

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-61566; File No. SR-FINRA-2009-065)

February 22, 2010

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as modified by Amendment No. 1 Thereto, to Require the Reporting of Transactions in Asset-Backed Securities to TRACE

I. Introduction

On October 1, 2009, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to designate asset-backed securities, mortgage-backed securities, and other similar securities (collectively, “Asset-Backed Securities”) as eligible for the Trade Reporting and Compliance Engine (“TRACE”), and to establish reporting, fee, and other requirements relating to such securities. The proposed rule change was published for comment in the Federal Register on October 28, 2009.³ The Commission received four comments in response to the proposal.⁴ On December 22, 2009, FINRA responded to the comments⁵ and on January 19, 2010, FINRA filed Amendment No. 1 to the proposal.⁶ The Commission is publishing this

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 60860 (October 21, 2009), 74 FR 55600 (“Notice”).

⁴ See *infra* note 13.

⁵ See letter from Sharon Zackula, Associate Vice President and Associate General Counsel, FINRA, to Elizabeth M. Murphy, Secretary, Commission, dated December 22, 2009 (“FINRA Letter”).

⁶ See *infra* Section III.

notice and order to solicit comments on Amendment No. 1 and to approve the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

II. Description of the Proposal

FINRA utilizes TRACE to collect from its members and publicly disseminate information on secondary over-the-counter transactions in corporate debt securities and, pursuant to a recent rule change to the Rule 6700 Series,⁷ Agency Debt Securities and certain primary market transactions. In this proposal, FINRA has proposed to expand TRACE to include the reporting (but not public dissemination) of Asset-Backed Securities. Specifically, the proposed rule change would:

(1) in Rule 6710, amend the defined terms (a) “TRACE-Eligible Security” to include Asset-Backed Securities; (b) “Reportable TRACE Transaction” to include specific requirements regarding certain Asset-Backed Securities; (c) “Agency Debt Security” to incorporate new defined terms; (d) “TRACE System Hours” to transfer the defined term from Rule 6730(a) to Rule 6710(bb); and (e) “Asset-Backed Security” to clarify that the definition included a residual tranche of an Asset-Backed Security;⁸

(2) to Rule 6710, add the defined terms, “Sponsor,” “Issuing Entity,” “TBA,” “Agency Pass-Through Mortgage-Backed Security,” “Factor,” “Specified Pool Transaction,” “Stipulation Transaction,” “Dollar Roll,” and “Remaining Principal Balance”;

(3) amend the definitions of “List or Fixed Offering Price Transaction” and “Takedown Transaction” in Rule 6710(q) and Rule 6710(r), respectively, to exclude from those defined terms transactions in any type of Asset-Backed Security;

⁷ See Securities Exchange Act Release No. 60726 (September 28, 2009), 74 FR 50991 (October 2, 2009) (approving SR-FINRA-2009-010).

⁸ See Amendment No. 1, infra Section III.

(4) in Rule 6710(y), amend the defined term “Stipulation Transaction” to delete the condition relating to the settlement of transactions not in conformity with certain uniform practices established as “good delivery”;

(5) in Rule 6710(w), amend the defined term “Factor”;⁹

(6) in Rule 6730, require the reporting of Asset-Backed Securities transactions;

(7) in Rule 6730(a)(6)(A), and for a six-month pilot period, establish the reporting period for Asset-Backed Securities transactions to no later than T+1 during TRACE System Hours;¹⁰

(8) in Rule 6730(d)(1), amend the requirement that a member input a commission stated in points per bond, and instead require reporting of the total dollar amount of a commission;

(9) in Rule 6730(d)(2), modify the manner that a member reports the Factor to require a member to report the Factor only if the Factor used is not the current most publicly available Factor for the Asset-Backed Security;

(10) in Rule 6730(d)(4)(B), add subparagraphs (i) and (ii) and, in subparagraph (ii), require members to report, for all transactions in Asset-Backed Securities, the actual date of settlement and indicate if the transaction will or will not settle “regular way”;¹¹

(11) in Rule 6750, provide that information on a transaction in a TRACE-Eligible Security that is an Asset-Backed Security will not be disseminated;

(12) in Rule 6760, require a member that is a Sponsor or an Issuing Entity of an Asset-Backed Security to provide the required notice to FINRA, and modify the notification requirements to accept a mortgage pool number in certain circumstances;

⁹ See id.

¹⁰ See id.

¹¹ See id.

(13) in Rule 7730, establish reporting fees for transactions in Asset-Backed Securities that are TRACE-Eligible Securities at the same rates in effect for transactions in corporate debt securities;¹² and

(14) in Rule 6700 Series, incorporate certain technical, administrative, and clarifying changes.

III. Summary of Comments and Amendment No. 1

The Commission received four comments on the proposed rule change,¹³ all of which generally supported the proposal.¹⁴

However, two commenters argued that FINRA's proposal did not go far enough, and recommended that FINRA also disseminate information about transactions in Asset-Backed Securities.¹⁵ In contrast, a third commenter supported FINRA's decision not to disseminate such information at the present time, and urged FINRA to study data collected on Asset-Backed Securities before making any determination regarding dissemination.¹⁶ FINRA agreed with the

¹² See id.

¹³ See letter from Beth N. Lawson, The Nelson Law Firm, LLC, dated November 13, 2009 ("Nelson Letter"); letter from Willard Stein, Ph.D., CFA, dated November 15, 2009 ("Stein Letter"); letter from John Hogue, Associate Portfolio Manager, Alexandria Capital Management Inc., dated November 17, 2009 ("Hogue Letter"); and letter from George P. Miller, Executive Director, American Securitization Forum and Randolph C. Snook, Senior Managing Director and Executive Vice President, Securities Industry and Financial Markets Association, dated November 18, 2009 ("SIFMA-ASF Letter") (collectively, the "Comment Letters").

¹⁴ See Nelson Letter (expressing strong support for increased price transparency); Stein Letter (supporting FINRA's proposal to designate Asset-Backed Securities as TRACE-eligible); Hogue Letter (stating that adding Asset-Backed Securities to the TRACE systems is a positive development); SIFMA-ASF Letter (stating that improvements to the transparency of structured finance products and markets are a necessary component to broad-based economic recovery).

¹⁵ See Stein Letter; Nelson Letter.

¹⁶ See SIFMA-ASF Letter at 2-3, 11-12.

third commenter and stated that the information on Asset-Backed Securities transactions should be collected and analyzed before it makes a decision regarding dissemination. FINRA added that, if it determines that the trading data provide a reasonable basis to seek dissemination of transaction information on Asset-Backed Securities, market participants and the public would have an opportunity to comment on a proposed rule change at that time.¹⁷

Two commenters expressed concern about FINRA's proposal to allow reports to be made by the close of business on the date of trade ("T"), and for transactions executed after 5:00 p.m. Eastern Time ("ET"), to the close of business on T+1.¹⁸ One of those commenters stated that the addition of Asset-Backed Securities to the TRACE system is a positive development, but questioned the usefulness of data that is not reported until T+1.¹⁹ A third commenter requested that FINRA extend the proposed reporting period for Asset-Backed Securities to the close of business on T+1 for all transactions, given the operational complexity of reporting such securities.²⁰ FINRA responded by proposing, in Amendment No. 1, for a six-month pilot period, to extend the reporting period for all transactions in Asset-Backed Securities to no later than T+1 during TRACE system hours.²¹ Upon expiration of the pilot program, the reporting

¹⁷ See FINRA Letter at 3-4.

¹⁸ See Stein Letter; Hogue Letter. FINRA Rule 6730(a) currently provides that all transactions in TRACE-Eligible Securities must be reported within 15 minutes of the time of execution, with certain exceptions for trades executed during non-TRACE System Hours. Rule 6730(a)(1) through (4) provides exceptions to the standard 15-minute reporting requirement if a member executes a transaction after or before TRACE System Hours or less than 15 minutes before the TRACE system closes.

¹⁹ See Hogue Letter.

²⁰ See SIFMA-ASF Letter at 6.

²¹ See Amendment No. 1; FINRA Letter at 2-3.

requirements would revert to the period originally proposed.²² FINRA also stated that, because the data are not subject to dissemination, allowing additional time for the reporting of Asset-Backed Securities transactions does not impact transparency.²³

One comment letter, submitted jointly by the American Securitization Forum and the Securities Industry and Financial Markets Association (“SIFMA-ASF”), raised a number of operational and technical issues. SIFMA-ASF noted, for example, that many Asset-Backed Securities do not have CUSIP numbers, and questioned how members could meet their reporting obligations for such securities.²⁴ In response, FINRA stated that it is working to develop a process for the efficient and timely identification of such securities and to provide a non-CUSIP security identifier when necessary.²⁵ Additionally, SIFMA-ASF requested that FINRA update and maintain the TRACE Issue Master File with information for all available Asset-Backed Securities, including Factor information in the TRACE system, prior to implementing its proposed rule change.²⁶ In response, FINRA agreed that, to facilitate and reduce reporting and

²² Rule 6730(a)(5) allows for an extended reporting period (until T+1) for “List or Fixed Offering Price Transaction” and “Takedown Transactions.” In this proposal, FINRA excluded Asset-Backed Securities from the definitions of List or Fixed Offering Price Transaction and Takedown Transaction. Therefore, upon the expiration of the pilot period, such transactions in Asset-Backed Securities would be required to be reported in accordance with the original proposal – *i.e.*, by the close of business on the date of trade (“T”), and for transactions executed after 5:00 p.m. ET, to the close of business on T+1. In contrast, any other List or Fixed Offering Price Transactions and Takedown Transactions would continue to be subject to T+1 reporting under Rule 6730(a)(5).

²³ See FINRA Letter at 2.

²⁴ See SIFMA-ASF Letter at 5.

²⁵ See FINRA Letter at 6.

²⁶ See SIFMA-ASF Letter at 9-10.

notification burdens to its members, it will obtain security information to update the TRACE Issue Master file prior to implementation of reporting requirements.²⁷

SIFMA-ASF suggested that FINRA modify the proposed requirement that a member report the specific Factor used to price an Asset-Backed Security transaction, recommending instead that FINRA obtain and maintain Factor information from master data files that are commercially available.²⁸ FINRA agreed with this comment and amended the proposal accordingly, and also proposed to add a sentence clarifying a member's reporting obligation for Asset-Backed Securities that are not priced using a Factor.

In the initial filing, FINRA proposed amendments regarding reporting the days to settlement. Specifically, FINRA proposed that: (1) for a transaction in an Agency Pass-Through Mortgage-Backed Security, no settlement-related indicator or modifier stating the number of days to settlement would be required in the transaction report if the settlement would be done in conformity with the uniform practices established as "good delivery" for such transactions on the next occurring monthly settlement date for such securities; and (2) for all other Asset-Backed Securities transactions, including transactions in Agency Pass-Through Mortgage-Backed Securities transactions not included in (1) above, members would report the number of days to settlement (e.g., ".s45," for a settlement scheduled to occur 45 days following execution). SIFMA-ASF suggested that FINRA amend these provisions to require members to report the actual date of settlement for all transactions in Asset-Backed Securities, rather than modifiers such as "regular way" or ".sNN." FINRA agreed with this comment²⁹ and proposed new rule text in Amendment No. 1 to effect this change.

²⁷ See FINRA Letter at 8.

²⁸ See SIFMA-ASF Letter at 3-6.

²⁹ See FINRA Letter at 6.

SIFMA-ASF further requested that FINRA phase in compliance for the new reporting requirements, making secondary market trades in Asset-Backed Securities reportable first, followed by primary market trades after six months.³⁰ FINRA disagreed with this suggestion and stated that, if it delayed implementation of the requirement for primary market reporting, it would not be aware of Asset-Backed Securities sold into the market during that period. FINRA further stated that its approach eliminates the implementation issue associated with determining if a transaction is a primary or secondary market transaction.³¹

Additionally, SIFMA-ASF requested that FINRA follow the approach where changes to several fields in customer transaction are separately classified as “amendments” rather than “late trades” to avoid penalizing broker-dealers for facilitating legitimate modifications to customer transactions that may occur in the normal course of business or that are the result of factors beyond their control.³² In response, FINRA stated that amended transaction reports are generally not required when modifications occur relating to delivery of assets or collateral or to settlement of a transaction.³³ SIFMA-ASF further asked that FINRA consider the additional costs to members for complying with the new reporting requirements and suggested eliminating the fees for modifying TRACE transaction reports.³⁴ FINRA responded that it is premature to consider any fee adjustments, as FINRA may incur greater costs in overseeing the market in light of the new data generated by reporting of transactions in Asset-Backed Securities.³⁵

³⁰ See SIFMA-ASF Letter at 10.

³¹ See FINRA Letter at 7.

³² See SIFMA-ASF Letter at 7.

³³ See FINRA Letter at 8.

³⁴ See SIFMA-ASF Letter at 11.

³⁵ See FINRA Letter at 9.

In Amendment No. 1, FINRA also made certain changes to the proposed rule text independent of any issues raised by commenters. FINRA determined that neither Rule 6730(a)(5)³⁶ nor the fee relief in Rule 7730(b)(1)(C) should apply to new issue Asset-Backed Securities, and in Amendment No. 1, FINRA proposed changes to certain rule text to effect this determination. Specifically, in Amendment No. 1, FINRA amended the definitions “List or Fixed Offering Price Transaction” in proposed Rule 6710(q) and “Takedown Transaction” in proposed Rule 6710(r) to exclude from such defined terms transactions in any type of Asset-Backed Security. As a result of this change, members will be required to pay reporting fees for all primary market transactions in Asset-Backed Securities, as no new issue transactions in Asset-Backed Securities would be eligible for the fee relief set forth in Rule 7730(b)(1)(C), which applies only to transactions that are a “List or Fixed Offering Price Transaction” or a “Takedown Transaction.”

Rule 6730(d)(1) currently requires a member to report a commission stated in points per bond. However, recognizing that many Asset-Backed Securities do not have par or principal values of \$1,000, FINRA is proposing in Amendment No. 1 to amend Rule 6730(d)(1) to require members to input the total dollar amount of a commission when reporting a transaction in an Asset-Backed Security, rather than stating the commission in points per bond.

Amendment No. 1 also would delete references to uniform practices established as “good delivery” in the defined terms “TBA” in Rule 6710(u) and “Stipulation Transaction” in Rule 6710(y), and revise the defined term “Factor” in Rule 6710(w). Also in Amendment No. 1, FINRA proposed to incorporate certain non-substantive, technical, clarifying, and formatting amendments in the Rule 6700 series and in Rule 7730.

³⁶ See supra note 22.

Finally, FINRA modified certain aspects of the proposed rule change to account for changes in the TRACE rules that had been approved recently by the Commission.³⁷ FINRA also represented in Amendment No. 1 that, if the Commission approves SR-FINRA-2009-065, as amended, it undertakes not to not make this proposal effective until the rule changes from the two intervening filings have become effective.

IV. Discussion

After carefully considering the proposal and the comments submitted, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.³⁸ In particular, the Commission finds that the proposed rule change is consistent with Section 15A(b)(6) of the Act,³⁹ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The Commission does not believe that the comments raise any issue that would preclude approval of the proposal.

Prior to TRACE's implementation, the NASD (FINRA's predecessor) did not have routine access to comprehensive transaction information for the over-the-counter corporate bond market, even though the NASD bore responsibility for surveilling and regulating that market. In

³⁷ See Securities Exchange Act Release No. 60726 (September 28, 2009), 74 FR 50991 (October 2, 2009) (approving SR-FINRA-2009-010); FINRA Regulatory Notice 09-57 (September 2009) (stating that the rule text of SR-FINRA-2009-010 becomes effective March 1, 2010); Securities Exchange Act Release No. 61012 (November 16, 2009), 74 FR 61189 (November 23, 2009) (approving SR-FINRA-2007-006). FINRA will publish a Regulatory Notice announcing the effective date of SR-FINRA-2007-006, which shall be a day shortly following the effective date of SR-FINRA-2009-010.

³⁸ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

³⁹ 15 U.S.C. 78o-3(b)(6).

originally approving TRACE, the Commission stated that obtaining such information to better conduct market surveillance was a fundamental means of promoting fairness and confidence in U.S. capital markets.⁴⁰ Similarly, with respect to the over-the-counter market for Asset-Backed Securities, FINRA currently does not possess the comprehensive transaction information that would help it carry out its statutory duties to regulate this market. The Commission believes, therefore, that it is reasonable and consistent with the Act for FINRA to expand TRACE to designate Asset-Backed Securities as TRACE-Eligible Securities, and to establish reporting, fee, and other requirements relating to such securities in the manner set forth in the proposal. Expanding TRACE to include Asset-Backed Securities is reasonably designed to help FINRA fulfill its mandate in Section 15A(b)(6) of the Act⁴¹ to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The Commission acknowledges the potential for firms covered by these new reporting requirements to incur certain compliance burdens. However, the Commission believes that any such burdens are justified by the overall benefits of regulators having access to more comprehensive trade information in the fixed income markets. The Commission notes that FINRA has proposed, for a six-month pilot period, a T+1 reporting period for Asset-Backed Securities, rather than a same-day reporting period as originally proposed.⁴² The Commission believes that this modification is reasonably designed to ease the compliance burdens on those

⁴⁰ See Securities Exchange Act Release No. 43873 (January 23, 2001) 66 FR 8131, 8136 (January 29, 2001).

⁴¹ 15 U.S.C. 78o-3(b)(6).

⁴² See Amendment No. 1.

affected by the proposal without significantly compromising FINRA's ability to obtain comprehensive transaction information regarding the market for Asset-Backed Securities.

The Commission notes that FINRA has not proposed to publicly disseminate any transaction information relating to Asset-Backed Securities at this time. FINRA believes that information on Asset-Backed Securities transactions should be collected and analyzed before making any decision regarding the utility of such information for transparency purposes or the consequences of dissemination on this market. FINRA has stated that, after a period of study, it would file a proposed rule change if it determined that its study of the trading data provides a reasonable basis to seek dissemination of transaction information on Asset-Backed Securities. The Commission has historically been supportive of efforts to improve post-trade transparency in the fixed income markets and encourages FINRA to carry out that study.

The Commission further finds that the proposed fees set forth in Rule 7730 for the reporting of transactions in Asset-Backed Securities are consistent with Section 15A(b)(5) of the Act,⁴³ which requires, among other things, that FINRA rules provide for the equitable allocation of reasonable dues, fees, and other charges among members and issuers and other persons using any facility or system that FINRA operates or controls.⁴⁴

V. Accelerated Approval

The Commission finds good cause, pursuant to Section 19(b)(2) of the Act,⁴⁵ for approving the proposed rule change, as modified by Amendment No. 1 thereto, prior to the 30th day after the date of publication of the amended proposal in the Federal Register. The changes

⁴³ 15 U.S.C. 78o-3(b)(5).

⁴⁴ The Commission notes that, because transaction information regarding Asset-Backed Securities will not be disseminated, FINRA has not proposed any market data fees for this information at this time.

⁴⁵ 15 U.S.C. 78s(b)(2).

proposed in Amendment No. 1 are minor and technical in nature or are designed to respond to specific concerns raised by commenters. Accordingly, the Commission finds that good cause exists to approve the proposal, as modified by Amendment No. 1, on an accelerated basis.

VI. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether Amendment No. 1 to the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2009-065 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2009-065. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F

Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing will also be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. SR-FINRA-2009-065 and should be submitted on or before [insert date 21 days from date of publication in the Federal Register].

VII. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁴⁶ that the proposed rule change (SR-FINRA-2009-065), as modified by Amendment No.1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁷

Florence E. Harmon
Deputy Secretary

⁴⁶ 15 U.S.C. 78s(b)(2).

⁴⁷ 17 CFR 200.30-3(a)(12).