

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-49607; File No. SR-NASD-2004-057)

April 23, 2004

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1 and 2 by the National Association of Securities Dealers, Inc. Relating to Proposed Amendments to Reduce the Reporting Period for Transactions in TRACE-Eligible Securities

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on April 1, 2004, the National Association of Securities Dealers, Inc. (“NASD”) 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 NASD. On April 16, 2004, NASD filed Amendment No. 1 to the proposed rule change.<sup>3</sup> On April 22, 2004, NASD filed Amendment No. 2 to the proposed rule change.<sup>4</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See letter from Sharon K. Zackula, Assistant General Counsel, NASD, to Katharine A. England, Assistant Director, Division of Market Regulation, SEC, dated April 16, 2004 (“Amendment No. 1”). Amendment No. 1 clarifies the effective dates that NASD will establish for the proposed rule change upon approval by the Commission.

<sup>4</sup> See letter from Sharon K. Zackula, Assistant General Counsel, NASD, to Katharine A. England, Assistant Director, Division of Market Regulation, SEC, dated April 22, 2004 (“Amendment No. 2”). Amendment No. 2 amends the discussion of industry and regulatory trends in the securities industry favoring more “real-time” reporting and “real-time” transmission of transaction information for clearance and settlement.

OF SUBSTANCE OF THE PROPOSED RULE CHANGE

NASD is proposing to amend Rule 6230(a) to reduce the period to report a transaction in a TRACE-eligible debt security in two stages: (i) from 45 to 30 minutes in stage one (“Stage One”), and (ii) subsequently, from 30 to 15 minutes in stage two (“Stage Two”). Rule 6230 is one of the Trade Reporting and Compliance Engine (“TRACE”) rules. Below is the text of the proposed rule change. Proposed new language is in *italics*; proposed deletions are in brackets.

Stage One Rule Text:

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**6200. TRADE REPORTING AND COMPLIANCE ENGINE (TRACE)**

\* \* \* \* \*

**6230. Transaction Reporting**

**(a) When and How Transactions are Reported**

A member that is required to report transaction information pursuant to paragraph (b) below must report such transaction information within 30[45] minutes of the time of execution, except as otherwise provided below, or the transaction report will be "late." The member must transmit the report to TRACE during the hours the TRACE system is open ("TRACE system hours"), which are 8:00 a.m. Eastern Time through 6:29:59 p.m. Eastern Time. Specific trade reporting obligations during a 24-hour cycle are set forth below.

**(1) Transactions Executed During TRACE System Hours**

Transactions in TRACE-eligible securities executed on a business day at or after 8:00 a.m. Eastern Time through 6:29:59 p.m. Eastern Time must be

reported within 30[45] minutes of the time of execution. If a transaction is executed on a business day less than 30[45] minutes before 6:30 p.m. Eastern Time, a member may report the transaction the next business day within 30[45] minutes after the TRACE system opens. If reporting the next business day, the member must indicate “as/of” and provide the actual transaction date.

**(2) Transactions Executed At or After 6:30 P.M. Through 11:59:59 P.M. Eastern Time**

Transactions in TRACE-eligible securities executed on a business day at or after 6:30 p.m. Eastern Time through 11:59:59 p.m. Eastern Time must be reported the next business day within 30[45] minutes after the TRACE system opens. The member must indicate “as/of” and provide the actual transaction date.

**(3) Transactions Executed At or After 12:00 A.M. Through 7:59:59 A.M. Eastern Time**

Transactions in TRACE-eligible securities executed on a business day at or after 12:00 a.m. Eastern Time through 7:59:59 a.m. Eastern Time must be reported the same day within 30[45] minutes after the TRACE system opens.

**(4) Transactions Executed on a Non-Business Day**

Transactions in TRACE-eligible securities executed on a Saturday, Sunday, or a federal or religious holiday on which the TRACE system is closed, at any time during that day (determined using Eastern Time), must be reported the next business day within 30[45] minutes after the TRACE system opens. The transaction must be reported as follows: the date of execution must be the first business day (the same day the report must be made); the execution time must be “12:01:00 a.m. Eastern Time” (stated in military time as “00:01:00”); and the modifier, “special price,” must be selected. In addition, the transaction must not

be designated “as/of”. When the reporting method chosen provides a “special price” memo field, the member must enter the actual date and time of the transaction in the field.

**(5) and (6) No Change**

**(b) through (f) No Change**

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Stage Two Rule Text:

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**6200. TRADE REPORTING AND COMPLIANCE ENGINE (TRACE)**

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**6230. Transaction Reporting**

**(a) When and How Transactions are Reported**

A member that is required to report transaction information pursuant to paragraph (b) below must report such transaction information within 15[30] minutes of the time of execution, except as otherwise provided below, or the transaction report will be "late." The member must transmit the report to TRACE during the hours the TRACE system is open ("TRACE system hours"), which are 8:00 a.m. Eastern Time through 6:29:59 p.m. Eastern Time. Specific trade reporting obligations during a 24-hour cycle are set forth below.

**(1) Transactions Executed During TRACE System Hours**

Transactions in TRACE-eligible securities executed on a business day at or after 8:00 a.m. Eastern Time through 6:29:59 p.m. Eastern Time must be reported within 15[30] minutes of the time of execution. If a transaction is

executed on a business day less than 15[30] minutes before 6:30 p.m. Eastern Time, a member may report the transaction the next business day within 15[30] minutes after the TRACE system opens. If reporting the next business day, the member must indicate “as/of” and provide the actual transaction date.

**(2) Transactions Executed At or After 6:30 P.M. Through 11:59:59 P.M. Eastern Time**

Transactions in TRACE-eligible securities executed on a business day at or after 6:30 p.m. Eastern Time through 11:59:59 p.m. Eastern Time must be reported the next business day within 15[30] minutes after the TRACE system opens. The member must indicate “as/of” and provide the actual transaction date.

**(3) Transactions Executed At or After 12:00 A.M. Through 7:59:59 A.M. Eastern Time**

Transactions in TRACE-eligible securities executed on a business day at or after 12:00 a.m. Eastern Time through 7:59:59 a.m. Eastern Time must be reported the same day within 15[30] minutes after the TRACE system opens.

**(4) Transactions Executed on a Non-Business Day**

Transactions in TRACE-eligible securities executed on a Saturday, Sunday, or a federal or religious holiday on which the TRACE system is closed, at any time during that day (determined using Eastern Time), must be reported the next business day within 15[30] minutes after the TRACE system opens. The transaction must be reported as follows: the date of execution must be the first business day (the same day the report must be made); the execution time must be “12:01:00 a.m. Eastern Time” (stated in military time as “00:01:00”); and the modifier, “special price,” must be selected. In addition, the transaction must not be designated “as/of”. When the reporting method chosen provides a “special

price” memo field, the member must enter the actual date and time of the transaction in the field.

**(5) and (6) No Change**

**(b) through (f) No Change**

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II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its filing with the Commission, NASD 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. NASD 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

NASD Rule 6230(a) currently requires a member that is a party to a transaction in a TRACE-eligible security to report the transaction information to TRACE within 45 minutes of the time of execution.<sup>5</sup> NASD is proposing to reduce the period to report a

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<sup>5</sup> Limited exceptions to the general requirement are stated in Rule 6230(a)(1) through (4), which provide for reporting a transaction the next business day that the TRACE system is open in certain circumstances. Specifically, in Rule 6230(a)(1), a member currently may elect to report a transaction the next business day that the TRACE system is open at any time within 45 minutes after the TRACE system opens, if the member executed the trade the prior business day less than 45 minutes before the TRACE system closed. (Currently, on a business day, the TRACE system is open from 8:00 a.m. Eastern Time to 6:30 p.m. Eastern Time to receive reports.) In Rule 6230(a)(2) through (4), members are directed how to report trades that occur (1) after TRACE system hours, (2) before TRACE system hours, or (3) on a weekend or a holiday. In each case, the member must

transaction in two stages. In Stage One, the reporting period will be reduced from 45 minutes to 30 minutes, and, in Stage Two, the reporting period will be reduced from 30 minutes to 15 minutes.

### **Stage One: Reduction of Reporting Period to 30 Minutes**

NASD is proposing to amend Rule 6230 to reduce the reporting period from 45 minutes to 30 minutes during Stage One. In Rule 6230(a), the general requirement to report transaction information within 45 minutes of the time of execution is restated as 30 minutes. In addition, NASD is proposing to amend the next-day reporting exceptions in Rules 6230(a)(1) through (4) to require that the report be filed within 30 minutes of the time the TRACE system opens instead of the current 45 minutes. Specifically, in Rule 6230(a)(1), a member could elect to report the next business day if a transaction occurs within 30 minutes before the TRACE system closing. If the member elects to report the following business day that the TRACE system is open, the member must report the transaction within 30 minutes after the TRACE system opens.<sup>6</sup> In addition, in Rule

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report the transaction the next business day that the TRACE system is open within 45 minutes of the opening.

<sup>6</sup> On days when NASD announces that the TRACE System will close early (e.g., at 2:00 p.m. on the day after Thanksgiving or the day before Independence Day), NASD will announce the early closing and specify when the TRACE System will cease accepting reports. When early closings in TRACE occur, NASD interprets Rule 6230(a)(1), as allowing a member (for a transaction that occurs just before the end of the TRACE System closing) to report the transaction on the day of execution before the system closes or the next business day, to provide the member the same flexibility that is provided when the TRACE System closes at 6:30 p.m. Eastern Time. For example, if NASD announces that the TRACE System will close at 2:00 p.m. Eastern Time and will not accept reports after that time, a 30-minute reporting period is in effect, and a member executes a transaction at 1:40 p.m. Eastern Time, the member may report the transaction on the day of execution (through 2:00 p.m. Eastern Time) or may report the transaction the next business day that the TRACE System is open within 30 minutes of the opening.

6230(a)(2) through (4), a member would be required to report transaction information for specified transactions the next business day that the TRACE system is open and would be required to do so within 30 minutes after the system's opening.

The effective date of Stage One, the 30-minute reporting period, will be October 1, 2004.

### **Stage Two**

In addition, NASD is proposing to amend Rule 6230 a second time to reduce the reporting period from 30 minutes to 15 minutes. The amended rule text set forth above as Stage Two contains the proposed changes.

The proposed rule change set forth in Stage Two also includes proposed amendments to Rule 6230(a)(1) through (a)(4) to reduce the reporting periods referenced therein from 30 minutes to 15 minutes; they are parallel to the amendments to paragraphs (a)(1) through (a)(4) of Rule 6230 that are proposed as part of Stage One and described above. Thus, NASD is proposing to amend the next-day reporting provisions in Rules 6230(a)(1) through (4) to require that a transaction report be filed within 15 minutes of the time the TRACE system opens instead of the 30-minute period that would then be in effect.<sup>7</sup>

The effective date of Stage Two, 15-minute reporting, will be July 1, 2005.

Under the proposal, members will have nine months after 30-minute reporting is

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<sup>7</sup> Specifically, in Rule 6230(a)(1), a member could elect to report the next business day if a transaction occurred within 15 minutes before the TRACE system closing. If the member elected to report the following business day that the TRACE system is open, the member must report the transaction within 15 minutes after the TRACE system opens. In addition, in Rule 6230(a)(2) through (4), a member would be required to report transaction information for specified transactions the next business day that the TRACE system is open and would be required to do so within 15 minutes after the system's opening.



implemented to prepare for Stage Two 15-minute reporting.

### **Rationale for Reducing The Reporting Period**

Consistent with longstanding NASD and SEC goals, NASD is proposing to reduce the reporting period from 45 minutes to 30 minutes, and from 30 minutes to 15 minutes, to improve transparency in the corporate debt securities markets for the benefit of investors and market participants. Reducing the reporting period to 30, then 15 minutes, will allow investors and market participants to obtain and evaluate pricing information more quickly than under the current reporting requirements, improving the timeliness and value of the information to investors and creating a qualitative increase in corporate bond market transparency.

By reducing the reporting period to 30, then 15 minutes, the reporting goal originally set forth in the proposed TRACE Rules in 1999 will be achieved.<sup>8</sup> In 2001, when the SEC approved the proposed TRACE Rules (then containing a 60-minute reporting period), the SEC stated its expectation that NASD would file a rule proposal within six months from the start date of TRACE to reduce the reporting period to 15 minutes. The SEC said, “NASD plans to reduce the time frame for reporting bond trades—from one hour to 15 minutes . . . . This will ensure that transaction information is reported to TRACE and released to the public before it becomes ‘stale.’”<sup>9</sup> The

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<sup>8</sup> See SR-NASD-99-65, filed on October 27, 1999, and amendments thereto.

<sup>9</sup> See Securities Exchange Act Release No. 43873 (January 23, 2001), 66 Fed. Reg. 8131, 8135 (January 29, 2001) (SEC Order approving SR-NASD-99-65). There were a number of technical, operational, and regulatory issues to resolve before NASD believed it was appropriate to propose 15-minute reporting. Shortly before TRACE began, at the SEC’s request, NASD developed a proposal to extend, rather than reduce, the reporting period from 60 minutes to 75 minutes to accommodate the DTCC’s participation in TRACE for those firms that wished to

NASD's 15-minute reporting goal was also restated in SR-NASD-2003-78, which is the proposed rule change to reduce the reporting period from 75 minutes to 45 minutes that the SEC approved on June 18, 2003.<sup>10</sup>

In this proposed rule change, NASD is proposing to achieve 15-minute reporting in two stages for several reasons. Firms have expressed concern about their ability to achieve a 15-minute reporting standard, and a two-stage process will allow firms to make incremental improvements in their reporting processes and provide time for them to adjust to the shorter periods. In addition, NASD is proposing both stages of the reduction in this proposed rule change, rather than in two separate rule proposals, to provide notice to the industry of the NASD's general plan to achieve 15-minute reporting. By doing so, the industry has a longer period to prepare for the changes and should be able to make the technical and operational changes needed to achieve 15-minute reporting more efficiently. In fact, many transactions are currently reported to TRACE within the 30 and 15-minute timeframes. Approximately eighty-four percent (84%) of all trades reported to TRACE in the first two months of 2004 were reported within 30 minutes. In addition, during the same period approximately seventy-three percent (73%) of all trades were reported within 15 minutes.

NASD's proposal to reduce the reporting period is also timely, because it moves

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report TRACE transactions via DTCC. (At that time, DTCC's system had certain operational limits, and 60-minute reporting would not have been possible using that system.) On October 1, 2003, 15 months after TRACE operated using a 75-minute reporting regimen, NASD reduced the reporting period to 45 minutes. This proposed rule change will reduce the reporting period to 15 minutes ultimately, in two stages.

<sup>10</sup> See Securities Exchange Act Release No. 47856 (May 14, 2003); 68 Fed. Reg. 27605 (May 20, 2003) (Notice of Filing of SR-NASD-2003-78 and Request for Comment), n. 7. SR-NASD-2003-78 was approved in Securities Exchange Act Release No. 48056 (June 18, 2003), 68 Fed. Reg. 37886 (June 25, 2003).

the corporate debt markets closer to general industry and regulatory trends favoring more “real-time” reporting, and “real-time” transmission of transaction information for clearance and settlement. The Depository Trust and Clearing Corporation (“DTCC”) is working with the industry in an initiative called RTTM. Broker-dealers currently transmit trade information “real-time” using RTTM’s interactive messaging, on more than 50% of all mortgaged-backed securities transactions and on approximately 95% of all government securities transactions processed through DTCC.<sup>11</sup>

Finally, NASD’s proposed rule change to reduce the reporting period is in accordance with SEC and industry requests for some degree of coordination regarding the reporting of debt securities. To accommodate TRACE participants’ requests for a “single DTCC pipeline” to process and report both corporate and municipal securities transactions, NASD has worked with the industry and DTCC to coordinate the timing of the implementation of the 15-minute reporting requirement with DTCC’s connection of RTTM directly to TRACE.

## 2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>12</sup> which requires, among other things, that NASD’s 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. NASD believes that the proposed rule change will provide NASD with

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<sup>11</sup> Government securities transactions are processed at DTCC’s Fixed Income Clearing Corporation (“FICC”) in its Government Securities Division, and mortgage-backed securities transactions are processed in FICC’s Mortgage-Backed Securities Division.

<sup>12</sup> 15 U.S.C. 78o-3(b)(6).

heightened capabilities to regulate and provide surveillance of the debt securities markets to prevent fraudulent and manipulative acts and practices, will improve transparency for the benefit of customers and other market participants by reducing the period between the time of execution of a transaction and the dissemination of transaction information for securities subject to dissemination in furtherance of the public interest and for the protection of investors.

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

NASD 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, as amended.

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 35 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 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](mailto:rule-comments@sec.gov). Please include File Number SR-NASD-2004-057 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-NASD-2004-057. 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 inspection and copying in the Commission's Public Reference Room. Copies of such filing also will be available for inspection and copying at the principal office of NASD. 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-NASD-2004-057 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>13</sup> 17 CFR 200.30-3(a)(12).