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August 15, 2005

Mr. Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

Re: File No. S7-06-05; Relating to New York Stock Exchange's Request for Exemption from Section 12(a) for Certain Debt Securities

Dear Mr. Katz:

The Bond Market Association ("Association")¹ appreciates this opportunity to comment to the Securities and Exchange Commission (the "SEC" or "Commission") on the request by the New York Stock Exchange ("NYSE") for exemptive relief from Section 12(a) of the Securities Exchange Act of 1934 (the "Exchange Act") to allow NYSE members to trade certain "unlisted" debt securities on the NYSE's Automated Bond System ("ABS"). If granted, NYSE members would be able to trade debt securities of certain issuers (generally reporting companies that have equity securities listed on the NYSE) even though the debt was not itself listed and did not comply with the registration requirement under Section 12(a) of the Exchange Act. As part of this initiative, the NYSE also filed a proposed rule change setting forth certain requirements for debt securities traded on the ABS.²

In its application for exemptive relief, the NYSE expressed optimism that the ABS trading system has the potential to provide greater bond market transparency and liquidity. The Association has long supported transparency in the bond markets so long as there is no negative effect on liquidity. We believe the NYSE initiative could potentially increase efficiency and competitiveness in the retail bond market and odd-lot

¹ The Association represents securities firms and banks that underwrite, trade and sell debt securities, both domestically and internationally. The Association's Member firms collectively represent in excess of 95% of the initial distribution and secondary market trading of municipal bonds, corporate bonds, mortgage and other asset-backed securities and other fixed income securities. More information about the Association is available on its website www.bondmarkets.com.

² Release No. 34-51999; File No. SR-NYSE-2004-69.

corporate debt securities (although not necessarily in the institutional market)³ and that the Commission should allow the initiative to proceed. However, the Association does have a variety of technical and policy concerns and questions, some of which should be addressed before the Commission grants exemptive relief and others of which may require further study after any such relief is granted.

I. Exchange as a “Broker”

As a starting matter, we observe that the NYSE is essentially asking exemptive relief from the SEC to allow the NYSE to act as a broker, rather than as an exchange. That is, the NYSE is requesting permission to act as an intermediary in securities that have not been listed either on the NYSE or on another exchange. Assuming that the NYSE’s request for relief is granted, the NYSE will, in effect, be competing with other brokers that also offer trading in the debt securities that will be traded on the NYSE, some of which brokers also offer trading in the same securities through electronic systems.

While the Association does not object to the NYSE acting as a broker, we are concerned that the fact that the NYSE will do so through its status as a “self-regulatory organization” (“SRO”), rather than as a broker in over-the-counter securities, will create some disruption to the existing regulatory scheme and also that this disparity in regulatory treatment has the potential to give the NYSE a variety of competitive advantages over the brokers with which it will be competing. The issues that we raise below in this letter are primarily intended to address the differential regulatory status of the NYSE vis-à-vis its competitors.

II. Trade Reporting and Trade Data

1. Integration of Trade Reporting

Currently, most of the corporate securities transactions that the NYSE intends to provide trade services for must be reported to the National Association of Securities Dealers (“NASD”) Trade Reporting and Compliance Engine System (“TRACE”). Users of TRACE pay the NASD a fee to access data reported on TRACE. The TRACE

³ The Association strongly believes in the strength and efficiency of the over-the-counter market. *See, e.g., Bond Market 2000* (October 1998)(“ Decentralized over-the-counter bond markets are critically important competitive alternatives to centralized auction markets because they provide flexibility to market participants, serve investors’ needs and facilitate innovation ... [and] offer market participants the execution flexibility to individually tailor the trading terms to suit a particular purpose, whether the terms relate to size, settlement, or any other special features deemed important by the parties to the trade”).

reporting requirement does not by its terms apply to debt securities that are “listed” on a national securities exchange and reported to the exchange.⁴

Thus, read literally, the TRACE reporting requirements would continue to apply to securities traded on ABS since ABS securities would not be “listed,” although we do not believe this is a result that the Commission or the NYSE intend. The Association is concerned that the trading of unlisted debt securities on the NYSE’s ABS would impose additional reporting requirements on member firms for trades on ABS. Given the transparency of the ABS, we believe that trades of unlisted debt securities effected on ABS should not be required to be reported to TRACE by broker-dealers. We urge the Commission to amend the TRACE Rule to clarify that trading of unlisted securities through the ABS does not need to be reported to TRACE.

Alternatively, if it is desirable to integrate TRACE and ABS data, the Association believes that the NYSE should be responsible for the reporting of ABS trades to TRACE, or vice versa, so that broker-dealers would not be subject to additional onerous manual reporting requirements, or have to bear any additional expense in retro-fitting existing system to accommodate dual reporting.

In any case, the Association believes that it would be helpful if the trading symbols used by the ABS were the same as those used by TRACE, especially if ABS becomes more widely used. This would be especially helpful for the retail sector of the market. The Association believes that other operational issues may arise in expanding the scope of tradable securities on ABS and would be happy to actively participate in an advisory committee should the NYSE choose to establish one to address such issues.

2. Ownership of the Trade Data should be Clarified

An issue that is closely related to trade reporting is the ownership of quote and trade data. The Commission has generally taken the view that SROs own certain of the quotation and trading data that is directly or indirectly generated by member firms. In fact, the SROs generate considerable portions of their revenue from the sale of such data.

The Association believes that the Commission should consider who will own the data generated by the ABS brokerage system. If the NYSE is deemed by the Commission to own the data, then the Association is concerned that member firms will be required to pay significant additional charges to obtain information for which they are currently already paying TRACE. As we have further noted above, the NYSE will in effect be competing with other brokers in effecting trades in unlisted debt securities. But unlike the SROs, these firms do not own the data that is created by trades generated through their systems. Thus, the Association is concerned that the NYSE’s status as an SRO, by virtue of allowing it to sell trade data, would afford the NYSE a significant competitive advantage over the other brokers with which the NYSE will be competing. The Association continues to believe that data on trades should be owned by the parties

⁴ See NASD Rule 6240(e)(2).

making such trades. And in the case of a public trading system such as the ABS, such data should be owned by the public and not any one entity. At a minimum, the Association believes that any fees imposed by the NYSE on the provision of such data must be reasonable and that the NYSE should not benefit from data ownership rights that are superior to its competitors.

III. Conflict Between NYSE's Roles as a Self Regulatory Organization and as a Broker of Unlisted Debt Securities

1. Regulator vs. Competitive Broker

As an initial matter, we note that the NYSE has already taken initiatives to separate its member regulation functions from its market regulation and operation functions. However, the Association is mindful that there has historically been a conflict between an exchange's role as a financial intermediary and its role as a regulator of financial intermediaries. As an SRO, the NYSE is entrusted with the duty to promulgate rules and monitor activities of its members. The Association believes that the Commission should consider the relationship between the NYSE's status as an SRO and its proposed role as a broker of unlisted corporate debt securities. To this end, we think that the Commission should also consider this issue in light of the expected privatization of the NYSE and monitor the NYSE periodically to evaluate any potential conflict that may arise.

2. Quotes on the ABS should not be Afforded Special Status

The Association is concerned that the NYSE or the SEC may in the future adopt regulations giving quotes posted on the NYSE special status by, for example, prohibiting firms and their customers from trading through such quotes, even though it benefits firms and their customers to do so.⁵ We are concerned not only about express rules benefiting NYSE quotes, which are at least subject to public comment, but by the possibility that regulators may use enforcement actions, or the threat of enforcement actions, predicated on best execution, as a device to pressure firms to interact with NYSE quotes. Accordingly, if the Commission does grant the NYSE relief, it should make clear that it will not now or in the future provide NYSE quotes with any special or preferential status.

3. Restrictive Trading Participation on ABS

Currently, all broker-dealers are generally able to participate in all markets for debt securities without being a member of an exchange since, as a practical matter, debt securities do not currently trade on exchanges. As a result, many members of the Association are not currently members of the NYSE or of other equity exchanges.

⁵ Firms and their customers would typically elect to trade through a quote that is of a small size, including an odd lot, and where the expense and inconvenience of trading does not justify the price differential.

The Association is thus concerned that the NYSE's proposal to create a closed (to non-NYSE members) trading system in certain fixed income securities could significantly injure broker-dealers that are not members of the NYSE and could effectively force those firms to become members of the NYSE or to acquire NYSE trading rights.⁶ The Association's concerns in this regard are magnified in light of the proposed NYSE privatization, which will likely result in a very material change in the way that trading privileges on the NYSE are granted. For example, the Association is concerned that if trading rights on ABS are limited to firms that also have rights to trade equity securities on the NYSE, the cost of ABS trading rights may be excessive in proportion to their actual value since the price of these rights will be effectively determined by the cost of the rights to trade equity securities. If that is the case, Association members who only trade fixed income securities will either be required to pay up for equity trading rights or else be excluded from a potentially significant market.

In order to address this concern, the Association believes that the Commission should consider making trading on the ABS open to all broker-dealers, subject to the payment of a limited transaction fee as is currently the case for automated trading systems. At a minimum, the Association urges the Commission to consider the competitive effects of the establishment of a "closed" trading market for fixed income securities and whether this will benefit investors. If the Commission does determine to allow the NYSE to exclude certain broker-dealers from trading, then the Commission should at least require the NYSE to offer trading privileges in ABS securities as a distinct right from trading privileges in equity securities, so that firms in the debt markets are not effectively forced to pay up for equity trading rights.

IV. Market Structure Issues

1. Further Exemptive Orders

As currently drafted, the NYSE's exemptive relief would only apply to trading on the NYSE of debt securities of issuers listed on the NYSE. However, it would seem reasonable to expect that further exemptive requests would follow from the grant of the NYSE request. The Association would like to raise certain questions that the Commission may consider as it evaluates what would be the market impact of further exemptions.

- Does the Commission intend to grant other exchanges the ability to trade on an unlisted basis in debt securities of issuers listed on those other exchanges? If so, what conditions does the Commission expect to impose in those future grants?

⁶ The SEC's language in the Notice of an Application characterizes the NYSE as requesting exemptive relief for its "members, brokers and dealers". *See* Release No. 34-51998 (July 8, 2005). However, we note that in its Application for an Exemption, the NYSE stated it is seeking exemptive relief for "NYSE members and member organizations". *See* Release No. 34-51998, Appendix A (July 8, 2005).

- Does the Commission intend to allow one exchange the ability to trade unlisted debt securities that are traded on another exchange? As a general matter, the Commission has moved away from allowing exchanges to have a monopoly in trading of any security. However, because of the structure of the NYSE's request, only the NYSE, and not the other exchanges, would have the ability to trade in the ABS traded debt securities.⁷ The grant of monopoly trading privileges to the NYSE combined with the ability of the NYSE to exclude trading by non-members is potentially worrisome and adds to the Association's concern about the pricing of ABS trading rights on the NYSE.
- Does the Commission see any benefit in issuers of equity securities continuing to list their debt securities on any exchange?

2. The Blue Sky Exemption under Section 18 should be Further Evaluated

Section 18 of the Securities Act of 1933 ("Securities Act") exempts covered securities from blue sky laws. "Covered securities" include, among others, securities listed on a national securities exchange and any securities senior to such securities. We note that the NYSE's proposal would apply to debt securities where the issuer or the issuer's parent (if the issuer is a wholly-owned subsidiary) has at least one class of registered equity securities. The Association is concerned that debt securities of issuers who do not themselves have equity securities listed on a national securities exchange (e.g., a wholly-owned subsidiary of a registered and listed issuer), would not benefit from the blue sky exemption. Furthermore, because debt securities traded on the ABS would no longer be "listed", the Association is concerned that unlisted securities that are senior to the previously listed debt securities would no longer be exempted from blue sky laws. The Association would like the Commission to take any action necessary to ensure that securities traded on the ABS be allowed to benefit from the blue sky exemption. Without such exemption, the benefits of the NYSE's proposal to the retail market would be limited, as retail investors in certain states could be prevented from purchasing ABS securities.

* * *

In conclusion, the Association is supportive of allowing the NYSE's proposal to proceed. However, we respectfully ask that the Commission consider the issues raised herein before allowing the NYSE to proceed. We would be pleased to discuss these issues further with the SEC staff, and appreciate your attention to our comments. Please contact the undersigned at (646) 637-9218 or via e-mail at Lhotchkiss@bondmarkets.com with any questions that you might have.

⁷ Section 12(f) of the Securities Act allows any national securities exchange to extend unlisted trading privileges to any security listed and registered on a national securities exchange. However, because the NYSE is proposing to trade certain unlisted securities on the ABS, Section 12(f) would not apply and the other exchanges would need to obtain their own exemptive relief from the SEC prior to allowing trading on such securities.

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Thank you for this opportunity to submit our views.

Very truly yours,

/s/ *Lynnette Kelly Hotchkiss*

Lynnette Kelly Hotchkiss
Senior Vice President and
Associate General Counsel

cc: ***Securities and Exchange Commission***

The Honorable Christopher Cox, Chairman
The Honorable Cynthia A. Glassman, Commissioner
The Honorable Paul S. Atkins, Commissioner
The Honorable Roel C. Campos, Commissioner
The Honorable Annette L. Nazareth, Commissioner
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The Bond Market Association

Corporate Credit Markets Division Executive Committee
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