

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-68414; File No. SR-FINRA-2012-052)

December 12, 2012

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change to Require Members to Report the Factor to TRACE in Asset-Backed Security Transactions (Except an Asset-Backed Security Traded TBA), in the Limited Instances When Members Effect Such Transactions as Agent and Charge a Commission

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that, on November 29, 2012, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend FINRA Rule 6730(d)(2) to require a member to report to Trade Reporting and Compliance Engine (TRACE) the Factor used to determine the size (volume) of each transaction in an Asset-Backed Security (except an Asset-Backed Security traded To Be Announced), in the limited instances when members effect such transactions as agent and charge a commission.

The text of the proposed rule change is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA and at the Commission’s Public Reference Room.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

In general, Asset-Backed Securities (“ABS”)³ are traded on a principal basis and only a small number of ABS transactions are traded on an agency basis and charge a commission.⁴ In the limited instances when a member executes an ABS transaction (except an ABS traded To Be Announced (a “TBA transaction”)) in an agency capacity and charges a commission, FINRA proposes to require members to report the Factor⁵ as discussed below.

Currently, under FINRA Rule 6730(c)(2) and Rule 6730(d)(2), a member is required to report the size of TRACE-Eligible Securities,⁶ including certain ABS, by reporting the total par or principal value of the debt securities traded. However, in a transaction in an ABS that is backed by mortgages or other assets that amortize over the life of the security (an “amortizing

³ See FINRA Rule 6710(m) for the definition of Asset-Backed Security.

⁴ From May 2011, when TRACE began receiving reports on ABS, to the present, whether measured by par value or number of transactions, transactions in ABS that are executed in an agency capacity and subject to a commission represent only approximately one percent of all ABS transactions.

⁵ See FINRA Rule 6710(w) for the definition of Factor.

⁶ See FINRA Rule 6710(a) for the definition of TRACE-Eligible Security.

ABS”), instead of reporting the total par or principal value, a member reports two items from which the size is calculable: (1) the original face value of the ABS, which is the size at issuance; and (2) the Factor, but only if the Factor used to execute the transaction is not the most current Factor that is publicly available at the time of execution of such transaction (a “non-conforming Factor”).⁷

A Factor is the decimal value that represents the proportion of (1) the principal value (or face value) of the pool of assets underlying an amortizing ABS remaining at the time of the execution of a transaction (typically referred to as “remaining principal balance” or “RPB”) to (2) the original face value of the ABS. Such Factors are published monthly by federal agencies or government-sponsored enterprises for ABS that are issued or guaranteed by them. Factors for other ABS generally are consolidated by certain commercial vendors that obtain them from servicers.

FINRA proposes to amend FINRA Rule 6730(d)(2) to require a member to report the Factor to TRACE for every transaction in an ABS (except TBA transactions) in the limited instances when the member effects that transaction as agent and charges a commission. The amendment is proposed to prepare for the dissemination of Specified Pool Transactions, and transactions in additional ABS market segments, if such transactions subsequently are disseminated under Rule 6750 in the future.⁸ The proposed rule change is necessary to ensure

⁷ When a member uses the most current Factor that is publicly available at the time of execution of the transaction, the member is not required to report the Factor. Instead, the TRACE system incorporates the most current Factor publicly available at the Time of Execution of the transaction. FINRA receives such information from commercial data vendors.

⁸ FINRA proposes the dissemination of certain Specified Pool Transactions in SR-FINRA-2012-042, which was approved recently by the SEC but is not yet effective. See Securities Exchange Act Release No. 68084 (October 23, 2012), 77 FR 65436 (October 26, 2012) (SEC Order Approving File No. SR-FINRA-2012-042 regarding a proposal to

the accuracy of the disseminated price of an ABS transaction, which, if traded on an agency basis and subject to a commission charge, is calculated using the Factor, the price and other information reported by a member that is a party to the transaction.

Though very few ABS transactions are executed in an agency capacity with a commission charged, when done so the TRACE system must calculate the disseminated price (or all-in price) based on the reported price, which is reported as a percentage of the RPB (e.g., 97), and add the proportionate amount of commission. However, the commission is reported as the total gross dollar amount (e.g., \$3,000.00).⁹ To account for the commission impact on the total price paid or received by the customer, the TRACE system calculates the amount of commission in relation to RPB, which takes the Factor into account.¹⁰

Currently, all components of the formula that would be used to calculate a disseminated price in an ABS transaction executed as agent, except the Factor, are reported by a member effecting the transaction. The proposed amendments to Rule 6730(d)(2) would ensure the accuracy of the disseminated price data by relying exclusively upon information, including the Factor, that would be reported by the members that are parties to a transaction. Accordingly, FINRA proposes in FINRA Rule 6730(d)(2)(B)(iv) that a member report the Factor in the limited instances when an ABS transaction is executed in an agency capacity with a commission charged (except for TBA transactions), regardless of whether such Factor is the most current

disseminate Agency Pass-Through Mortgage-Backed Securities traded in Specified Pool Transactions and SBA-Backed ABS traded TBA and in Specified Pool Transactions). The effective date of the amendments in SR-FINRA-2012-042 will be announced in a Regulatory Notice.

⁹ FINRA Rules 6730(c)(3) and 6730(d)(1) require members to report the price, which must exclude the commission, and separately report the total dollar amount of the commission.

¹⁰ The portion of the commission is calculated by dividing the dollar amount of the commission by the total size (which is the product of the original face value multiplied by the Factor). The resulting number is multiplied by 100.

Factor publicly available at execution or is a non-conforming Factor. In addition, FINRA proposes supplementary material to clarify that the requirement to report the Factor will apply to every ABS transaction executed in an agency capacity with a commission charged, including the very small number of transactions in non-amortizing ABS.¹¹

FINRA also proposes to reorganize, with technical amendments, the current requirements to report size in FINRA Rule 6730(d)(2). First, the requirement to report size for transactions in securities other than ABS would be set forth in proposed Rule 6730(d)(2)(A) and would continue to require members to report the total par value or principal value of the security. Second, proposed FINRA Rule 6730(d)(2)(B)(i), (ii) and (iii) would restate current requirements regarding reporting size of other transactions in ABS as follows: in (B)(i), for a TBA transaction, a member would be required to report the original face value of the security; in (B)(ii), for a transaction in an amortizing ABS, other than a TBA transaction, a member would be required to report the original face value of the security and, if a member used a Factor to execute the transaction that was not the most current Factor publicly available at the Time of Execution, to report the Factor used, except if executed in an agency capacity and subject to the requirements of proposed FINRA Rule 6730(d)(2)(B)(iv) as described above; and in (B)(iii), for a transaction in a non-amortizing ABS, a member would be required to report the original face value of the security, except if executed in an agency capacity and subject to the requirements of proposed FINRA Rule 6730(d)(2)(B)(iv) as described above.

¹¹ FINRA recognizes that in non-amortizing ABS, such as ABS backed by credit card receivables, amortization does not occur, and thus, a Factor is not generally referenced to indicate the size of a transaction. However, since so few transactions are executed in agency capacity with commission charged, proposed FINRA Rule 6730(d)(2)(B)(iv) would not distinguish between amortizing ABS and non-amortizing ABS, and would require a member to report a Factor in every ABS transaction (except TBA transactions) executed in agency capacity with a commission charged. For any such transactions in a non-amortizing ABS, a member would report 1.0 as the Factor.

FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 270 days following publication of the Regulatory Notice announcing Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹² 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. FINRA believes that the proposed rule change will ensure the accuracy of the price transparency provided by TRACE by requiring members that are party to an ABS transaction (except a TBA transaction) to report the Factor in the limited instances when the transaction is executed in agency capacity with a commission charged. FINRA believes the tailored reporting requirement is appropriate given that only approximately one percent of all ABS transactions are executed in agency capacity with a commission charged. FINRA believes that the price transparency provided by TRACE assists all market participants in determining the quality of their executions and member firms in complying with their regulatory obligations, including best execution obligations. In addition, accurate price transparency may have a positive impact on the quality of pricing for valuation purposes.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

¹² 15 U.S.C. 78o-3(b)(6).

FINRA believes that the proposed rule change will ensure the accuracy of the price transparency provided by TRACE by requiring members that are party to an ABS transaction (except a TBA transaction) to report the Factor in the limited instances when a transaction is executed in agency capacity with a commission charged. FINRA believes the reporting requirement is appropriately tailored to minimize the burden and cost of complying with the rule in that the proposed requirement will apply only to approximately one percent of all ABS transactions. In addition, the proposed reporting requirement applies equally to any member that executes such transactions.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether 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-2012-052 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-2012-052. 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 website (<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 website 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 also will 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 Number SR-FINRA-2012-052 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹³

Kevin M. O'Neill
Deputy Secretary

¹³ 17 CFR 200.30-3(a)(12).