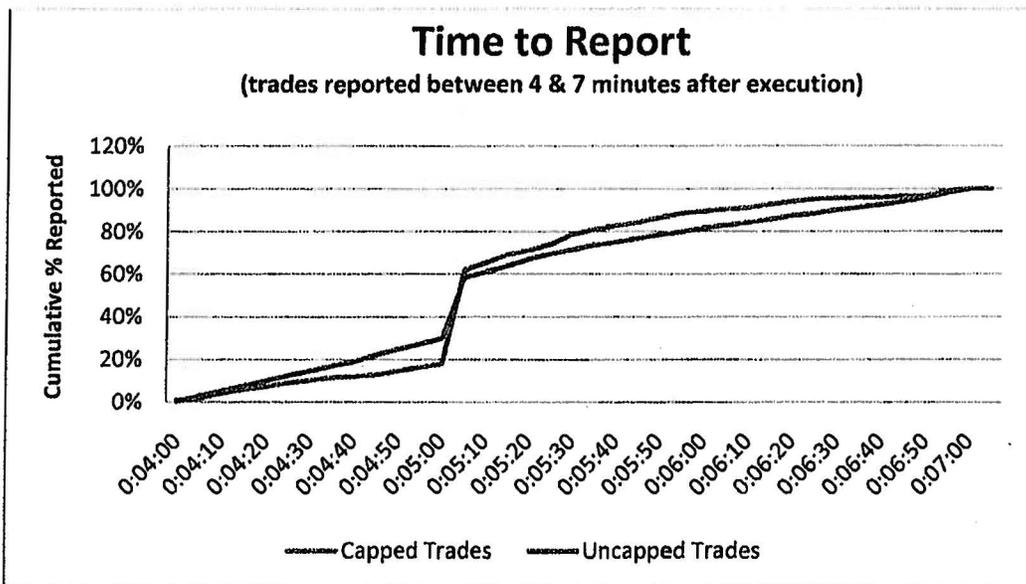
2. **Identification of trades done via electronic trading platforms**- We'd like to suggest that there be, at a minimum, an identifier letting the public know whether the transaction occurred via an electronic platform such as ECNs or an ATS.
3. **Earlier opening to the TRACE feed** – TRACE system hours are currently set as 8:00AM through 6:29:59PM, Eastern Time. During August 2012, 2% of the corporate bond transactions had reported execution times outside the TRACE system hours. 1.5% of the corporate bond transactions occurred between 6AM and 8AM, with 80% of these transactions occurring after 7am. We ask that FINRA consider extending the TRACE reporting and dissemination services by changing the opening time to 6:00 AM. This move will improve the transparency of trades occurring in overnight sessions and allow these trades to inform the setting of opening levels in the market.
4. **Foreign, non-FINRA member, Broker Dealers** – These trades look like customer trades which is misleading to the market. The reporting party, a US registered Broker Dealer, should identify these transactions as Broker Dealer or create a new category such as unregulated foreign dealer rather than Customer.
5. **Enhance the classification of Investment Grade versus High Yield debt** – To the extent that different volume caps continue to exist based upon credit quality, Benchmark urges FINRA to minimize the anomalies that are allowed to leak into the market. It appears that many bonds are initially designated as High Yield when they are first added to the FINRA Issue Master file due to the lack of assigned credit ratings. After several days, many of these issues are upgraded to investment grade, once ratings are formally published. During the first few days after issuance, which are often quite active, the disseminated trade sizes are capped at 1MM.

For example, on 9/18/2012 Novartis Capital came to market with a 2-tranche deal totaling \$2B, split between 10 & 30 year maturities. These issues were added to the issue master file on that day as high yield/unrated bonds. There were 52 reported trades in the 10-yr issue on the 18<sup>th</sup>. 29 of these trades had size capped at \$1MM. On the 19<sup>th</sup>, another 98 trades were reported, with 45 showing a capped trade size of \$1MM. The issue master records were updated as of the 20<sup>th</sup> to investment grade, after Aa2/AA- ratings were assigned by Moody's and S&P. As of September 20<sup>th</sup>, the capped volume limit rose to \$5MM+.

FINRA Rule 6710(h) states, "If a TRACE-Eligible Security is unrated, for purposes of TRACE, FINRA may classify the TRACE-Eligible Security as an Investment Grade security." Benchmark urges FINRA to utilize its authority under Rule 6710(h) and designate unrated new issues as investment grade when similar bonds from the issuer are already in the market carrying investment grade ratings, as is the case for the Novartis bonds in the example. If non-investment grade ratings are assigned later, the designation can be modified.

6. **Timeliness of Trade reporting** – Through the information available on the TRACE feed, we have observed that a disproportionate number of trades seem to be reported at precisely 5 minutes after trade execution. The chart below focuses on trades reported on 9/18/12 that came in 4 to 7 minutes after execution (similar patterns are observable on other days). Over 25% of the trades were reported exactly 5 minutes after execution. For trades with capped volumes, 44% of the trades in this interval and 5% of all trades were reported at 5 minutes. This seems to be counter to the spirit of reporting as soon as technologically feasible.

Additionally, we recently analyzed trades reported from May 2012 through August 2012. This analysis identified that 94% of the trades were reported to FINRA in less than 5 minutes. Of these trades the average reporting time was less than a minute while the median reporting time was less than a half a minute. Therefore, given the current reporting technology environment it seems feasible to both report and disseminate trades in less than one minute.



7. **Enhance its policies and processes to report data which was not previously reported due to reference data errors.** Over the past year, we have seen scenarios where a bond was originally designated for dissemination on the TRACE feed and then erroneously reclassified as a 144a, which given the existing dissemination rules, made the bonds ineligible for inclusion on the data feed. Once the reference data was corrected, there was no process to release the omitted transactions to the marketplace. While administrative issues are unavoidable, procedures need to be adopted to ensure that the all eligible transactions are reported to the market.

**Recent Regulatory Reporting Improvements in Other OTC Markets:**

On August 24, 2012, the Municipal Securities Rulemaking Board("the MSRB") filed amendments with the SEC to enhance price transparency for large trades.<sup>3</sup> The amendment proposes to enhance the Real-Time unmasking of trades greater than \$1 million to \$5 million with full

<sup>3</sup> MSRB Notice 2012-29(June 1, 2012)

disclosure on the real-size 5 business days later. From our perspective the Municipal Market is more opaque than the corporate market given that it has over 50,000 issuers and over 1.2 million unique instruments.

Should FINRA determine that capped trade sizes are in the markets best interest, then we'd like to see FINRA consider making the full trade size available within a similar timeframe rather than the current 18 – 21 month embargo which exists today.

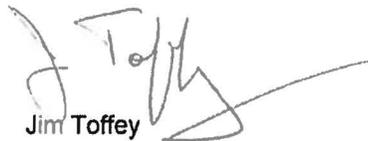
**Ease of Implementation:**

As far as implementation of our proposal for Actual Trade reporting is concerned, since the actual trade size is currently captured through BTDS there should not be any business process changes to market participants or direct technology implementation costs to them. As far as our suggestions for improvement to the existing TRACE reporting service are concerned they require potential changes to either FINRA or Market Participants, but in our estimate are not overly burdensome in nature and would greatly enhance the value of post-trade reporting data to market participants and investors alike.

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We wish to thank FINRA and its staff for their work in developing this Request for Comment and for this opportunity to comment on it. We would be pleased to discuss these comments in greater detail to help facilitate your review. If you have any questions, please do not hesitate to contact the undersigned at (212) 220-4740.

Sincerely yours,



Jim Toffey  
CEO  
Benchmark Solutions, Inc.