PIMCO

March 28, 2014

Submitted via Email to pubcom@finra.org
Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: Proposed Amendments to FINRA Rule 4210 for TBA Transactions

Dear Ms. Asquith:

Pacific Investment Management Company LLC (**"PIMCO"**) is pleased to submit this letter to the Financial Industry Regulatory Authority (**"FINRA"**) in response to FINRA's request for comment on its proposed amendments to FINRA Rule 4210, which would establish margin requirements for transactions in "Covered Agency Securities," which include transactions in the "To-Be-Announced" (**"TBA"**) market[1] (the **"Proposed Amendments"**).

PIMCO is a global investment management firm that serves an array of clients and manages retirement and other assets for millions of people in the U.S. and throughout the world. Our clients include state, municipal, union and private sector pension and retirement plans, educational foundations, endowments, philanthropic and healthcare institutions, in addition to millions of individual mutual fund investors. PIMCO manages assets in a fiduciary capacity on behalf of its clients and does not invest for its own account.

PIMCO participates in numerous working groups that are submitting separate comment letters to FINRA. Since we have addressed the majority of our comments through those letters, this letter will focus on one significant omission from some of those letters that we believe FINRA should be made aware of, namely that Covered Agency Securities should be defined by reference to a uniform settlement cycle of T+3.

As you know the Treasury Market Practices Group (the **"TMPG"**) developed a set of Best Practices for Treasury, Agency Debt and Agency Mortgage-Backed Securities Markets (the **"TMPG Best Practices"**) providing guidelines for market participants in the TBA market. In addition to issuing the TMPG Best Practices, the TMPG also issued a recommendation regarding the margining of forward-settling agency mortgage-backed securities (**"agency MBS"**), which proposed requiring margin for four broad categories of agency MBS transactions, including TBA

[1] The TBA market includes transactions in adjustable rate mortgages (**"ARMs"**), Specified Pool Transactions and Collateralized Mortgage Obligations (**"CMOs"**) with forward settlement dates.

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transactions, specified pool transactions, adjustable-rate mortgage ("**ARM**") transactions, and collateralized mortgage obligation ("**CMO**") transactions (the "**Margining Recommendation**").[2] The Margining Recommendation provided that margining be applied based on the type of agency MBS transaction, utilizing the existing market trading and settlement conventions for each transaction type. Accordingly, the TMPG recommended that for TBA, specified pool and ARM transactions, all trades for which the difference between trade date and contractual settlement date is greater than one business day (T+1), be subject to margining; and for CMO transactions, that all trades for which the difference between trade date and contractual settlement date is greater than three business days (T+3) be subject to margining. The Proposed Amendments similarly define Covered Agency Securities by reference to the settlement cycles set forth in the TMPG Best Practices, which results in disparate margining treatment for TBA transactions based on their customary settlement cycles. While we generally agree with the TMPG Best Practices, for the reasons set forth below, we strongly believe that this aspect of the Margining Recommendation was ill-considered and will have a significantly adverse effect on the markets.

PIMCO supports a simplified approach wherein the margining requirement is applicable to all Covered Agency Securities with settlement cycles of greater than T+3. We believe that a split among various types of transactions on the basis of length of their customary settlement cycles is an unworkable distinction and should be dropped in favor of a more uniform rule that treats TBA transactions, Specified Pool transactions and CMOs similarly. A T+3 settlement cycle is the industry standard for the vast majority of fixed income securities (including mortgage pools). Our understanding is that the TMPG applied the greater than T+1 settlement cycle to TBAs, specified pool and ARM transactions because they believed this was the normal settlement cycle for these products. This is an inaccurate understanding, and therefore we think this error needs to be corrected to accurately match the normal settlement cycles of these products. In fact, specified pools and ARM transactions normally settle on a T+3 settlement cycle. Importantly, we are concerned that this mismatch will impede the liquidity of PIMCO's clients. Either the settlement cycles that include Covered Agency Securities need to match the settlement cycles of the spot market for those securities (from greater than T+1 to greater than T+3), or the settlement cycles of the spot markets should be moved to match the settlement cycles that include Covered Agency Securities (from T+3 to T+1).

As a result a number of market participants are likely to be driven out of this investment or incentivized to transact with banks that are *not* FINRA Members, thereby causing the market to become more consolidated among fewer larger players and reducing the liquidity of the TBA market. Also, because market participants may trade packaged transactions in these asset classes, we believe it is preferable that margin requirements be symmetrical for the various legs of the packaged transaction. In stark contrast, the simplified approach we recommend does not prevent market participants from agreeing bilaterally to margin transactions that settle on a T+1 or T+2 basis and therefore will not impose any additional systems or administrative burdens or costs on Members.

PIMCO supports the aim of the Proposed Amendments to mitigate the counterparty credit risk borne by participants in the TBA market and reduce the potential for systemic risk. Broadly

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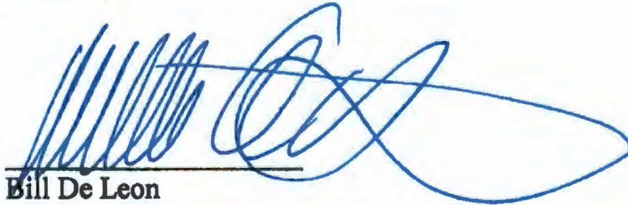
[2] Treasury Markets Practice Group, TMPG Releases Updates to Agency MBS Margining Recommendation, March 27, 2013 (*available at* www.newyorkfed.org/tmpg).

speaking, PIMCO agrees with the need to reduce counterparty exposure and has been an early adopter of numerous market practices to this end. In fact, PIMCO has documented and fully collateralized its trades significantly before the financial crisis. However, despite our strong stance on reduction of counterparty risk exposure, after having done our own internal analysis, we believe that the significant costs and possible harm to the market that is likely to result from disparate margining treatment for TBAs, Specified pool and CMO transactions significantly outweighs any possible reduction in systemic risk.

Further, while we recognize the need to have a unified approach to regulation of the TBA market and to avoid market fragmentation, we recommend that if, and to the extent that, either the TMPG or FINRA modifies the scope of inclusion of these instruments, the two organizations work together to harmonize their provisions.

PIMCO appreciates the opportunity to comment on the Proposed Amendments. Should you have any questions regarding our comments, please do not hesitate to call Bill De Leon at 949-720-7612 or Aaron Kim at 212-739-3567.

Sincerely,



Bill De Leon
Managing Director