

proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

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 email to rule-comments@sec.gov. Please include File Number SR–NASDAQ–2016–048 on the subject line.

Paper Comments

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090.

All submissions should refer to File Number SR–NASDAQ–2016–048. This file number should be included on the subject line if email 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 such filing also will be available for inspection and copying at the principal office of the Exchange. 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–

NASDAQ–2016–048, and should be submitted on or before May 6, 2016.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁷

Robert W. Errett,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–77579; File No. SR–FINRA–2015–036]

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 2 and Designation of a Longer Period for Commission Action on Proceedings To Determine Whether To Approve or Disapprove a Proposed Rule Change To Amend FINRA Rule 4210 (Margin Requirements) To Establish Margin Requirements for the TBA Market, as Modified by Amendment Nos. 1 and 2

April 11, 2016.

I. Introduction

On October 6, 2015, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”)¹ and Rule 19b–4 thereunder,² a proposed rule change to amend FINRA Rule 4210 (Margin Requirements) to establish margin requirements for covered agency transactions, also referred to, for purposes of this proposed rule change as the To Be Announced (“TBA”) market.

The proposed rule change was published for comment in the **Federal Register** on October 20, 2015.³ On November 10, 2015, FINRA extended the time period in which the Commission must approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change to January 15, 2016.⁴ The Commission

¹⁷ 17 CFR 200.30–3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b–4.

³ See Exchange Act Release No. 76148 (Oct. 14, 2015), 80 FR 63603 (Oct. 20, 2015) (File No. SR–FINRA–2015–036) (“Notice”).

⁴ See Extension No. 1, dated November 10, 2015. FINRA's extension of time for Commission action. The extension is available at http://www.finra.org/sites/default/files/rule_filing_file/SR-FINRA-2015-036-extension-1.pdf.

received 109 comment letters in response to the proposal.⁵ On January 13, 2016, FINRA responded to the comments and filed Amendment No. 1 to the proposal.⁶ On January 14, 2016, the Commission issued an order instituting proceedings pursuant to Section 19(b)(2)(B) of the Exchange Act⁷ to determine whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1. The Order Instituting Proceedings was published in the **Federal Register** on January 21, 2016.⁸ The Commission received 23 comment letters in response to the Order Instituting Proceedings.⁹

⁵ See Exchange Act Release No. 76908 (Jan. 14, 2016), 81 FR 3532 (Jan. 21, 2016) (Order Instituting Proceedings To Determine Whether To Approve or Disapprove Proposed Rule Change to Amend FINRA Rule 4210 (Margin Requirements), to Establish Margin Requirements for the TBA Market, as Modified by Partial Amendment No. 1) (“Order Instituting Proceedings”).

⁶ See Amendment No. 1, dated January 13, 2016 (“Amendment No. 1”). FINRA's responses to comments received and proposed amendments are included in Amendment No. 1.

⁷ 15 U.S.C. 78s(b)(2)(B) (if the Commission does not approve or disapprove a proposed rule change under Section 19(b)(2)(A) of the Exchange Act—*i.e.*, within 90 days of publication of notice of the filing of the proposed rule change in the **Federal Register**—the Commission shall institute proceedings to determine whether to approve or disapprove the proposed rule change).

⁸ See *supra* note 5.

⁹ See Letters from Matrix Applications, LLC, dated February 9, 2016 (“Matrix 2 Letter”); Tari Flannery, M&T Realty Capital Corporation, dated February 9, 2016 (“M&T 2 Realty Letter”); Holly MacDonald-Korth, JW Korth & Company, dated February 9, 2016 (“Korth Letter”); Chris Melton, Coastal Securities, dated February 10, 2016 (“Coastal 2 Letter”); Rodrigo Lopez, NorthMarq Capital Finance, L.L.C., dated February 10, 2016 (“NorthMarq 2 Letter”); Steve Wendel, CBRE, Inc., dated February 11, 2016 (“CBRE 2 Letter”); Tony Love, Forest City Capital Corporation, dated February 11, 2016 (“Forest City 3 Letter”); Robert Kirkwood, Lancaster Pollard Mortgage Company, dated February 11, 2016 (“Lancaster Pollard 2 Letter”); Mike Nicholas, Bond Dealers of America, dated February 11, 2016 (“BDA 2 Letter”); Blake Lanford, Walker & Dunlop, LLC, dated February 11, 2016 (“W&D 2 Letter”); Allen Riggs, Vining Sparks IBG, LP, dated February 11, 2016 (“Vining Sparks Letter”); John Gidman, Association of Institutional Investors, dated February 11, 2016 (“AII 2 Letter”); Christopher B. Killian, Securities Industry and Financial Markets Association, dated February 11, 2016 (“SIFMA 2 Letter”); Roderick D. Owens, Committee on Healthcare Financing, dated February 10, 2016 (“CHF 2 Letter”); Bruce Sandweiss, Gershman Mortgage, dated February 11, 2016 (“Gershman 3 Letter”); Timothy W. Cameron and Laura Martin, Securities Industry and Financial Markets Association, Asset Management Group, dated February 11, 2016 (“SIFMA AMG 2 Letter”); Mike McRobers, Prudential Mortgage Capital Company, dated February 11, 2016 (“Prudential 2 Letter”); James M. Cain, Sutherland Asbill & Brennan LLP (on behalf of Federal Home Loan Banks), dated February 11, 2016 (“Sutherland 2 Letter”); Carl B. Wilkerson, American Council of Life Insurers, dated February 11, 2016 (“ACLI 2 Letter”); David H. Stevens, Mortgage Bankers Association, dated February 11, 2016 (“MBA 2 Letter”); U.S. Senator Tom Cotton, dated February

Continued

March 21, 2016, FINRA responded to the comments and filed Amendment No. 2.¹⁰ The Commission is publishing this notice to solicit comments on Amendment No. 2 to the proposed rule change from interested persons and to extend to June 16, 2016 the time period in which the Commission must approve or disapprove the proposed rule change, as modified by Amendment Nos. 1 and 2.

II. Description of the Proposed Rule Change¹¹

In its filing, FINRA proposed amendments to FINRA Rule 4210 (Margin Requirements) to establish requirements for: (1) TBA transactions,¹² inclusive of adjustable rate mortgage (“ARM”) transactions; (2) Specified Pool Transactions;¹³ and (3) transactions in Collateralized Mortgage Obligations (“CMOs”),¹⁴ issued in conformity with a program of an agency¹⁵ or Government-Sponsored Enterprise (“GSE”),¹⁶ with forward settlement dates, (collectively, “Covered Agency Transactions,” also referred to for purposes of this filing, as the “TBA market”).

FINRA stated that most trading of agency and GSE Mortgage-Backed Security (“MBS”) takes place in the TBA market, which is characterized by transactions with forward settlements as long as several months past the trade

date.¹⁷ FINRA stated that historically, the TBA market is one of the few markets where a significant portion of activity is unmarginated, thereby creating a potential risk arising from counterparty exposure. With a view to this gap between the TBA market versus other markets, FINRA noted the TPMG recommended standards (the “TPMG best practices”) regarding the margining of forward-settling agency MBS transactions.¹⁸ FINRA stated that the TPMG best practices are recommendations and as such currently are not rule requirements. FINRA’s present requirements do not address the TBA market generally.¹⁹

Accordingly, to establish margin requirements for Covered Agency Transactions, FINRA proposed to redesignate current paragraph (e)(2)(H) of Rule 4210 as new paragraph (e)(2)(I), to add new paragraph (e)(2)(H) to Rule 4210, to make conforming revisions to paragraphs (a)(13)(B)(i), (e)(2)(F), (e)(2)(G), (e)(2)(I), as redesignated by the rule change, and (f)(6), and to add to the rule new Supplementary Materials .02 through .05. The proposed rule change is described in further detail below.

A. Proposed FINRA Rule 4210(e)(2)(H) (Covered Agency Transactions)²⁰

The core requirements of the proposed rule change are set forth in new paragraph (e)(2)(H) of FINRA Rule 4210.

1. Definition of Covered Agency Transactions (Proposed FINRA Rule 4210(e)(2)(H)(i)c)²¹

Proposed paragraph (e)(2)(H)(i)c. of the rule would define Covered Agency Transactions to mean:

- TBA transactions, as defined in FINRA Rule 6710(u), inclusive of ARM transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;
- Specified Pool Transactions, as defined in FINRA Rule 6710(x), for which the difference between the trade date and contractual settlement date is greater than one business day; and
- CMOs, as defined in FINRA Rule 6710(dd), issued in conformity with a program of an agency, as defined in FINRA Rule 6710(k), or a GSE, as defined in FINRA Rule 6710(n), for which the difference between the trade date and contractual settlement date is greater than three business days.

2. Other Key Definitions Established by the Proposed Rule Change (Proposed FINRA Rule 4210(e)(2)(H)(i))²²

In addition to Covered Agency Transactions, the proposed rule change would establish the following key definitions for purposes of new paragraph (e)(2)(H) of Rule 4210:

- The term “bilateral transaction” means a Covered Agency Transaction that is not cleared through a registered clearing agency as defined in paragraph (f)(2)(A)(xxviii) of Rule 4210;
- The term “counterparty” means any person that enters into a Covered Agency Transaction with a member and includes a “customer” as defined in paragraph (a)(3) of Rule 4210;
- The term “deficiency” means the amount of any required but uncollected maintenance margin and any required but uncollected mark to market loss;
- The term “gross open position” means, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty’s contracts with the member and which the counterparty intends to deliver;
- The term “maintenance margin” means margin equal to two percent of

¹¹ 2016 (“Senator Cotton Letter”); Robert Tirschwell, Brean Capital, LLC, dated February 17, 2016 (“Brean Capital 3 Letter”); Lauren Sarper, Prudential Financial, Inc., dated March 1, 2016 (“Prudential 3 Letter”).

¹⁰ See Amendment No. 2, dated March 21, 2016 (“Amendment No. 2”). FINRA’s responses to comments received on the Order Instituting Proceedings and proposed amendments in Amendment No. 1 are included in Amendment No. 2. The text of Amendment No. 2 is available on FINRA’s Web site at <http://www.finra.org>, at the principal office of FINRA, and at the Commission’s Public Reference Room.

¹¹ The proposed rule change, as modified by Amendment No. 1, as described in this Item II, is excerpted, in part, from the Notice, which was substantially prepared by FINRA, and the Order Instituting Proceedings. See *supra* notes 3 and 5. Amendment No. 2 is described in section II.D. below.

¹² See FINRA Rule 6710(u) (defining TBA to mean a transaction in an Agency Pass-Through Mortgage-Backed Security (“MBS”) or a Small Business Administration (“SBA”) Backed Asset-Backed Security (“ABS”) where the parties agree that the seller will deliver to the buyer a pool or pools of a specified face amount and meeting certain other criteria but the specific pool or pools to be delivered at settlement is not specified at the Time of Execution, and includes TBA transactions for good delivery and TBA transactions not for good delivery).

¹³ See FINRA Rule 6710(x).

¹⁴ See FINRA Rule 6710(dd).

¹⁵ See FINRA Rule 6710(k).

¹⁶ See FINRA Rule 6710(n) and 2 U.S.C. 622(8).

¹⁷ See, e.g., James Vickery & Joshua Wright, TBA Trading and Liquidity in the Agency MBS Market, Federal Reserve Bank of New York (“FRBNY”) Economic Policy Review, May 2013, available at, <https://www.newyorkfed.org/medialibrary/media/research/epr/2013/1212vick.pdf>; see also, SEC’s Staff Report, Enhancing Disclosure in the Mortgage-Backed Securities Markets, January 2003, available at, <https://www.sec.gov/news/studies/mortgagebacked.htm>; see also, Treasury Market Practices Group (“TPMG”), Margining in Agency MBS Trading, November 2012, available at, https://www.newyorkfed.org/medialibrary/microsites/tmpg/files/margining_tmpg_11142012.pdf (the “TPMG Report”). The TPMG is a group of market professionals that participate in the TBA market and is sponsored by the FRBNY.

¹⁸ See TPMG, Best Practices for Treasury, Agency, Debt, and Agency Mortgage-Backed Securities Markets, revised June 10, 2015, available at, https://www.newyorkfed.org/medialibrary/microsites/tmpg/files/TPMG_June%202015_Best%20Practices.

¹⁹ See Interpretations/01 through/08 of FINRA Rule 4210(e)(2)(F), available at, <http://www.finra.org/web/groups/industry/@ip/@reg/@rules/documents/industry/p122203.pdf>. Such guidance references TBAs largely in the context of Government National Mortgage Association (“GNMA”) securities. The modern TBA market is much broader than GNMA securities.

²⁰ This section describes the proposed rule change prior to the proposed amendments in Amendment No. 2, which are described in section II.D. below.

²¹ See *supra* notes 3 and 5; see also, Exhibit 5 in Amendment No. 1, text of proposed rule change, as modified by Amendment No. 1.

²² See *supra* notes 3 and 5; see also, Exhibit 5 in Amendment No. 1, text of proposed rule change, as modified by Amendment No. 1.

the contract value of the net long or net short position, by CUSIP, with the counterparty;

- The term “mark to market loss” means the counterparty’s loss resulting from marking a Covered Agency Transaction to the market;
- The term “mortgage banker” means an entity, however organized, that engages in the business of providing real estate financing collateralized by liens on such real estate;
- The term “round robin” trade means any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer; and
- The term “standby” means contracts that are put options that trade over-the-counter (“OTC”), as defined in paragraph (f)(2)(A)(xxvii) of Rule 4210, with initial and final confirmation procedures similar to those on forward transactions.

3. Requirements for Covered Agency Transactions (Proposed FINRA Rule 4210(e)(2)(H)(ii))²³

The specific requirements that would apply to Covered Agency Transactions are set forth in proposed paragraph (e)(2)(H)(ii). These requirements would address the types of counterparties that are subject to the proposed rule, risk limit determinations, specified exceptions from the proposed margin requirements, transactions with exempt accounts,²⁴ transactions with non-exempt accounts, the handling of de minimis transfer amounts, and the treatment of standbys.

• Counterparties Subject to the Rule

Paragraph (e)(2)(H)(ii)a. of the proposed rule provides that all Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, are subject to the provisions of paragraph (e)(2)(H) of the rule. However, paragraph (e)(2)(H)(ii)a.1. of the proposed rule provides that with respect to Covered Agency Transactions with any counterparty that is a Federal banking agency, as defined in 12 U.S.C. 1813(z) under the Federal Deposit Insurance Act, central bank, multinational central

bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b., as discussed below.

In Amendment No. 1, FINRA proposed to add to FINRA Rule 4210 paragraph (e)(2)(H)(ii)a.2. to provide that a member may elect not to apply the margin requirements of paragraph (e)(2)(H) of the rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided that: (1) Such securities are issued in conformity with a program of an Agency, as defined in FINRA Rule 6710(k), or a GSE, as defined in FINRA Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade; and (2) the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b. of Rule 4210.²⁵

• Risk Limits

Paragraph (e)(2)(H)(ii)b. of the rule provides that members that engage in Covered Agency Transactions with any counterparty shall make a determination in writing of a risk limit for each such counterparty that the member shall enforce. The rule provides that the risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member’s written risk policies and procedures. Further, in connection with risk limit determinations, the proposed rule establishes new Supplementary Material .05. The new Supplementary Material provides that, for purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of the rule:

- If a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level, except with respect to any account or group of commonly controlled accounts whose assets managed by that investment adviser

constitute more than 10 percent of the investment adviser’s regulatory assets under management as reported on the investment adviser’s most recent Form ADV;

- Members of limited size and resources that do not have a credit risk officer or credit risk committee may designate an appropriately registered principal to make the risk limit determinations;
- The member may base the risk limit determination on consideration of all products involved in the member’s business with the counterparty, provided the member makes a daily record of the counterparty’s risk limit usage; and
- A member shall consider whether the margin required pursuant to the rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements.

Exceptions From the Proposed Margin Requirements: (1) Registered Clearing Agencies; (2) Gross Open Positions of \$2.5 Million or Less in Aggregate

Paragraph (e)(2)(H)(ii)c. provides that the margin requirements specified in paragraph (e)(2)(H) of the rule shall not apply to:

- Covered Agency Transactions that are cleared through a registered clearing agency, as defined in FINRA Rule 4210(f)(2)(A)(xxviii), and are subject to the margin requirements of that clearing agency; and
- any counterparty that has gross open positions in Covered Agency Transactions with the member amounting to \$2.5 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a Delivery Versus Payment (“DVP”) basis or for cash; provided, however, that such exception from the margin requirements shall not apply to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in FINRA Rule 6710(z),²⁶ or round robin trades, or that uses other financing techniques for its Covered Agency Transactions.

Transactions With Exempt Accounts

Paragraph (e)(2)(H)(ii)d. of the proposed rule provides that, on any net long or net short position, by CUSIP, resulting from bilateral transactions

²³ This section describes the proposed rule change prior to the proposed amendments in Amendment No. 2, which are described in section II.D. below.

²⁴ The term “exempt account” is defined under FINRA Rule 4210(a)(13). FINRA is proposing a conforming revision to paragraph (a)(13)(B)(i) so that the phrase “for purposes of paragraphs (e)(2)(F) and (e)(2)(G)” would read “for purposes of paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H).” See *supra* note 5.

²⁵ See Exhibit 4 and Exhibit 5 in Amendment No. 1. Proposed Rule 4210(e)(2)(H)(ii)b. sets forth the rule’s requirements as to written risk limits. See *also supra* notes 5 and 6.

²⁶ See FINRA Rule 6710(z).

with a counterparty that is an exempt account, no maintenance margin shall be required. However, the rule provides that such transactions must be marked to the market daily and the member must collect any net mark to market loss, unless otherwise provided under paragraph (e)(2)(H)(ii)f. The rule provides that if the mark to market loss is not satisfied by the close of business on the next business day after the business day on which the mark to market loss arises, the member shall be required to deduct the amount of the mark to market loss from net capital as provided in Exchange Act Rule 15c3-1 until such time the mark to market loss is satisfied. The rule requires that if such mark to market loss is not satisfied within five business days from the date the loss was created, the member must promptly liquidate positions to satisfy the mark to market loss, unless FINRA has specifically granted the member additional time. Under the rule, members may treat mortgage bankers that use Covered Agency Transactions to hedge their pipeline of mortgage commitments as exempt accounts for purposes of paragraph (e)(2)(H) of this Rule.

Transactions With Non-Exempt Accounts

Paragraph (e)(2)(H)(ii)e. of the rule provides that, on any net long or net short position, by CUSIP, resulting from bilateral transactions with a counterparty that is not an exempt account, maintenance margin, plus any net mark to market loss on such transactions, shall be required margin, and the member shall collect the deficiency, as defined in paragraph (e)(2)(H)(i)d. of the rule, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of the rule. The rule provides that if the deficiency is not satisfied by the close of business on the next business day after the business day on which the deficiency arises, the member shall be required to deduct the amount of the deficiency from net capital as provided in Exchange Act Rule 15c3-1 until such time the deficiency is satisfied. Further, the rule provides that if such deficiency is not satisfied within five business days from the date the deficiency was created, the member shall promptly liquidate positions to satisfy the deficiency, unless FINRA has specifically granted the member additional time.

The rule provides that no maintenance margin is required if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding

the trade date for such transaction and the customer regularly settles its Covered Agency Transactions on a DVP basis or for cash; provided, however, that such exception from the required maintenance margin shall not apply to a non-exempt account that, in its transactions with the member, engages in dollar rolls, as defined in FINRA Rule 6710(z), or round robin trades, as defined in proposed FINRA Rule 4210(e)(2)(H)(i)i., or that uses other financing techniques for its Covered Agency Transactions.

De Minimis Transfer Amounts

Paragraph (e)(2)(H)(ii)f. of the rule provides that any deficiency, as set forth in paragraph (e)(2)(H)(ii)e. of the rule, or mark to market losses, as set forth in paragraph (e)(2)(H)(ii)d. of the rule, with a single counterparty shall not give rise to any margin requirement, and as such need not be collected or charged to net capital, if the aggregate of such amounts with such counterparty does not exceed \$250,000 (“the de minimis transfer amount”). The proposed rule provides that the full amount of the sum of the required maintenance margin and any mark to market loss must be collected when such sum exceeds the de minimis transfer amount.

Unrealized Profits; Standbys

Paragraph (e)(2)(H)(ii)g. of the rule provides that unrealized profits in one Covered Agency Transaction position may offset losses from other Covered Agency Transaction positions in the same counterparty’s account and the amount of net unrealized profits may be used to reduce margin requirements. With respect to standbys, only profits (in-the-money amounts), if any, on long standbys shall be recognized.

*B. Conforming Amendments to FINRA Rule 4210(e)(2)(F) (Transactions With Exempt Accounts Involving Certain “Good Faith” Securities) and FINRA Rule 4210(e)(2)(G) (Transactions With Exempt Accounts Involving Highly Rated Foreign Sovereign Debt Securities and Investment Grade Debt Securities)*²⁷

The proposed rule change makes a number of revisions to paragraphs (e)(2)(F) and (e)(2)(G) of FINRA Rule 4210:²⁸

- The proposed rule change revises the opening sentence of paragraph

²⁷ This section describes the proposed rule change prior to the proposed amendments in Amendment No. 2, which are described in section II.D. below.

²⁸ See *supra* notes 3 and 5; see also, Exhibit 5 in Amendment No. 1, text of proposed rule change, as modified by Amendment No. 1.

(e)(2)(F) to clarify that the paragraph’s scope does not apply to Covered Agency Transactions as defined pursuant to new paragraph (e)(2)(H). Accordingly, as amended, paragraph (e)(2)(F) states: “Other than for Covered Agency Transactions as defined in paragraph (e)(2)(H) of this Rule . . .” For similar reasons, the proposed rule change revises paragraph (e)(2)(G) to clarify that the paragraph’s scope does not apply to a position subject to new paragraph (e)(2)(H) in addition to paragraph (e)(2)(F) as the paragraph currently states. As amended, the parenthetical in the opening sentence of the paragraph states: “[O]ther than a position subject to paragraph (e)(2)(F) or (e)(2)(H) of this Rule).”

- Current, pre-revision paragraph (e)(2)(H)(i) provides that members must maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraphs (e)(2)(F) and (e)(2)(G) of the rule which shall be made available to FINRA upon request. The proposed rule change places this language in paragraphs (e)(2)(F) and (e)(2)(G) and deletes it from its current location. Accordingly, FINRA proposes to move to paragraphs (e)(2)(F) and (e)(2)(G): “Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to [this paragraph], which shall be made available to FINRA upon request.” Further, FINRA proposes to add to each: “The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member’s written risk policies and procedures.” FINRA believes Amendment No. 1 makes the risk limit determination language in paragraphs (e)(2)(F) and (e)(2)(G) more congruent with the corresponding language proposed for new paragraph (e)(2)(H) of the rule.

- The proposed rule change revises the references in paragraphs (e)(2)(F) and (e)(2)(G) to the limits on net capital deductions as set forth in current paragraph (e)(2)(H) to read “paragraph (e)(2)(I)” in conformity with that paragraph’s redesignation pursuant to the rule change.

*C. Redesignated Paragraph (e)(2)(I) (Limits on Net Capital Deductions)*²⁹

Under current paragraph (e)(2)(H) of FINRA Rule 4210, in brief, a member must provide prompt written notice to FINRA and is prohibited from entering

²⁹ This section describes the proposed rule change prior to the proposed amendments in Amendment No. 2, which are described in section II.D. below.

into any new transactions that could increase the member's specified credit exposure if net capital deductions taken by the member as a result of marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G), over a five day business period, exceed: (1) For a single account or group of commonly controlled accounts, five percent of the member's tentative net capital (as defined in Exchange Act Rule 15c3-1); or (2) for all accounts combined, 25 percent of the member's tentative net capital (again, as defined in Exchange Act Rule 15c3-1). As discussed above, the proposed rule change redesignates current paragraph (e)(2)(H) of the rule as paragraph (e)(2)(I), deletes current paragraph (e)(2)(H)(i), and makes conforming revisions to paragraph (e)(2)(I), as redesignated, for the purpose of clarifying that the provisions of that paragraph are meant to include Covered Agency Transactions as set forth in new paragraph (e)(2)(H). In addition, the proposed rule change clarifies that de minimis transfer amounts must be included toward the five percent and 25 percent thresholds as specified in the rule, as well as amounts pursuant to the specified exception under paragraph (e)(2)(H) for gross open positions of \$2.5 million or less in aggregate.

Redesignated paragraph (e)(2)(I) of the rule provides that, in the event that the net capital deductions taken by a member as a result of deficiencies or marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) of the rule (exclusive of the percentage requirements established thereunder), plus any mark to market loss as set forth under paragraph (e)(2)(H)(ii)d. of the rule and any deficiency as set forth under paragraph (e)(2)(H)(ii)e. of the rule, and inclusive of all amounts excepted from margin requirements as set forth under paragraph (e)(2)(H)(ii)c.2. of the rule or any de minimis transfer amount as set forth under paragraph (e)(2)(H)(ii)f. of the rule, exceed:³⁰

- For any one account or group of commonly controlled accounts, 5 percent of the member's tentative net capital (as such term is defined in Exchange Act Rule 15c3-1), or
- for all accounts combined, 25 percent of the member's tentative net capital (as such term is defined in Exchange Act Rule 15c3-1), and,
- such excess as calculated in paragraphs (e)(2)(I)(i)a. or b. of the rule continues to exist on the fifth business day after it was incurred,

³⁰ See *supra* notes 3 and 5; see also, Exhibit 5 in Amendment No. 1, text of proposed rule change, as modified by Amendment No. 1.

The member must give prompt written notice to FINRA and shall not enter into any new transaction(s) subject to the provisions of paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of the rule that would result in an increase in the amount of such excess under, as applicable, paragraph (e)(2)(I)(i) of the rule.

In Amendment No. 1, FINRA proposed that the risk limit determination requirements as set forth in paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H) of Rule 4210 and proposed Supplementary Material .05 become effective six months from the date the proposed rule change is approved by the Commission.³¹ FINRA proposed that the remainder of the proposed rule change become effective 18 months from the date the proposed rule change is approved by the Commission.³²

D. Amendment No. 2³³

In Amendment No. 2, FINRA responded to comments received on the Order Instituting Proceedings³⁴ and, in response to comments, proposes to amend the rule language in paragraph (e)(2)(H)(ii)a.2. In Amendment No. 2, FINRA is also proposing a conforming formatting revision to proposed paragraph (e)(2)(H)(ii)a.1. of the rule.

1. Multifamily and Project Loan Securities

Commenters expressed support for the proposed exception for multifamily and project loan securities as set forth in proposed paragraph (e)(2)(H)(ii)a.2. in Amendment No. 1.³⁵ Several commenters asked that FINRA provide guidance to ensure that the risk limit determinations as proposed do not disrupt existing practices or arrangements between mortgage bankers and member firms, are not inconsistently or arbitrarily applied, or are not otherwise interpreted as requiring member firms to impose margin requirements with respect to transactions in the specified products, and called for care in the implementation of the requirement.³⁶ One commenter asked FINRA to state

³¹ See *supra* notes 5 and 6.

³² See *supra* note 5.

³³ See *supra* note 10. With the exception of comments received related to multifamily housing and project loan securities, FINRA's responses to comments received on the Order Instituting Proceedings are discussed in section III. below. See *supra* note 5.

³⁴ See *supra* note 5.

³⁵ See CBRE 2 Letter, Forest City 3 Letter, Gershman 3 Letter, Lancaster 2 Letter, M&T Realty 2 Letter, MBA 2 Letter, NorthMarq 2 Letter, and W&D 2 Letter.

³⁶ See CBRE 2 Letter, Forest City 3 Letter, Gershman 3 Letter, Lancaster 2 Letter, MBA 2 Letter, and W&D 2 Letter.

that there are no conditions at this time that would require margining with respect to such transactions.³⁷ Some commenters said that FINRA should engage in various forms of communication or outreach to clarify the rule.³⁸ Other commenters suggested FINRA clarify the intent of the proposed exception by changing "a member may elect not to apply the margin requirements" to "a member is not required to apply the margin requirements."³⁹ Some commenters expressed concern that, because of changes in nomenclature or other future action by the agencies or GSEs, some securities that have the characteristics of multifamily and project loan securities may not be documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, and may thereby inadvertently not be included within the proposed exception.⁴⁰ These commenters proffered language so that the scope of the proposed exception would include other multifamily and project loan securities with "substantially similar" characteristics issued in conformity with a program or an agency or GSE.

Some commenters opposed the modified rule language in Amendment No. 1 on grounds that the rule should not permit members discretion to impose margin requirements as to multifamily and project loan securities and that such securities should be fully exempted from the proposed rule's application.⁴¹ One commenter said that FINRA should confirm that good faith deposits provide sufficient protection to broker-dealers involved in multifamily and project loan securities transactions, that FINRA did not do analysis of good faith deposits, that giving broker-dealers discretion to impose margin in such transactions protects the broker-dealer but not other parties to the trade, and that in the presence of margin, lenders in multifamily projects will not be able to structure their mortgage costs confidently.⁴² Another commenter said that multifamily and project loan securities should be fully exempted from the proposed rule because such securities do not present systemic risk.⁴³ This commenter said that there are significant protections in place to

³⁷ See Forest City 3 Letter.

³⁸ See Forest City 3 Letter and W&D 2 Letter.

³⁹ See MBA 2 Letter and Lancaster 2 Letter.

⁴⁰ See Forest City 3 Letter, Gershman 3 Letter, Lancaster 2 Letter, and MBA 2 Letter.

⁴¹ See CHF 2 Letter and Prudential 2 Letter.

⁴² See CHF 2 Letter.

⁴³ See Prudential 2 Letter.

insulate purchasers of such securities from credit and counterparty risk, that under the proposed rule margin would depend upon a broker-dealer's risk limit determination, that there would be no objective standard for when margin would be required, and that FINRA offered no clear rationale for including multifamily and project loan securities in any margining regime.⁴⁴ The commenter proffered language to fully exempt multifamily and project loan securities from the rule's application and suggested that additional language be added to enable broker-dealers and sellers of multifamily and project loan securities to agree contractually on appropriate margin and to count good faith deposits toward margin.⁴⁵

In response, FINRA is sensitive to commenters' concerns that the proposed rule not disrupt business activity. FINRA stated in Amendment No. 1 that FINRA is not proposing at this time to require that members apply the proposed margin requirements⁴⁶ to multifamily and project loan securities, subject to the conditions as specified in proposed paragraph (e)(2)(H)(ii)a.2. of Rule 4210. In the interest of further clarity, FINRA proposes in Amendment No. 2 to revise the phrase "a member may elect not to apply the margin requirements . . ." in paragraph (e)(2)(H)(ii)a.2. to read "a member is not required to apply the margin requirements . . ." ⁴⁷ However, while the rule is not intended to require margin as to transactions in multifamily and project loan securities, neither is it intended to prevent members from imposing margin. As FINRA stated in Amendment No. 1, the proposal imposes on members the requirement to make and enforce risk limits as to counterparties in multifamily and project loan securities to help ensure that members are properly monitoring their risk. The rule presumes that risk limits will be a tool that members may employ to exercise sound discretion as to the management of their business. Members need, and under FINRA rules have, discretion to impose margin over and above the requirements under the rules.⁴⁸ Though it is possible that

members' application of the risk limit requirements may lead to different determinations among members as to multifamily and project loan securities, FINRA notes that members and their counterparties have been transacting in these products for a considerable time and they are well understood to the industry. FINRA will consider further guidance as needed.

FINRA notes the concern that, owing to changes in nomenclature or other future action by the agencies or GSEs, some securities that have the characteristics of multifamily and project loan securities may not be documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, and may thereby inadvertently fall outside the scope of the exception proposed under paragraph (e)(2)(H)(ii)a.2. In response, in Amendment No. 2, FINRA proposes to revise proposed paragraph (e)(2)(H)(ii)a.2.A. to add the phrase "or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory Notice or similar communication." As such, proposed paragraph (e)(2)(H)(ii)a.2.A. as revised would read: ". . . such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade, or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory Notice or similar communication . . ." ⁴⁹ FINRA believes that the revised language should help promote clarity in the rule's application by ensuring that FINRA has the ability to efficiently include within the scope

paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of the rule, a member "shall consider whether the margin required pursuant to this Rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements." See Exhibit 5 in Amendment No. 2.

⁴⁹ See proposed FINRA Rule (e)(2)(H)(ii)a.2.A. in Exhibit 4 in Amendment No. 2.

of the proposed exception, by Regulatory Notice or similar communication, any multifamily and project loan securities, consistent with the rule's intent, that may otherwise inadvertently be omitted.

In response to comments, FINRA believes that a complete exemption for multifamily and project loan securities, not only with respect to the margin requirements, but also the obligation of members to make and enforce risk limits, would not serve the interests of sound regulation.⁵⁰ As already noted above and in Amendment No. 1, the rule's risk limit provisions are designed as an appropriately tailored requirement to ensure that members are properly managing their risk. It would undercut the core purposes of the rule to create classes of products within the Covered Agency Transactions category where such monitoring is not required. FINRA does not believe that a separate analysis of good faith deposits is necessary given that, as more fully set forth in Amendment No. 1, FINRA took note of the provision of good faith deposits by the borrower to the lender, among other characteristics of multifamily and project loan securities, in considering the exception set forth in the proposed rule. Nor does FINRA propose to introduce into the rule language providing for negotiation of margin or for recognition of good faith deposits. FINRA does not object to parties engaging in negotiation, provided the margin requirements as set forth under the rule are met. FINRA does not believe it is necessary to separately set forth a rationale for regulation of multifamily and project loan securities for purposes of Amendment No. 2 given that, in the original filing, FINRA set forth in full the rationale for regulating Covered Agency Transactions and, in Amendment No. 1, FINRA specifically addressed its proposed approach to multifamily and project loan securities.⁵¹

2. Other

In Amendment No. 2 (not in response to a comment), FINRA has made a conforming formatting revision to proposed paragraph (e)(2)(H)(ii)a.1. of the rule so that the phrase "paragraph (e)(2)(H)(ii)b; and . . ." reads "paragraph (e)(2)(H)(ii)b.; and . . ." ⁵²

⁵⁰ See CHF 2 Letter, Prudential 2 Letter and Prudential 3 Letter.

⁵¹ See *supra* notes 3 and 5.

⁵² See Exhibit 4 in Amendment No. 2.

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ See *supra* note 5. The "proposed margin requirements" refers to the margin requirements as to Covered Agency Transactions as set forth in the original filing, as modified by Amendment Nos. 1 and 2. Products or transactions that are outside the scope of Covered Agency Transactions are otherwise subject to the requirements of FINRA Rule 4210, as applicable.

⁴⁷ See proposed FINRA Rule (e)(2)(H)(ii)a.2. in Exhibit 4 in Amendment No. 2.

⁴⁸ FINRA noted that proposed Supplementary Material .05(a)(4) provides that, for purposes of

III. Summary of Comments and FINRA's Responses⁵³

As noted above, the Commission received 23 comment letters on the proposed rule change, as modified by Amendment No. 1.⁵⁴ These comments and FINRA's responses to the comments are summarized below.⁵⁵

A. Impact and Costs of the Proposal (Other Than With Respect to Multifamily and Project Loan Securities)

Commenters expressed concerns regarding the proposed rule's potential impact on the market and the costs of implementing the requirements.⁵⁶ One commenter believed that the comment period has been inadequate and that FINRA did not quantify the proposal's burdens on all broker-dealers and market participants.⁵⁷ This commenter said that FINRA's economic impact statement in the proposed rule change was deficient.⁵⁸ Another commenter said FINRA should consider the comprehensive costs and burdens of the proposal vis-à-vis the cost of alternatives recommended by the commenter.⁵⁹ This commenter also said its members have observed the shifting of TBA market business to non-FINRA members, who have a significant competitive advantage over FINRA-regulated broker-dealers.⁶⁰ Further, this commenter said that the proposal would result in a reduction in the number of investors willing to invest in TBA market products, and that it would be willing to work with FINRA to supply market or economic information within the access of its members.⁶¹ One commenter said that the costs of the proposal would be considerable, that implementation work would be extensive in executing or renegotiating Master Securities Forward Transaction Agreements ("MSFTAs"), and that requirements such as maintenance margin and position liquidation would impose additional costs.⁶² Another commenter said the proposal would have an inequitable impact on competition between small dealers and large dealers, that many small dealers would exit the TBA market rather than implement the rule, that large firms might not be willing to deal with small

firms, and that liquidity for small firms would be negatively affected.⁶³ A different commenter said that many firms that pose no systemic risk potential and do only a moderate amount of mortgage business may choose to exit the marketplace rather than comply with the rule, which would further harm liquidity in the U.S. fixed income market, with possible adverse effects on the U.S. mortgage market, and that the proposal would require small-to-medium sized dealers to execute margin agreements with all their mortgage counterparties.⁶⁴ This commenter said that large investment managers would be unlikely to agree to execute margin agreements with an unlimited number of counterparties.⁶⁵ Similarly, another commenter said that the proposal would exacerbate a concentration of activity in the largest active firms and that the rule would impose burdens on investment managers, who would enter into margin agreements only with the largest dealer counterparties, thereby negatively impacting smaller firms.⁶⁶ One commenter stated that as a result of the proposal only FINRA members would be required to impose margin requirements and that non-FINRA member banks that currently are following the TMPG best practices may choose not to do so.⁶⁷ This commenter said that smaller members would exit the market rather than implement the required margin.⁶⁸ Similarly, another commenter said large firms that follow the TMPG best practices already have margining mechanisms in place but that smaller firms would be disproportionately affected by the proposal because more TBA market transactions will migrate to non-FINRA member banks.⁶⁹ This commenter said the proposal would lead to fewer competitors and higher costs for consumers.⁷⁰

Some commenters proffered estimates as to the cost of implementing the proposal.⁷¹ A commenter said the proposal would require FINRA members of all sizes, regardless of how active they are in the market, to hire new personnel to comply with the rule.⁷² This commenter said that hiring three new employees to staff a new margin department would cost an estimated \$150,000 per employee per year, that

third party vendor technology could cost \$625,000 in licensing fees in the first year, and that a competing vendor solution would cost as much as \$875,000 over the first two years of use.⁷³ Another commenter stated that buying or licensing a system to comply with the rule would cost over \$100,000, that there would be costs for development resources, and that cost for implementation could run to \$250,000 or more.⁷⁴ This commenter said that third party pricing would be between \$150,000 and \$400,000 per year depending on the vendor, that two or maybe three employees would be needed, and that this could cost an additional \$200,000 per year.⁷⁵ This commenter said the ongoing cost of the proposal would be in the \$300,000 to \$400,000 range.⁷⁶

In response, FINRA addressed the commenters' concerns in the original filing and in Amendment No. 1.⁷⁷ In the original filing, FINRA set forth an extensive analysis of the proposal's potential impact.⁷⁸ FINRA addressed, among other things, the proposal's potential impact on mortgage bankers,⁷⁹ broker-dealers, including smaller firms,⁸⁰ and retail customers and consumers, and presented quantitative analysis of trade and account data.⁸¹ As FINRA discussed in the original filing, and again in response to comments in Amendment No. 1, FINRA noted that there will likely be direct and indirect costs associated with the rule change, and that firms will be impacted.⁸² FINRA considered and analyzed alternatives.⁸³ FINRA also set forth the need for the rule change, including the need to manage the risk to members extending credit and to help maintain a properly functioning retail mortgage market even in stressed market conditions.⁸⁴ FINRA noted that comment on the proposed rule change has been solicited on three occasions: First in response to *Regulatory Notice 14-02*;⁸⁵ second in response to the original filing; and third in response to the Order Instituting Proceedings. In three rounds of comment, with a total of

⁷³ *Id.*

⁷⁴ See Vining Sparks Letter.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ See *supra* notes 3 and 5.

⁷⁸ See Notice, 80 FR 63603, 63611 through 63615.

⁷⁹ See Notice, 80 FR 63603, 63611.

⁸⁰ See Notice, 80 FR 63603, 63612 through 63613.

⁸¹ See Notice, 80 FR 63603, 63611 through 63614.

⁸² See Notice, 80 FR 63603, 63611; see also *supra* notes 5 and 6.

⁸³ See Notice, 80 FR 63603, 63614 through 63615.

⁸⁴ See Notice, 80 FR 63603, 63604, 63611, 63613.

⁸⁵ See *Regulatory Notice 14-02* (January 2014) (FINRA Requests Comment on Proposed Amendments to FINRA Rule 4210 for Transactions in the TBA Market).

⁵³ Comments related to the multifamily housing and project loan securities are addressed in section II.D. above.

⁵⁴ See *supra* notes 5 and 6.

⁵⁵ See *supra* note 10.

⁵⁶ See ACLI 2 Letter, AII 2 Letter, BDA 2 Letter, Coastal 2 Letter, Senator Cotton Letter, Korth Letter, SIFMA AMG 2 Letter, and Vining Sparks Letter.

⁵⁷ See ACLI 2 Letter.

⁵⁸ *Id.*

⁵⁹ See SIFMA 2 Letter.

⁶⁰ *Id.*

⁶¹ *Id.*

⁶² See AII 2 Letter.

⁶³ See Korth Letter.

⁶⁴ See Senator Cotton Letter.

⁶⁵ *Id.*

⁶⁶ See BDA 2 Letter.

⁶⁷ See Coastal 2 Letter.

⁶⁸ *Id.*

⁶⁹ See Vining Sparks Letter.

⁷⁰ *Id.*

⁷¹ See BDA 2 Letter and Vining Sparks Letter.

⁷² See BDA 2 Letter.

132 individual letter comments,⁸⁶ a handful of commenters have provided in the public record specific, quantified estimates as to the potential cost of implementing the proposed rule change.⁸⁷ FINRA notes commenters concerns as to the quantitative analysis.⁸⁸ However, FINRA further notes that a key purpose of the comment process is to supply the public record with specific information for regulators to consider in the development of rulemaking. FINRA notes that it is of little assistance to the comment process to state in a comment letter that the pertinent information is available, and then not provide such information in the letter for public review.

In response to comments, FINRA has engaged in ongoing discussions with various market participants and providers to understand the potential regulatory costs of compliance with the proposed rule.⁸⁹ Similar to the original filing,⁹⁰ FINRA believes the commenters' estimates fall toward the higher end of the cost range for building, upgrading, maintaining, licensing or outsourcing the necessary systems and hiring of necessary staff. FINRA understands that estimates will vary depending on the size and business model of a firm, and the extent of its current and anticipated involvement in TBA market transactions.

As a result of these ongoing discussions, FINRA understands that some firms have been transacting in the TBA market for years and margining has been a common practice due to the TMPG best practices or prudent counterparty risk management practices at these firms. These firms already have the technology and staffing in place for collateral management in their repo, swap and OTC derivatives transactions and would only have to build into their current systems the exceptions provided for under the proposed rule.⁹¹ Costs associated with such enhancements or additions to the current systems should vary based on the scalability and flexibility of such systems. For instance, sources at one firm estimated that it

required approximately 60 hours of programming time, at a cost of approximately \$5,000, to build systems to track margin obligations consistent with the TMPG best practices. The same firm did not plan to hire additional staff to track margin obligations pursuant to the proposed rule; however, another firm estimated that its total annual costs to comply with the proposed requirements could run from \$60,000 to \$100,000, including both staffing and technology costs.

FINRA understands that there are various technology solutions and service providers for firms that have relatively less engagement in TBA market transactions, and therefore would need more affordable and flexible products. One service provider to firms noted that costs could vary widely depending on the level of service that a firm purchases and estimated that it would be typical of its firm customers to pay, in addition to a basic set up fee of \$1,000, approximately \$1,000 to \$2,500 per month for the use of a web-based system to manage margin requirements pursuant to the proposed rule. While this service is purely designed to compute margin obligations, the provider estimated that a firm seeking more robust levels of service, which would include a more sophisticated tracking system of counterparty exposures and margin obligations for all of its asset types, including margining for TBA market transactions, could spend higher amounts on software to manage such systems, and that installation and preparation would require approximately one week.

FINRA understands that firms with significant trading activity in the TBA market may already have the systems built, or the flexibility to enhance current systems, to comply with the proposed rule, whereas firms with relatively little activity in this market, whose business models and trading activity would qualify them for the exceptions as set forth in the proposed rule, can find affordable solutions. One firm that does a significant business in the TBA market said that it has already built systems to reflect the TMPG best practices and estimated it would need to spend \$50,000 to \$100,000 on additional software and technology costs to reflect the additional requirements under the proposed rule change, and would need to hire two to three additional staff at approximately \$70,000 to \$100,000 per person to track margin obligations. FINRA acknowledges that there may also be firms whose customers' trading activity in the TBA market may qualify them for

the de minimis transfer exception on some days only, and may be at a level that would require a more sophisticated margin tracking system on other days. Implementation costs may be higher for such firms, as they may have to determine the size of their activity in TBA market transactions and hence scale their systems accordingly, or they may choose to implement more rigorous solutions in order to avoid non-compliance. FINRA recognizes that some firms may seek to update existing master agreements or to renegotiate master agreement terms upon the adoption of the proposed rule. Any related costs to these activities will likely vary with the amount of the activity conducted by a member, the number of counterparties and the amount of the activity conducted by its counterparties.

B. Scope of the Proposal

One commenter said that the scope of Covered Agency Transactions should be amended to cover only forward settling TBA market transactions whose settlement dates extend beyond the relevant industry-published standard settlement dates.⁹² Another commenter stated the rule should exclude Specified Pool Transactions, ARMs and CMOs on grounds similar to the proposed exception for multifamily and project loan securities.⁹³ A different commenter said that, on similar grounds, SBA securities should be excluded from the proposal.⁹⁴ And, one commenter stated that the proposed rule should not include Specified Pool Transactions and CMOs, that these products do not pose systemic risks, that FINRA should analyze the specified pool and CMO markets, and that FINRA should address why the proposed rule requirements are not being imposed on member banks of the Federal Reserve System.⁹⁵

In response, in the original filing, and again in response to comment in Amendment No. 1, FINRA addressed the commenters' concerns as to the scope of Covered Agency Transactions as defined in the rule.⁹⁶ FINRA notes that Specified Pool Transactions, ARMs, CMOs and the SBA securities as specified under the rule all share the type of extended settlement risk that the proposed rule change aims to address, for which reason they are included within the scope of Covered Agency Transactions. FINRA's reasoning and

⁸⁶ FINRA received 29 comments in response to *Regulatory Notice* 14-02. As discussed above, the Commission received 55 individual letter comments and 54 form letters in response to the Notice, and 23 individual letter comments in response to the Order Instituting Proceedings.

⁸⁷ See Notice, note 90 at 80 FR 63603, 63613; see also, BDA 2 Letter and Vining Sparks Letter, as discussed above.

⁸⁸ See SIFMA 2 Letter and ACLI 2 Letter.

⁸⁹ See BDA 2 Letter and Vining Sparks Letter.

⁹⁰ See Notice, 80 FR 63603, 63613.

⁹¹ See, e.g., the "cash account" exceptions and the de minimis transfer amount as discussed in Sections F and G, respectively, of Amendment No. 2.

⁹² See ACLI 2 Letter.

⁹³ See BDA 2 Letter.

⁹⁴ See Vining Sparks Letter.

⁹⁵ See Coastal 2 Letter.

⁹⁶ See Notice, 80 FR 63603, 63605, 63615 through 63616; see also *supra* notes 3 and 5.

approach as to multifamily and project loan securities, as set forth in Amendment Nos. 1 and 2, are designed with a view to those products in the totality of their characteristics, which is distinct from the products raised by the commenters. For the reasons set forth in the original filing and Amendment No. 1, FINRA does not propose to revise the definition of Covered Agency Transactions.⁹⁷

C. Creation of Account Types

One commenter said that the proposed rule change effectively mandates that members create an account type that would be specific to TBA market transactions.⁹⁸ This commenter said that is because the proposed rule imposes distinct requirements from other types of products, and that the requirements are being imposed at the same time as industry is preparing to expend significant resources to migrate to “T+2” settlement.

In response, FINRA notes that the proposed rule does not mandate the creation of account types dedicated to TBA market transactions. Based on discussions with various market participants and service providers, FINRA believes it is well within the operational and technological ability of firms to appropriately handle margining of TBA market transactions. As discussed above, FINRA has acknowledged that implementation of the proposal will involve costs. FINRA is aware that the proposed rule change is not the only regulatory development that could affect firms. At the same time, however, FINRA notes that regulation, like industry, continually evolves with new and ongoing initiatives. FINRA is aware that the T+2 migration will involve demands on member resources, yet FINRA also notes that the T+2 initiative, with all its attendant resource demands, has been sought and advocated by industry.⁹⁹ It would not be consistent with FINRA’s mission of investor protection and market integrity, nor could it ever be feasible, for FINRA to refrain from rulemaking until the completion of every initiative by other regulators and by industry that could impose burdens or demands on resources.

⁹⁷ See *supra* notes 3 and 5.

⁹⁸ See SIFMA 2 Letter.

⁹⁹ See Letter from Paul Schott Stevens, President & CEO, Investment Company Institute, and Kenneth E. Bentsen, Jr., President and CEO, SIFMA, to Mary Jo White, Chair, Commission (June 18, 2015).

D. Maintenance Margin

As set forth more fully in the original filing and again in Amendment No. 1,¹⁰⁰ non-exempt accounts¹⁰¹ would be required to post two percent maintenance margin plus any net mark to market loss on their Covered Agency Transactions.¹⁰² A few commenters expressed opposition to the proposed maintenance margin requirement.¹⁰³ These commenters believed that the proposal is inconsistent with the TMPG best practices, that the requirement would unfairly affect market participants that do not pose systemic risk, and that the requirement places FINRA members at a competitive disadvantage. One commenter said that if FINRA imposes the maintenance margin requirement, the requirement should be revised so as to be easier to implement.¹⁰⁴ This commenter said that FINRA should consider a tiered approach for trades that are under a defined gross dollar amount and that clarification as to the requirement’s application to DVP accounts is needed.¹⁰⁵

In its response, in the original filing and again in Amendment No. 1, FINRA addressed the commenters’ concerns as to the proposed maintenance margin requirement.¹⁰⁶ FINRA noted that maintenance margin is a mainstay of margin regimes in the securities industry, and, as such, the need to appropriately track transactions should be well understood to market participants. FINRA is sensitive to commenters’ concerns as to the potential impact of the requirement on members and their non-exempt customer accounts. For this reason, as set forth more fully in the original filing, and as discussed further below, FINRA revised the proposal to include an exception tailored to customers engaging in non-margined, cash account business.¹⁰⁷ As such, in response to comments, FINRA does not believe it is necessary or appropriate to further tier the requirement.¹⁰⁸ With respect to the application of the requirement to DVP accounts, FINRA will consider specific

¹⁰⁰ See *supra* notes 3 and 5.

¹⁰¹ The term “exempt account” is defined under FINRA Rule 4210(a)(13). See Notice, 80 FR 63603, 63606; see also proposed FINRA Rule 4210(a)(13)(B)(i) in Exhibit 5 in Amendment No. 2.

¹⁰² See Notice, 80 FR 63603, 63607 through 63608; see also *supra* notes 3 and 5.

¹⁰³ See AII 2 Letter, Matrix 2 Letter, SIFMA 2 Letter, and SIFMA AMG 2 Letter.

¹⁰⁴ See Matrix 2 Letter.

¹⁰⁵ *Id.*

¹⁰⁶ See Notice, 80 FR 63603, 63616 through 63617; see also *supra* notes 3 and 5.

¹⁰⁷ See *supra* notes 3 and 5.

¹⁰⁸ See Matrix 2 Letter.

interpretive issues as they are raised and will consider guidance as needed. FINRA does not propose to revise the maintenance margin requirement.

E. “Cash Account” Exceptions

As set forth more fully in the original filing, the proposed margin requirements would not apply to any counterparty that has gross open positions¹⁰⁹ in Covered Agency Transactions with the member amounting to \$2.5 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a DVP basis or for cash. Similarly, a non-exempt account would be excepted from the rule’s proposed two percent maintenance margin requirement if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and the customer regularly settles its Covered Agency Transactions on a DVP basis or for cash. The rule uses parallel language with respect to both of these exceptions to provide that they are not available to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in FINRA Rule 6710(z),¹¹⁰ or “round robin”¹¹¹ trades, or that uses other financing techniques for its Covered Agency Transactions. FINRA further noted that these exceptions are intended to address the concerns of smaller customers engaging in non-margined, cash account business.¹¹²

¹⁰⁹ See *supra* note 3. Paragraph (e)(2)(H)(i)e. of the rule defines “gross open position” to mean, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty’s contracts with the member and which the counterparty intends to deliver. See Exhibit 5 in Amendment No. 2.

¹¹⁰ FINRA Rule 6710(z) defines “dollar roll” to mean a simultaneous sale and purchase of an Agency Pass-Through MBS for different settlement dates, where the initial seller agrees to take delivery, upon settlement of the re-purchase transaction, of the same or substantially similar securities.

¹¹¹ Paragraph (e)(2)(H)(i)i. defines “round robin” trade to mean any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer. See Exhibit 5 in Amendment No. 2.

¹¹² See Notice, 80 FR 63603, 63605. For convenience, the \$2.5 million and maintenance

One commenter said that it was not clear how FINRA had arrived at the \$2.5 million exception and suggested that the amount should be raised to \$10 million.¹¹³ Another commenter said members should be allowed to negotiate the amount.¹¹⁴ A different commenter stated that it had concerns about how to interpret the term “regularly settles” and that it was skeptical that members would find it worthwhile to build systems to comply with the cash account exceptions, thereby making it likely members will not offer them to counterparties.¹¹⁵ This commenter said it would take the term “regularly settles” to mean “a substantial portion of the time.”¹¹⁶

In response, FINRA addressed commenters’ concerns in Amendment No. 1 and does not propose to modify the cash account exceptions as proposed in the original filing.¹¹⁷ The cash account exceptions are designed to help address the concerns of smaller participants in the market. If members believe that it is too onerous to offer these exceptions to their customers, they are not obligated under the rule to do so. Commenters on the original filing asked for guidance as to the term “regularly settles,”¹¹⁸ and in response FINRA noted that, as worded, the term “regularly settles” is designed to provide scope for flexibility on members’ part as to how they implement the exceptions. FINRA said that it expects that members are in a position to make reasonable judgments as to the observed pattern and course of dealing in their customers’ behavior by virtue of their interactions with their customers. However, FINRA does not agree with one commenter’s interpretation that “regularly” is to be equated with “substantial portion of the time.”¹¹⁹ FINRA views the term “regularly” as conveying the prevailing or dominant pattern and course of the customer’s behavior. FINRA stated in Amendment No. 1 that, in ascertaining the customer’s regular pattern, a member may use the customer’s history of transactions with the member, as well as any other relevant information of which the member is aware, and, further, that members should be able to rely on the reasonable representations of their customers where necessary for

margin exceptions are referred to as the “cash account” exceptions for purposes of Amendment No. 2.

¹¹³ See SIFMA 2 Letter.

¹¹⁴ See SIFMA AMG 2 Letter.

¹¹⁵ See SIFMA 2 Letter.

¹¹⁶ *Id.*

¹¹⁷ See *supra* notes 5 and 10.

¹¹⁸ See *supra* notes 5 and 6.

¹¹⁹ See SIFMA 2 Letter.

purposes of the requirement. As FINRA noted in Amendment No. 1, FINRA will consider issuing further guidance as needed.¹²⁰

With respect to a commenter’s suggestion to increase the \$2.5 million amount to \$10 million,¹²¹ FINRA noted in the original filing, and again in Amendment No. 1, that the amount is meant to be appropriately tailored to smaller accounts that are less likely to pose systemic risk.¹²² FINRA noted that increasing the amount would undermine the rule’s purpose. FINRA does not object if parties attempt to negotiate thresholds, provided the thresholds are not greater than prescribed by the rule. In that regard, FINRA noted that permitting parties to negotiate higher thresholds by separate agreement, whether entered into before the rule takes effect or afterwards, would only serve to cut against the rule’s objectives.

F. De Minimis Transfer

The proposed rule sets forth, for a single counterparty, a \$250,000 de minimis transfer amount up to which margin need not be collected or charged to net capital, as specified by the rule.¹²³ One commenter stated members should be allowed to negotiate the de minimis transfer amount with their counterparties.¹²⁴ Some commenters said the de minimis transfer amount should be \$500,000,¹²⁵ which one commenter suggested would align with requirements for swaps.¹²⁶ A different commenter said the amount should be \$1 million.¹²⁷ One commenter expressed concern that members would end up needing to monitor the \$250,000 amount even though it would benefit few if any customers.¹²⁸

In response, FINRA addressed commenters’ concerns in Amendment No. 1 and does not propose to modify the de minimis transfer provisions as proposed in the original filing.¹²⁹ FINRA noted in the original filing that the de minimis transfer amount is meant to be appropriately tailored to help prevent smaller members from being subject to competitive disadvantage.¹³⁰ FINRA noted that increasing the amount

¹²⁰ See *supra* notes 5 and 10.

¹²¹ See SIFMA 2 Letter.

¹²² See Notice, 80 FR 63603, 63616; see also *supra* notes 3 and 5.

¹²³ See Notice, 80 FR 63603, 63608; see also *supra* notes 3 and 5.

¹²⁴ See SIFMA AMG 2 Letter.

¹²⁵ See ACLI 2 Letter and SIFMA 2 Letter.

¹²⁶ See SIFMA 2 Letter.

¹²⁷ See BDA 2 Letter.

¹²⁸ See SIFMA 2 Letter.

¹²⁹ See *supra* notes 3 and 5.

¹³⁰ See Notice, 80 FR 63603, 63608, 63617; see also *supra* notes 3 and 5.

would undermine the rule’s purpose. As noted above, FINRA does not object if parties attempt to negotiate de minimis transfer thresholds, provided the thresholds are not greater than prescribed by the rule.

G. Timing of Margin Collection and Position Liquidation

The proposed rule provides that, with respect to exempt accounts, if a mark to market loss, or, with respect to non-exempt accounts, a deficiency, is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member must deduct the amount of the mark to market loss or deficiency from net capital as provided in Exchange Act Rule 15c3–1. Further, unless FINRA has specifically granted the member additional time, the member is required to liquidate positions if, with respect to exempt accounts, a mark to market loss is not satisfied within five business days, or, with respect to non-exempt accounts, a deficiency is not satisfied within such period.¹³¹ One commenter said the required timing of margin collection should be replaced with a three-day transfer period.¹³² Another commenter said that the proposed margin collection timing is operationally impractical for TBA market transactions, that the requirement would create technological difficulties because it deviates from ordinary operational practices, that FINRA’s Regulatory Extension System would not be suitable for requirements that are impractical to begin with, and that the portfolio margin provisions under FINRA Rule 4210(g)(10)(B) are not a comparable analogy for purposes of margin collection timing.¹³³ This commenter also said the Regulatory Extension System is intended to grant waivers from ordinarily applicable requirements arising under unusual circumstances.¹³⁴ This commenter asked whether the Regulatory Extension System would accommodate permanent waivers for certain firms and customers and whether there would be any limit to the number of waivers a firm could obtain either generally or for a particular customer.¹³⁵ Another commenter suggested the proposed requirement is not consistent with FINRA Rule 4210.¹³⁶ With respect to the proposed

¹³¹ See Notice, 80 FR 63603, 63607 through 63608; see also *supra* notes 3 and 5.

¹³² See SIFMA AMG 2 Letter.

¹³³ See SIFMA 2 Letter.

¹³⁴ *Id.*

¹³⁵ *Id.*

¹³⁶ See Matrix 2 Letter.

liquidation requirement, some commenters said the requirement should be omitted, that five business days is too short, and that parties should be permitted to negotiate the time frames under the rule.¹³⁷

In response, FINRA addressed the commenters' concerns in Amendment No. 1.¹³⁸ FINRA does not propose to modify the proposed requirements. As FINRA noted in Amendment No. 1, consistent with longstanding practice under FINRA Rule 4210(f)(6), the proposed rule allows FINRA to specifically grant the member additional time.¹³⁹ FINRA maintains, and regularly updates,¹⁴⁰ the Regulatory Extension System for this purpose, which is well understood to industry participants. In response to comments, FINRA notes that the Regulatory Extension System does not grant waivers from requirements under Rule 4210, whether permanent or temporary.¹⁴¹ Additional time is granted, pursuant to the rule, for meeting specified obligations and, consistent with longstanding practice under the rule, FINRA may limit or restrict the extensions granted for a firm or customer. FINRA will consider additional guidance as needed. FINRA referenced the portfolio margin rules in Amendment No. 1 to illustrate that, with respect to the timing of margin collection, the proposed language "by the close of business on the next business day after the business day" on which the mark to market loss or deficiency arises is consistent with existing language under Rule 4210 and is well understood by members.¹⁴² With respect to the liquidation requirement, FINRA noted that the five business day period should provide sufficient time for members to resolve issues. Further, as FINRA noted in the original filing and in Amendment No. 1, FINRA believes the specified period is appropriate in view of the potential counterparty risk in the TBA market.¹⁴³

H. Two-Way (Bilateral) Margin

Some commenters said that the proposed rule change should require bilateral, two-way margining.¹⁴⁴ In

response, FINRA addressed this in the original filing and in Amendment No. 1. FINRA noted its support for the use of two-way margining as a means of managing risk.¹⁴⁵ However, FINRA noted that it does not propose to address such a requirement at this time as part of the proposed rule change.

I. Third Party Custodians

A commenter said the proposed rule change should provide for a member's counterparty to have the right to segregate any margin posted with a FINRA member with an independent third party custodian.¹⁴⁶ In response, FINRA addressed this concern in Amendment No. 1.¹⁴⁷ FINRA noted that, with respect to third party custodial arrangements, FINRA believes these are best addressed in separate rulemaking or guidance, as appropriate. FINRA welcomes further discussion of these issues, but does not propose to address them as part of the proposed rule change.

J. Exchange Act Rule 15c3-3

One commenter said that the proposed rule change does not address the treatment of customer margin for purposes of the segregation requirements under Exchange Act Rule 15c3-3.¹⁴⁸ This commenter suggested that the Commission should issue an interpretation to correspond with the proposed rule change.¹⁴⁹ FINRA notes the suggestion is outside the scope of the proposed rule change and welcomes further discussion of this issue.

K. Sovereign Entities

As set forth more fully in the original filing, the proposed rule provides that, with respect to Covered Agency Transactions with any counterparty that is a federal banking agency, as defined in 12 U.S.C. 1813(z),¹⁵⁰ central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of the proposed rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph

(e)(2)(H)(ii)b.¹⁵¹ One commenter said that sovereign wealth funds should be excepted from the proposed margin requirements.¹⁵² In response, FINRA addressed this concern in the original filing¹⁵³ and again in Amendment No. 1.¹⁵⁴ FINRA believes that to include sovereign wealth funds within the parameters of the proposed exception would create perverse incentives for regulatory arbitrage.

L. Exempt Account Treatment

Some commenters said that the exempt account definition should be expanded as part of the rule change to include foreign equivalent entities and collective investment trusts.¹⁵⁵ Another commenter suggested the exempt account definition should be updated.¹⁵⁶ In response, in Amendment No. 1, FINRA noted that, other than for purposes of one conforming revision, as set forth in the original filing,¹⁵⁷ the proposed rule change is not intended to revisit the definition of exempt accounts for the broader purposes of Rule 4210. FINRA believes that this issue is properly addressed by separate rulemaking or guidance, as appropriate.

M. Third Party Providers

A commenter suggested that FINRA should make clear that members required to collect margin under the proposed rule change may utilize third party service providers and products.¹⁵⁸ FINRA addressed this concern in Amendment No. 1.¹⁵⁹ FINRA believes that third party service providers are permissible provided the member complies with all applicable rules and guidance, including, among other things, the member's obligations under FINRA Rule 3110 and as described in *Notice to Members 05-48* (July 2005) (Outsourcing).

N. Netting Services

A commenter said that the proposal should not be implemented until the Mortgage-Backed Securities Division ("MBSD") of Fixed Income Clearing Corporation enlarges the universe of transactions for which it provides netting services and that, until MBSD does so, the proposal would unfairly

¹³⁷ See ACLI 2 Letter, Matrix 2 Letter, SIFMA 2 Letter, and SIFMA AMG 2 Letter.

¹³⁸ See *supra* note 5.

¹³⁹ See *supra* note 5.

¹⁴⁰ See, e.g., *Regulatory Notice* 10-28 (June 2010) (Extension of Time Requests); *Regulatory Notice* 14-13 (March 2014) (Regulatory Extension System Update).

¹⁴¹ See SIFMA 2 Letter.

¹⁴² See FINRA Rule 4210(g)(10)(B); see *supra* note 5.

¹⁴³ See Notice, 80 FR 63603, 63619; see also *supra* notes 3 and 5.

¹⁴⁴ See ACLI 2 Letter, SIFMA AMG 2 Letter, and Sutherland 2 Letter.

¹⁴⁵ See Notice, 80 FR 63603, 63619 through 63620; see also *supra* notes 3 and 5.

¹⁴⁶ See Sutherland 2 Letter.

¹⁴⁷ See *supra* notes 5 and 6.

¹⁴⁸ See SIFMA 2 Letter.

¹⁴⁹ *Id.*

¹⁵⁰ 12 U.S.C. 1813(z) defines federal banking agency to mean the Comptroller of the Currency, the Board of Governors of the Federal Reserve System ("Federal Reserve Board"), or the Federal Deposit Insurance Corporation.

¹⁵¹ See Notice, 80 FR 63603, 63606; see also *supra* notes 3 and 5.

¹⁵² See SIFMA AMG 2 Letter.

¹⁵³ See Notice, 80 FR 63603, 63619.

¹⁵⁴ See *supra* note 5.

¹⁵⁵ See SIFMA 2 Letter and SIFMA AMG 2 Letter.

¹⁵⁶ See Matrix 2 Letter.

¹⁵⁷ See Notice, 80 FR 63603, 63606; see also *supra* notes 3 and 5.

¹⁵⁸ See Matrix 2 Letter.

¹⁵⁹ See *supra* note 5.

discriminate against mid-sized firms.¹⁶⁰ In Amendment No. 1, FINRA noted that coordination with MBSD is outside the scope of the proposed rule change.¹⁶¹ FINRA welcomes further discussion of this issue.

O. Scope of FINRA's Authority

Some commenters said that the proposed rule change is not consistent with the intent of Section 7 of the Exchange Act and questioned FINRA's authority to proceed with the proposed rule change.¹⁶² The commenters cited the Senate Report¹⁶³ in connection with Congress's adoption of the Secondary Mortgage Market Enhancement Act of 1984¹⁶⁴ ("SMMEA") in support of this view. In response, FINRA notes that Section 7 of the Exchange Act sets forth the parameters of the margin setting authority of the Federal Reserve Board and does not bar action by FINRA. SMMEA does not address FINRA's authority as the statute was designed, among other things, to level the competitive playing field between issuers of private-label MBS (defined under the SMMEA as "mortgage related securities" under Section 3(a)(41) of the Exchange Act) vis-à-vis agency and GSE MBS.¹⁶⁵ As FINRA noted in the original filing and Amendment No. 1, FINRA believes the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Exchange Act.¹⁶⁶

P. Implementation Period

In Amendment No. 1, FINRA stated that it believes that a phased implementation should be appropriate. FINRA proposed that the risk limit determination requirements as set forth in paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H) of Rule 4210 and proposed

Supplementary Material .05 of the rule become effective six months from the date the proposed rule change is approved by the Commission. FINRA proposed that the remainder of the proposed rule change become effective 18 months from the date the proposed rule change is approved by the Commission.¹⁶⁷ One commenter said 18 months represents a reasonable time frame.¹⁶⁸ Another commenter said that the implementation time frame as proposed in Amendment No. 1 is sufficiently reasonable.¹⁶⁹ A different commenter said that compliance with the proposed requirements would be difficult to complete and that it would prefer a time frame of 24 months, but that its members could aim to complete their implementation work within 18 months.¹⁷⁰ One commenter said that an implementation period of at least 18 months would be appropriate and that two years would be more practical.¹⁷¹ This commenter said that the proposed six-month period for implementation of the risk limit requirements would effectively require broker-dealers to complete their diligence as to their customers within six months even though the proposed rule does not take effect in full until a year after that six-month period.¹⁷² Another commenter said that it would need 18 to 24 months to complete implementation of the proposed requirements and suggested that FINRA should not have a separate time frame for the risk limit requirements.¹⁷³

In response, FINRA does not propose to change the implementation periods as set forth in Amendment No. 1.¹⁷⁴ FINRA does not believe it would serve the public interest to extend implementation of the rule beyond 18 months once approved by the Commission. FINRA believes the six-month time frame for the risk limit requirements is appropriate given that members engaging in business in the TBA market should undertake the effort to understand their counterparties.

IV. Designation of a Longer Period for Commission Action on Proceedings To Determine Whether To Approve or Disapprove SR-FINRA-2015-036

Section 19(b)(2) of the Exchange Act¹⁷⁵ provides that, after initiating approval or disapproval proceedings,

the Commission shall issue an order approving or disapproving the proposed rule change not later than 180 days after the date of the publication of the notice of filing of the proposed rule change. The Commission may extend the period for issuing an order approving or disapproving the proposed rule change, however, by not more than 60 days if the Commission determines that a longer period is appropriate and publishes the reasons for such determination.¹⁷⁶ The 180th day after publication of the Notice in the **Federal Register** is April 17, 2016 and the 240th day after publication of the Notice in the **Federal Register** is June 16, 2016.¹⁷⁷

The Commission is extending the 180-day time period. The Commission finds that it is appropriate to designate a longer period within which to take action on the proposed rule change so that it has sufficient time to consider the proposed rule change, as modified by Amendment Nos. 1 and 2, including the matters raised in the comment letters and FINRA's submissions.

V. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the filing, as amended by Amendment No. 2, is consistent with the Exchange 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 email to rule-comments@sec.gov. Please include File Number SR-FINRA-2015-036 on the subject line.

Paper Comments

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

All submissions should refer to File Number SR-FINRA-2015-036. This file number should be included on the subject line if email 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

¹⁶⁰ See Brean Capital 3 Letter.

¹⁶¹ See *supra* note 5.

¹⁶² See BDA 2 Letter, Coastal 2 Letter, and Senator Cotton Letter.

¹⁶³ See S. Rep. No. 293, 98th Cong., 2d Session (1983).

¹⁶⁴ Public Law 98-440, 98 Stat. 1689 (1984).

¹⁶⁵ See David Abelman, *The Secondary Mortgage Market Enhancement Act*, 14 Real Estate Law Journal 136, 138 (1985) (noting that Congress sought to encourage private issuance by eliminating competitive advantages in favor of government issued securities); Edward L. Pittman, *Economic and Regulatory Developments Affecting Mortgage Related Securities*, 64 Notre Dame Law Review 497, 537 (noting that the SMMEA amendments to Section 7 of the Exchange Act were intended to facilitate the creation of mortgage related securities).

¹⁶⁶ See 80 FR 63603, 63609. Section 15A(b)(6) of the Exchange Act 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. See also *supra* notes 3 and 5.

¹⁶⁷ See *supra* note 5.

¹⁶⁸ See ACLI 2 Letter.

¹⁶⁹ See AII 2 Letter.

¹⁷⁰ See SIFMA AMG 2 Letter.

¹⁷¹ See SIFMA 2 Letter.

¹⁷² *Id.*

¹⁷³ See Vining Sparks Letter.

¹⁷⁴ See *supra* note 5.

¹⁷⁵ 15 U.S.C. 78s(b)(2).

¹⁷⁶ 15 U.S.C. 78s(b)(2)(B)(ii)(III)(aa).

¹⁷⁷ See *supra* note 3.

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 a.m. and 3 p.m. Copies of such 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-2015-036 and should be submitted on or before May 2, 2016.

Accordingly, the Commission, pursuant to Section 19(b)(2)(B) of the Exchange Act, designates June 16, 2016 as the date by which the Commission shall either approve or disapprove the proposed rule change (File No. SR-FINRA-2015-036).

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁷⁸

Robert W. Errett,
Deputy Secretary.

[FR Doc. 2016-08644 Filed 4-14-16; 8:45 am]

BILLING CODE 8011-01-P

DEPARTMENT OF STATE

[Public Notice: 9519]

Culturally Significant Objects Imported for Exhibition Determinations: "Emperors' Treasures: Chinese Art From the National Palace Museum, Taipei" Exhibition

SUMMARY: Notice is hereby given of the following determinations: Pursuant to the authority vested in me by the Act of October 19, 1965 (79 Stat. 985; 22 U.S.C. 2459), E.O. 12047 of March 27, 1978, the Foreign Affairs Reform and Restructuring Act of 1998 (112 Stat. 2681, *et seq.*; 22 U.S.C. 6501 note, *et seq.*), Delegation of Authority No. 234 of October 1, 1999, Delegation of Authority No. 236-3 of August 28, 2000 (and, as appropriate, Delegation of Authority No. 257-1 of December 11, 2015), I hereby determine that the objects to be included in the exhibition "Emperors' Treasures: Chinese Art from the

National Palace Museum, Taipei," imported from abroad for temporary exhibition within the United States, are of cultural significance. The objects are imported pursuant to a loan agreement with the foreign owner or custodian. I also determine that the exhibition or display of the exhibit objects at the Asian Art Museum, San Francisco, California, from on or about June 17, 2016, until on or about September 18, 2016, at the Museum of Fine Arts, Houston, Houston, Texas, from on or about October 23, 2016, until on or about January 22, 2017, and at possible additional exhibitions or venues yet to be determined, is in the national interest. I have ordered that Public Notice of these Determinations be published in the **Federal Register**.

FOR FURTHER INFORMATION CONTACT: For further information, including a list of the imported objects, contact the Office of Public Diplomacy and Public Affairs in the Office of the Legal Adviser, U.S. Department of State (telephone: 202-632-6471; email: section2459@state.gov). The mailing address is U.S. Department of State, L/PD, SA-5, Suite 5H03, Washington, DC 20522-0505.

Dated: April 11, 2016.

Mark Taplin,

Deputy Assistant Secretary for Policy, Bureau of Educational and Cultural Affairs, Department of State.

[FR Doc. 2016-08767 Filed 4-14-16; 8:45 am]

BILLING CODE 4710-05-P

DEPARTMENT OF STATE

[Public Notice: 9516]

Notice of Intent To Prepare an Environmental Impact Statement for the Proposed Upland Pipeline in Williams, Mountrail, and Burke Counties, North Dakota and Conduct a Public Scoping Meeting

AGENCY: Department of State.

ACTION: Notice.

SUMMARY: The U.S. Department of State (Department) is issuing this Notice of Intent (NOI) to inform the public that it will prepare an Environmental Impact Statement (EIS), consistent with the National Environmental Policy Act (NEPA) of 1969 (as implemented by the Council on Environmental Quality regulations found at 40 CFR parts 1500-1508), to evaluate potential impacts from the construction, connection, operation, and maintenance of a proposed new 20-inch diameter pipeline and associated infrastructure in North Dakota that would export crude oil from the United States to Canada.

The Upland Pipeline EIS will address potential direct, indirect, and cumulative environmental impacts from the proposed action and will evaluate a range of reasonable alternatives, including a no action alternative.

The Department also plans to host a public scoping meeting on Tuesday, May 10, 2016 from 4:00-7:00 p.m. at the Farm Festival Building in Tioga, North Dakota to solicit public comments for consideration in establishing the scope of the EIS.

DATES: The Department invites the public, governmental agencies, tribal governments, and all other interested parties to comment on the scope of the EIS. All such comments should be provided within the 45-day public scoping period, which starts with the publication of this Notice in the **Federal Register** on April 15, 2016 and will continue until May 31, 2016. Written, electronic, and oral comments will be given equal weight and the Department will consider all comments received or postmarked by May 30, 2016. Comments received or postmarked after that date may be considered to the extent practicable.

ADDRESSES: Written comments may be submitted at www.regulations.gov by entering the title of this Notice into the search field and following the prompts. Comments may also be submitted by mail, addressed to: Upland Project Manager, Office of Environmental Quality and Transboundary Issues, Room 2726, U.S. Department of State, 2201 C Street NW., Washington, DC 20520. All comments from agencies or organizations should indicate a contact person for the agency or organization.

Comments may also be submitted at the public scoping meeting on Tuesday, May 10, 2016 from 4:00-7:00 p.m. at the following address: Farm Festival Building, 640 6th Street North, Tioga, North Dakota.

FURTHER INFORMATION: For information contact the Upland Project Manager at the address listed in **ADDRESSES**, by email at UplandReview@state.gov, or by fax at (202) 647-5947. Information on the proposed project details, Presidential Permit application, status of the environmental review, etc. may be found at: <http://www.state.gov/e/enr/applicant/applicants/uplandpipeline/>.

SUPPLEMENTARY INFORMATION:

Project Description

On April 22, 2015, Upland Pipeline, LLC (Upland), which is a subsidiary of TransCanada Pipeline Limited, submitted an application for a new Presidential Permit under E. O. 13337 of April 30, 2004 (69 FR 25299) to

¹⁷⁸ 17 CFR 200.30-3(a)(12); 17 CFR 200.30-3(a)(57).