

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * 26	SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 Form 19b-4		File No.* SR - 2018 - * 032	Amendment No. (req. for Amendments *)
Filing by Financial Industry Regulatory Authority Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934				
Initial * <input checked="" type="checkbox"/>	Amendment * <input type="checkbox"/>	Withdrawal <input type="checkbox"/>	Section 19(b)(2) * <input checked="" type="checkbox"/>	Section 19(b)(3)(A) * <input type="checkbox"/>
			Section 19(b)(3)(B) * <input type="checkbox"/>	
			Rule	
Pilot <input type="checkbox"/>	Extension of Time Period for Commission Action * <input type="checkbox"/>	Date Expires * <input type="text"/>	<input type="checkbox"/> 19b-4(f)(1) <input type="checkbox"/> 19b-4(f)(2) <input type="checkbox"/> 19b-4(f)(3)	<input type="checkbox"/> 19b-4(f)(4) <input type="checkbox"/> 19b-4(f)(5) <input type="checkbox"/> 19b-4(f)(6)
Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010			Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934	
Section 806(e)(1) * <input type="checkbox"/>		Section 806(e)(2) * <input type="checkbox"/>		Section 3C(b)(2) * <input type="checkbox"/>
Exhibit 2 Sent As Paper Document <input type="checkbox"/>		Exhibit 3 Sent As Paper Document <input type="checkbox"/>		
Description				
Provide a brief description of the action (limit 250 characters, required when Initial is checked *).				
<input type="text" value="Proposed Rule Change to Amend FINRA Rule 6710 to Modify Agency Debt Security Dissemination Protocols"/>				
Contact Information				
Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.				
First Name * <input type="text" value="Racquel"/>		Last Name * <input type="text" value="Russell"/>		
Title * <input type="text" value="Associate General Counsel"/>				
E-mail * <input type="text" value="racquel.russell@finra.org"/>				
Telephone * <input type="text" value="(202) 728-8363"/>		Fax <input type="text" value="(202) 728-8264"/>		
Signature				
Pursuant to the requirements of the Securities Exchange Act of 1934,				
has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.				
(Title *)				
Date	<input type="text" value="08/16/2018"/>	<input type="text" value="Vice President and Director - Appellate Group"/>		
By	<input type="text" value="Alan Lawhead"/>	<input type="text" value="Alan Lawhead, Alan.Lawhead@finra.org"/>		
(Name *)				
NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.				

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFF website.

Form 19b-4 Information *

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

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Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ Financial Industry Regulatory Authority, Inc. (“FINRA”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to amend FINRA Rule 6710 to modify the dissemination protocols with respect to Agency Debt Securities.

2. Procedures of the Self-Regulatory Organization

At its meeting on May 10, 2018, the FINRA Board of Governors authorized the filing of the proposed rule change with the SEC. No other action by FINRA is necessary for the filing of the proposed rule change.

If the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 120 days following publication of the Regulatory Notice announcing Commission approval.

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

(a) Purpose

FINRA requires members to report to the Trade Reporting and Compliance Engine (“TRACE”) transactions in TRACE-Eligible Securities,² including securities that

¹ 15 U.S.C. 78s(b)(1).

² Rule 6710 generally defines a “TRACE-Eligible Security” as: a debt security that is United States (“U.S.”) dollar-denominated and is: (1) issued by a U.S. or foreign private issuer, and, if a “restricted security” as defined in Securities Act Rule 144(a)(3), sold pursuant to Securities Act Rule 144A; (2) issued or

meet the definition of “Agency Debt Security.”³ FINRA disseminates transaction information on Agency Debt Securities and displays either the actual size (volume) of the transaction or a capped amount, depending on whether the security is rated as Investment Grade,⁴ Non-Investment Grade,⁵ or is unrated. For transactions in Agency Debt

guaranteed by an Agency as defined in Rule 6710(k) or a Government-Sponsored Enterprise as defined in Rule 6710(n); or (3) a U.S. Treasury Security as defined in Rule 6710(p). “TRACE-Eligible Security” does not include a debt security that is issued by a foreign sovereign or a Money Market Instrument as defined in Rule 6710(o).

- ³ “Agency Debt Security” generally includes a debt security (i) issued or guaranteed by an Agency as defined in Rule 6710(k); (ii) issued or guaranteed by a Government-Sponsored Enterprise (“GSE”) as defined in Rule 6710(n); or (iii) issued by a trust or other entity that was established or sponsored by a GSE for the purpose of issuing debt securities, where such enterprise provides collateral to the trust or other entity or retains a material net economic interest in the reference tranches associated with the securities issued by the trust or other entity. Rule 6710(n) provides that “Government-Sponsored Enterprise” has the same meaning as defined in 2 U.S.C. § 622(8).
- ⁴ Rule 6710 provides that “Investment Grade” means “a TRACE-Eligible Security that, if rated by only one nationally recognized statistical rating organization (“NRSRO”), is rated in one of the four highest generic rating categories; or if rated by more than one NRSRO, is rated in one of the four highest generic rating categories by all or a majority of such NRSROs; provided that if the NRSROs assign ratings that are evenly divided between (i) the four highest generic ratings and (ii) ratings lower than the four highest generic ratings, FINRA will classify the TRACE-Eligible Security as Non-Investment Grade for purposes of TRACE. If a TRACE-Eligible Security is unrated, for purposes of TRACE, FINRA may classify the TRACE-Eligible Security as an Investment Grade security. FINRA will classify an unrated Agency Debt Security as defined in [Rule 6710(l)] as an Investment Grade security for purposes of the dissemination of transaction volume.” See FINRA Rule 6710(h).
- ⁵ Rule 6710 provides that “Non-Investment Grade” means “a TRACE-Eligible Security that, if rated by only one NRSRO, is rated lower than one of the four highest generic rating categories; or if rated by more than one NRSRO, is rated lower than one of the four highest generic rating categories by all or a majority of such NRSROs. Except as provided in paragraph (h), if a TRACE-Eligible Security is unrated, FINRA may classify the TRACE-Eligible Security as a Non-Investment Grade security.” See FINRA Rule 6710(i).

Securities that are either Investment Grade or unrated, FINRA disseminates the actual size of the trade for transactions less than or equal to \$5 million in par value traded, thus providing actual transaction size up to \$5 million, and disseminates “\$5MM+” for trades exceeding \$5 million in par value traded.⁶ For transactions in Agency Debt Securities that are Non-Investment Grade, FINRA disseminates the actual size of the trade for transactions less than or equal to \$1 million in par value, and disseminates “1MM+” for trades exceeding \$1 million in par value traded.⁷

FINRA is proposing to apply a \$5 million dissemination cap to all Agency Debt Securities, regardless of the rating assigned to the security. When adopting the original dissemination caps for Agency Debt Securities, FINRA believed that unrated Agency Debt Securities should default to the \$5 million dissemination cap due to factors such as that they trade more consistently with Investment Grade securities that are subject to the \$5 million dissemination cap. While Non-Investment Grade Agency Debt Securities have been disseminated with the \$1 million dissemination cap, FINRA is not aware of the existence of any Non-Investment Grade Agency Debt Securities other than credit risk transfer securities (“CRTs”), a type of Agency Debt Security issued by Fannie Mae (“Fannie”) and Freddie Mac (“Freddie”). Based on experience gained with CRTs and in consultation with Fannie and Freddie, FINRA believes that it is appropriate to disseminate Non-Investment Grade CRTs with the \$5 million dissemination cap. Because CRTs are the only type of Agency Debt Security rated less than Investment

⁶ See Securities Exchange Act Release No. 59733 (April 8, 2009), 74 FR 17709 (April 16, 2009) (Notice of Filing of File No. SR-FINRA-2009-010).

⁷ See supra note 6.

Grade, FINRA is proposing to simplify the dissemination structure by applying the \$5 million dissemination cap to all Agency Debt Securities irrespective of rating.

FINRA notes that transactions in the vast majority of securities issued by Fannie and Freddie are disseminated with the actual size of the trade (uncapped), and, of those that are capped, the vast majority are disseminated with the \$5 million cap: 94.4% of all transactions in direct obligations issued by Fannie and Freddie, including CRTs, currently are disseminated with the actual size of the trade. Of the remaining 5.6% that are capped (both at \$1 million and \$5 million), 95% currently are disseminated with the \$5 million cap. Thus, FINRA believes that the proposed modification to apply the \$5 million dissemination cap to all Agency Debt Securities uniformly will have a minimal impact, while simplifying the dissemination structure and providing additional transparency in Agency Debt Securities.

As noted in Item 2 of this filing, if the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 120 days following publication of the Regulatory Notice announcing Commission approval.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁸ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public

⁸ 15 U.S.C. 78q-3(b)(6).

interest. The proposed rule change would benefit investors in that it would simplify the dissemination structure by creating a uniform dissemination protocol for all Agency Debt Securities, and would increase transparency for transactions in Non-Investment Grade Agency Debt Securities over \$1 million. Additionally, the proposed rule change would have a minimal impact as the vast majority of capped transactions in Agency Debt Securities are already disseminated with the \$5 million cap.

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

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

Economic Impact Assessment

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the potential economic impacts, including anticipated costs, benefits, and distributional and competitive effects, relative to the current baseline, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

Economic Baseline

As of December 31, 2017, there were 35 Investment Grade, 9 Non-Investment Grade, and 172 unrated CRT classes (based on TRACE data). FINRA notes that certain CRTs are currently the only type of Agency Debt Security with a Non-Investment Grade rating. The outstanding amount of these issues are \$770 million, \$350 million and \$2,877 million for Investment Grade, Non-Investment Grade and unrated issues

respectively. Table 1 presents the number of trades reported to TRACE and nominal trade value of CRT CUSIPs by rating for the calendar year beginning January 1, 2017.⁹

Table 1

Grade	Trades		Trade Value	
	Number	Percent	Dollars (millions)	Percent
Non-Investment	1,950	13.6%	8,800.9	13.6%
Investment	1,988	13.8%	8,880.1	13.7%
Unrated	10,423	72.6%	47,077.7	72.7%

Under the existing dissemination protocols, Agency Debt Securities that are unrated or rated Investment Grade are disseminated with a \$5 million dissemination cap, where trades over \$5 million are displayed as “5MM+.” Non-Investment Grade Agency Debt Securities are disseminated with a \$1 million dissemination cap, where trades over \$1 million are displayed as “1MM+.” Table 2 presents the number and percent of trades and nominal trade value disseminated with actual trade sizes or displayed with “5MM+” for Investment Grade or unrated CRT CUSIPs for calendar year 2017. These statistics include all trades reported to TRACE during the period, and thus would include two trade reports for interdealer trades and one trade report for dealer to customer trades (two-sided trade data).¹⁰

⁹ Each CRT deal utilizes a senior/subordinate structure in which credit protection is provided to the senior class by the subordinate classes in priority order. The senior class and subordinate tranches, while part of the same CRT issuance, are separate securities and each are assigned a unique CUSIP. In addition, each CRT class can be further tranching to provide additional optionality for investors’ needs. As such, each CRT class is associated with multiple unique CUSIPs. We note that only the CUSIP associated with the senior tranche contributes to the amount of debt outstanding for a given CRT class.

¹⁰ For calendar year 2017, there were 11,341 trades reported to TRACE, that include only one trade report for interdealer trades and one trade report for dealer to

Table 2

Grade	Trades			
	≤\$5M		>\$5M	
	Number	Percent	Number	Percent
Investment	1,524	76.7%	464	23.3%
Unrated	8,435	80.9%	1,988	19.1%
	Trade value			
	≤\$5M		>\$5M	
	Dollars (millions)	Percent	Dollars (millions)	Percent
Investment	2,591.5	29.2%	6,288.6	28.2%
Unrated	22,390.9	47.6%	24,686.7	46.6%

Table 3 presents the number and percent of trades and nominal trade value disseminated with actual trade sizes or displayed with “1MM+” for Non-Investment Grade CRT CUSIPs for calendar year 2017.¹¹

Table 3

Grade	Trades			
	≤\$1M		>\$1M	
	Number	Percent	Number	Percent
Non-Investment	222	11.4%	1,728	88.6%
	Trade value			
	≤\$1M		>\$1M	
	Dollars (millions)	Percent	Dollars (millions)	Percent
Non-Investment	139.7	1.6%	8,661.2	98.4%

customer trades (one-sided trade data), in Investment Grade and unrated CRT CUSIPs, of which 20.8% were displayed as “5MM+.”

¹¹ For calendar year 2017, there were 1,712 trades reported to TRACE, that include only one trade report for interdealer trades and one trade report for dealer to customer trades (one-sided trade data), in Non-Investment Grade CUSIPs, of which 88.3% were displayed as “1MM+.”

Economic Impact

Based on transactions during calendar year 2017, this proposal would have led to dissemination of additional trade size information for 1,112 trades in 82 CRT CUSIPs than disseminated under the current protocols. This increased transparency could have impacts on investors, market makers and issuers. Markets participants, especially uninformed investors, generally anticipate that they benefit from greater price transparency because, in the presence of this information, they are more likely to gain more timely information about the current price of an asset. Knowing this, they may be more willing to commit capital.¹²

At the same time, FINRA understands that some firms believe that transparency about the size of larger trades impedes their ability to commit capital and hence may have a negative impact on liquidity. Increasing transparency may increase the amount of information available to uninformed investors on transaction size and price. This may reduce the informed investors' relative advantage by decreasing the bid-ask spread earned by an informed investor or increasing the bid-ask spread paid by an informed investor. Furthermore, firms may be less willing to trade as principal and hold these securities in inventory, leading to wider spreads or less depth, if they fear that investors

¹² For instance, one study that examined corporate bond transactions in TRACE from January 2003 through January 2005 found that “[c]osts are lower for bonds with transparent trade prices, and they drop when the TRACE system starts to publicly disseminate their prices. The results suggest that public traders benefit significantly from price transparency.” For additional details, *see* Amy K. Edwards, Lawrence E. Harris, and Michael S. Piwowar, Corporate Bond Market Transaction Costs and Transparency, *Journal of Finance* 62, No. 3, 1421–1451 (2007).

may identify the firms' inventory position.¹³ In addition, existing institutional investors that prefer trading in large sizes or at the current level of transparency in Non-Investment Grade CRTs may substitute trading in other asset classes, if the investors fear others may identify their holdings. The consensus of the academic literature studying the impact of transparency in a variety of settings in U.S. fixed income markets is that greater transparency is associated with lower costs to end customers and positive to neutral impacts on market liquidity.¹⁴ In addition, FINRA has discussed the proposed rule change with Fannie and Freddie, both of which support the application of the \$5 million dissemination cap to all CRTs.

Alternatives

No alternatives are under consideration.

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

Written comments were neither solicited nor received.

6. **Extension of Time Period for Commission Action**

FINRA does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.¹⁵

7. **Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)**

Not applicable.

¹³ See supra note 12.

¹⁴ See supra note 12.

¹⁵ 15 U.S.C. 78s(b)(2).

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

11. Exhibits

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 5. Text of the proposed rule change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-FINRA-2018-032)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Amend FINRA Rule 6710 to Modify Agency Debt Security Dissemination Protocols

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

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

FINRA is proposing to amend FINRA Rule 6710 to modify the dissemination protocols with respect to Agency Debt Securities.

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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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

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

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

1. Purpose

FINRA requires members to report to the Trade Reporting and Compliance Engine (“TRACE”) transactions in TRACE-Eligible Securities,³ including securities that meet the definition of “Agency Debt Security.”⁴ FINRA disseminates transaction information on Agency Debt Securities and displays either the actual size (volume) of the

³ Rule 6710 generally defines a “TRACE-Eligible Security” as: a debt security that is United States (“U.S.”) dollar-denominated and is: (1) issued by a U.S. or foreign private issuer, and, if a “restricted security” as defined in Securities Act Rule 144(a)(3), sold pursuant to Securities Act Rule 144A; (2) issued or guaranteed by an Agency as defined in Rule 6710(k) or a Government-Sponsored Enterprise as defined in Rule 6710(n); or (3) a U.S. Treasury Security as defined in Rule 6710(p). “TRACE-Eligible Security” does not include a debt security that is issued by a foreign sovereign or a Money Market Instrument as defined in Rule 6710(o).

⁴ “Agency Debt Security” generally includes a debt security (i) issued or guaranteed by an Agency as defined in Rule 6710(k); (ii) issued or guaranteed by a Government-Sponsored Enterprise (“GSE”) as defined in Rule 6710(n); or (iii) issued by a trust or other entity that was established or sponsored by a GSE for the purpose of issuing debt securities, where such enterprise provides collateral to the trust or other entity or retains a material net economic interest in the reference tranches associated with the securities issued by the trust or other entity. Rule 6710(n) provides that “Government-Sponsored Enterprise” has the same meaning as defined in 2 U.S.C. § 622(8).

transaction or a capped amount, depending on whether the security is rated as Investment Grade,⁵ Non-Investment Grade,⁶ or is unrated. For transactions in Agency Debt Securities that are either Investment Grade or unrated, FINRA disseminates the actual size of the trade for transactions less than or equal to \$5 million in par value traded, thus providing actual transaction size up to \$5 million, and disseminates “\$5MM+” for trades exceeding \$5 million in par value traded.⁷ For transactions in Agency Debt Securities that are Non-Investment Grade, FINRA disseminates the actual size of the trade for transactions less than or equal to \$1 million in par value, and disseminates “1MM+” for trades exceeding \$1 million in par value traded.⁸

⁵ Rule 6710 provides that “Investment Grade” means “a TRACE-Eligible Security that, if rated by only one nationally recognized statistical rating organization (“NRSRO”), is rated in one of the four highest generic rating categories; or if rated by more than one NRSRO, is rated in one of the four highest generic rating categories by all or a majority of such NRSROs; provided that if the NRSROs assign ratings that are evenly divided between (i) the four highest generic ratings and (ii) ratings lower than the four highest generic ratings, FINRA will classify the TRACE-Eligible Security as Non-Investment Grade for purposes of TRACE. If a TRACE-Eligible Security is unrated, for purposes of TRACE, FINRA may classify the TRACE-Eligible Security as an Investment Grade security. FINRA will classify an unrated Agency Debt Security as defined in [Rule 6710(l)] as an Investment Grade security for purposes of the dissemination of transaction volume.” See FINRA Rule 6710(h).

⁶ Rule 6710 provides that “Non-Investment Grade” means “a TRACE-Eligible Security that, if rated by only one NRSRO, is rated lower than one of the four highest generic rating categories; or if rated by more than one NRSRO, is rated lower than one of the four highest generic rating categories by all or a majority of such NRSROs. Except as provided in paragraph (h), if a TRACE-Eligible Security is unrated, FINRA may classify the TRACE-Eligible Security as a Non-Investment Grade security.” See FINRA Rule 6710(i).

⁷ See Securities Exchange Act Release No. 59733 (April 8, 2009), 74 FR 17709 (April 16, 2009) (Notice of Filing of File No. SR-FINRA-2009-010).

⁸ See supra note 7.

FINRA is proposing to apply a \$5 million dissemination cap to all Agency Debt Securities, regardless of the rating assigned to the security. When adopting the original dissemination caps for Agency Debt Securities, FINRA believed that unrated Agency Debt Securities should default to the \$5 million dissemination cap due to factors such as that they trade more consistently with Investment Grade securities that are subject to the \$5 million dissemination cap. While Non-Investment Grade Agency Debt Securities have been disseminated with the \$1 million dissemination cap, FINRA is not aware of the existence of any Non-Investment Grade Agency Debt Securities other than credit risk transfer securities (“CRTs”), a type of Agency Debt Security issued by Fannie Mae (“Fannie”) and Freddie Mac (“Freddie”). Based on experience gained with CRTs and in consultation with Fannie and Freddie, FINRA believes that it is appropriate to disseminate Non-Investment Grade CRTs with the \$5 million dissemination cap. Because CRTs are the only type of Agency Debt Security rated less than Investment Grade, FINRA is proposing to simplify the dissemination structure by applying the \$5 million dissemination cap to all Agency Debt Securities irrespective of rating.

FINRA notes that transactions in the vast majority of securities issued by Fannie and Freddie are disseminated with the actual size of the trade (uncapped), and, of those that are capped, the vast majority are disseminated with the \$5 million cap: 94.4% of all transactions in direct obligations issued by Fannie and Freddie, including CRTs, currently are disseminated with the actual size of the trade. Of the remaining 5.6% that are capped (both at \$1 million and \$5 million), 95% currently are disseminated with the \$5 million cap. Thus, FINRA believes that the proposed modification to apply the \$5 million dissemination cap to all Agency Debt Securities uniformly will have a minimal impact,

while simplifying the dissemination structure and providing additional transparency in Agency Debt Securities.

If the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 120 days following publication of the Regulatory Notice announcing Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁹ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The proposed rule change would benefit investors in that it would simplify the dissemination structure by creating a uniform dissemination protocol for all Agency Debt Securities, and would increase transparency for transactions in Non-Investment Grade Agency Debt Securities over \$1 million. Additionally, the proposed rule change would have a minimal impact as the vast majority of capped transactions in Agency Debt Securities are already disseminated with the \$5 million cap.

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

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

⁹ 15 U.S.C. 78q-3(b)(6).

Economic Impact Assessment

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the potential economic impacts, including anticipated costs, benefits, and distributional and competitive effects, relative to the current baseline, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

Economic Baseline

As of December 31, 2017, there were 35 Investment Grade, 9 Non-Investment Grade, and 172 unrated CRT classes (based on TRACE data). FINRA notes that certain CRTs are currently the only type of Agency Debt Security with a Non-Investment Grade rating. The outstanding amount of these issues are \$770 million, \$350 million and \$2,877 million for Investment Grade, Non-Investment Grade and unrated issues respectively. Table 1 presents the number of trades reported to TRACE and nominal trade value of CRT CUSIPs by rating for the calendar year beginning January 1, 2017.¹⁰

¹⁰ Each CRT deal utilizes a senior/subordinate structure in which credit protection is provided to the senior class by the subordinate classes in priority order. The senior class and subordinate tranches, while part of the same CRT issuance, are separate securities and each are assigned a unique CUSIP. In addition, each CRT class can be further tranching to provide additional optionality for investors' needs. As such, each CRT class is associated with multiple unique CUSIPs. We note that only the CUSIP associated with the senior tranche contributes to the amount of debt outstanding for a given CRT class.

Table 1

Grade	Trades		Trade Value	
	Number	Percent	Dollars (millions)	Percent
Non-Investment	1,950	13.6%	8,800.9	13.6%
Investment	1,988	13.8%	8,880.1	13.7%
Unrated	10,423	72.6%	47,077.7	72.7%

Under the existing dissemination protocols, Agency Debt Securities that are unrated or rated Investment Grade are disseminated with a \$5 million dissemination cap, where trades over \$5 million are displayed as “5MM+.” Non-Investment Grade Agency Debt Securities are disseminated with a \$1 million dissemination cap, where trades over \$1 million are displayed as “1MM+.” Table 2 presents the number and percent of trades and nominal trade value disseminated with actual trade sizes or displayed with “5MM+” for Investment Grade or unrated CRT CUSIPs for calendar year 2017. These statistics include all trades reported to TRACE during the period, and thus would include two trade reports for interdealer trades and one trade report for dealer to customer trades (two-sided trade data).¹¹

¹¹ For calendar year 2017, there were 11,341 trades reported to TRACE, that include only one trade report for interdealer trades and one trade report for dealer to customer trades (one-sided trade data), in Investment Grade and unrated CRT CUSIPs, of which 20.8% were displayed as “5MM+.”

Table 2

Grade	Trades			
	≤\$5M		>\$5M	
	Number	Percent	Number	Percent
Investment	1,524	76.7%	464	23.3%
Unrated	8,435	80.9%	1,988	19.1%
	Trade value			
	≤\$5M		>\$5M	
	Dollars (millions)	Percent	Dollars (millions)	Percent
Investment	2,591.5	29.2%	6,288.6	28.2%
Unrated	22,390.9	47.6%	24,686.7	46.6%

Table 3 presents the number and percent of trades and nominal trade value disseminated with actual trade sizes or displayed with “1MM+” for Non-Investment Grade CRT CUSIPs for calendar year 2017.¹²

Table 3

Grade	Trades			
	≤\$1M		>\$1M	
	Number	Percent	Number	Percent
Non-Investment	222	11.4%	1,728	88.6%
	Trade value			
	≤\$1M		>\$1M	
	Dollars (millions)	Percent	Dollars (millions)	Percent
Non-Investment	139.7	1.6%	8,661.2	98.4%

Economic Impact

Based on transactions during calendar year 2017, this proposal would have led to dissemination of additional trade size information for 1,112 trades in 82 CRT CUSIPs

¹² For calendar year 2017, there were 1,712 trades reported to TRACE, that include only one trade report for interdealer trades and one trade report for dealer to customer trades (one-sided trade data), in Non-Investment Grade CUSIPs, of which 88.3% were displayed as “1MM+.”

than disseminated under the current protocols. This increased transparency could have impacts on investors, market makers and issuers. Markets participants, especially uninformed investors, generally anticipate that they benefit from greater price transparency because, in the presence of this information, they are more likely to gain more timely information about the current price of an asset. Knowing this, they may be more willing to commit capital.¹³

At the same time, FINRA understands that some firms believe that transparency about the size of larger trades impedes their ability to commit capital and hence may have a negative impact on liquidity. Increasing transparency may increase the amount of information available to uninformed investors on transaction size and price. This may reduce the informed investors' relative advantage by decreasing the bid-ask spread earned by an informed investor or increasing the bid-ask spread paid by an informed investor. Furthermore, firms may be less willing to trade as principal and hold these securities in inventory, leading to wider spreads or less depth, if they fear that investors may identify the firms' inventory position.¹⁴ In addition, existing institutional investors that prefer trading in large sizes or at the current level of transparency in Non-Investment Grade CRTs may substitute trading in other asset classes, if the investors fear others may identify their holdings. The consensus of the academic literature studying the impact of

¹³ For instance, one study that examined corporate bond transactions in TRACE from January 2003 through January 2005 found that “[c]osts are lower for bonds with transparent trade prices, and they drop when the TRACE system starts to publicly disseminate their prices. The results suggest that public traders benefit significantly from price transparency.” For additional details, see Amy K. Edwards, Lawrence E. Harris, and Michael S. Piwowar, *Corporate Bond Market Transaction Costs and Transparency*, *Journal of Finance* 62, No. 3, 1421–1451 (2007).

¹⁴ See supra note 13.

transparency in a variety of settings in U.S. fixed income markets is that greater transparency is associated with lower costs to end customers and positive to neutral impacts on market liquidity.¹⁵ In addition, FINRA has discussed the proposed rule change with Fannie and Freddie, both of which support the application of the \$5 million dissemination cap to all CRTs.

Alternatives

No alternatives are under consideration.

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

Written comments were neither solicited nor received.

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

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

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

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

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

¹⁵ See supra note 13.

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2018-032 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2018-032. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 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. Persons submitting comments are cautioned that we do not redact or edit personal

identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2018-032 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁶

Robert W. Errett
Deputy Secretary

¹⁶ 17 CFR 200.30-3(a)(12).

EXHIBIT 5

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

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6000. QUOTATION, ORDER, AND TRANSACTION REPORTING FACILITIES

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6700. TRADE REPORTING AND COMPLIANCE ENGINE (TRACE)

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6710. Definitions

The terms used in this Rule 6700 Series shall have the same meaning as those defined in the FINRA By-Laws and rules unless otherwise specified. For the purposes of this Rule 6700 Series, the following terms have the following meaning:

(a) through (g) No Change.

(h) “Investment Grade” means a TRACE-Eligible Security that, if rated by only one nationally recognized statistical rating organization (“NRSRO”), is rated in one of the four highest generic rating categories; or if rated by more than one NRSRO, is rated in one of the four highest generic rating categories by all or a majority of such NRSROs; provided that if the NRSROs assign ratings that are evenly divided between (i) the four highest generic ratings and (ii) ratings lower than the four highest generic ratings, FINRA will classify the TRACE-Eligible Security as Non-Investment Grade for purposes of TRACE. If a TRACE-Eligible Security is unrated, for purposes of TRACE, FINRA may classify the TRACE-Eligible Security as an Investment Grade security. FINRA will classify any [unrated] Agency Debt Security as defined in paragraph (l) as an Investment Grade security for purposes of the dissemination of transaction volume.

(i) through (ii) No Change.

••• **Supplementary Material:** -----

No Change.

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