ATS Fixed Income Trading Volume

FINRA Requests Comment on a Proposal to Publish ATS Volume Data for Corporate Bonds and Agency Debt Securities on FINRA’s Website

Comment Period Expires: September 7, 2019

Summary
FINRA requests comment on a proposal to expand the alternative trading system (ATS) volume data that it publishes on its website to include information on transactions in corporate bonds and agency debt securities that occur within an ATS and are reported to FINRA’s Trade Reporting and Compliance Engine (TRACE).

Questions concerning this Notice should be directed to:
- Chris Stone, Vice President, Transparency Services, at (202) 728-8457 or chris.stone@finra.org;
- Patrick Geraghty, Vice President, Market Regulation, at (240) 386-4973 or patrick.geraghty@finra.org;
- Racquel Russell, Associate General Counsel, Office of General Counsel (OGC), at (202) 728-8363 or racquel.russell@finra.org; or
- Robert McNamee, Assistant General Counsel, OGC, at (202) 728-8012 or robert.mcnamee@finra.org.

Referenced Rules
- FINRA Rule 6110
- FINRA Rule 6610
- FINRA Rule 6710
- FINRA Rule 6720
- FINRA Rule 6730
- FINRA Rule 6732
- FINRA Rule 6750
Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by September 7, 2019.

Comments must be submitted through one of the following methods:

- Emailing comments to pubcom@finra.org; or
- Mailing comments in hard copy to:
  Jennifer Piorko Mitchell
  Office of the Corporate Secretary
  FINRA
  1735 K Street, NW
  Washington, DC 20006-1506

To help FINRA process comments more efficiently, persons should use only one method to comment on the proposal.

Important Notes: The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this Notice will be made available to the public on the FINRA website. Generally, FINRA will post comments as they are received.¹

Before becoming effective, the proposed rule change must be filed with the Securities and Exchange Commission (SEC) pursuant to Section 19(b) of the SEA.²

Background & Discussion

To improve market transparency relating to trading occurring on ATSs, in June 2014, FINRA began publishing individual ATS volume information for equity securities on its website.³ In its proposed rule change relating to ATS data publication, FINRA stated that it intended “periodically to assess the reporting and publication of information to consider whether modifications to the scope of securities covered, the delay between the activity and publication, or the frequency of publication of the information are appropriate.”⁴ FINRA also stated that it would not publish data for TRACE-Eligible Securities⁵ until FINRA “had the opportunity to evaluate the data…and the differences between the existing trade reporting regimes applicable to equity and debt securities.”⁶ Since that time, FINRA has been evaluating ATS data and believes it is now appropriate to include individual ATS volume data for certain TRACE-Eligible Securities.
Accordingly, FINRA is soliciting comment on a proposal to publish volume and trade count information for corporate and agency debt securities, categorized by individual security (i.e., CUSIP) and ATS, in a format similar to that currently published for equity securities. The published data would include both the total number of transactions and aggregate dollar volume traded for transactions in a particular corporate bond or agency debt security executed within the ATS and reported to FINRA during the aggregation period. The ATS data would be aggregated on a monthly basis and published with a three-month delay (e.g., aggregate ATS data for the month of February 2019 would be published in June 2019). FINRA would not charge for the aggregated ATS fixed income data, which would be published on FINRA’s website.

While FINRA recognizes that there are other significant fixed income electronic trading platforms that are not ATSs, for example, request-for-quote (RFQ) platforms, FINRA believes it is appropriate at this time to take a phased and measured approach, as was done with equity securities. Specifically, the proposal would initially be limited to ATSs, which currently are identifiable in TRACE by a unique market participant identifier (MPID) pursuant to Rule 6720(c) (Alternative Trading Systems). FINRA also believes it is appropriate initially to limit fixed income ATS data publication to corporate and agency debt securities because these product types account for the majority of publicly identified ATS activity in TRACE-Eligible Securities. FINRA may consider including additional asset classes in published ATS volume data in the future; e.g., transactions involving Securitized Products.

Similar to the approach with the publication of ATS equity volume, FINRA proposes initially to require that each ATS self-report to FINRA its aggregate weekly volume information and number of trades, by security, in corporate and agency debt securities that are TRACE-Eligible Securities. Self-reporting by ATSs would occur on a security-by-security basis within seven business days after the end of each week. FINRA would then publish the data as described above. As with the ATS equity volume data, FINRA staff intends to compare the self-reported ATS volume data with the transaction information firms report to TRACE to verify the accuracy of volume and trade counts. Once FINRA is comfortable with relying on trade reporting data to calculate the volume, it would eliminate the self-reporting requirement and would derive the published data directly from the transaction information reported to TRACE.

FINRA proposes that the published data would reflect: (1) sale trades and related volume reported by the ATS; and (2) the sell-side of trades and related volume between member subscribers where the ATS is identified on the trade report pursuant to Rule 6730(c)(13) (i.e., an exempt ATS). FINRA believes this approach would help ensure that the published trade counts and corresponding volume information do not reflect multi-leg or dually reported transactions more than once.
Economic Impact Assessment

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the regulatory need for the proposed rule change and its potential economic impacts, including anticipated costs and benefits.

Regulatory Need

FINRA is proposing to publish volume and trade count information for corporate and agency debt securities, with the intent to improve market transparency relating to trading in these instruments on ATSs. As mentioned above, FINRA makes similar information for equity securities available to the public, and has received support from the industry on its transparency initiatives in the equity markets.¹⁶

Economic Baseline

Pursuant to FINRA Rule 6720(c) (Alternative Trading Systems), since February 2, 2015, TRACE participants that operate an ATS have been required to use a separate MPID to report all transactions that are executed within the ATS to TRACE. Also, since 2016, disseminated TRACE transactions contain a new identifier to indicate when the reporting party or contra-party is an ATS or when a trade is executed on an ATS.¹⁷ Therefore, market participants can today observe real-time whether a party to a disseminated transaction is a dealer, non-member affiliate of a member, customer or an ATS.

However, real-time dissemination does not disclose the identity of the ATSs, as all ATSs are identified using a generic ATS reporting party and contra-party type and an ATS flag. Hence, market participants currently lack a relevant component in evaluating the historical location of liquidity in individual corporate bond and agency debt issues.

To assess the current structure of the market, FINRA analyzed a sample of corporate bond and agency debt transactions reported to TRACE between August 2016 and November 2018. In the sample period, there were, on average, 923,511 trades in a month for corporate bonds and 32,474 trades in a month for agency debt, corresponding to an average monthly dollar volume of approximately $427 billion and $66 billion, respectively. Trades in corporate bonds occurred on 16 unique ATSs and trades in agency debt securities occurred on nine unique ATSs. While ATS trades accounted for between 25 percent and 30 percent of total transactions in all corporate bonds, for agency debt securities, such statistic increased from approximately 18 percent in the beginning of the sample period to over 30 percent in the last quarter of 2018.

There were, on average, 20,566 and 3,001 unique corporate bond and agency debt CUSIPs, respectively, that traded in a given month during the sample period. Approximately 59 percent of the corporate bond and 54 percent of the agency debt CUSIPs that traded in a given month traded on at least one ATS. In the sample of bonds that traded on at least one ATS, a corporate bond traded, on average, on 2.43 ATSs in a given month, whereas the same figure was 1.52 for an agency debt security.
Approximately 98 percent of the trading activity on ATSs occurred against broker-dealers, whereas the remaining were against other market participants; i.e., customers or non-member affiliates of broker-dealers. An ATS had, on average, 63 broker-dealer counterparties in a month in corporate bonds and 31 broker-dealer counterparties in agency debt.

**Economic Impacts**

The current proposal would expand the benefits of FINRA’s ATS transparency program to market participants by providing transparency on monthly aggregate trading on ATSs in corporate bond and agency debt securities. The additional information may help broker-dealers and their customers in assessing where liquidity is concentrated, and may mitigate some of the search costs associated with seeking a counterparty to a trade. Economic theory suggests that reduced search costs would be associated with fewer lost opportunities to trade. Similarly, such information may inform routing decisions and may help achieve a better execution, such as by providing a better price or a faster execution.

As noted above, the proposed rule change initially imposes a new weekly reporting obligation on ATSs. FINRA expects that ATSs impacted by this proposal should already maintain this information pursuant to Regulation ATS. Because of the existing recordkeeping obligations in Regulation ATS, FINRA does not believe that the weekly reporting requirements in the proposed rule change will impose significant costs on firms or will require firms to expend significant resources.

As discussed above, once FINRA eliminates the self-reporting requirement and starts deriving the published data directly from the transaction data, the proposal to publish aggregate ATS trade counts and volume data would not impose any additional reporting requirements on firms, and as a result would impose no direct costs on firms. Some ATSs may choose to incur costs to verify the information FINRA publishes (e.g., trade counts), but these costs are not anticipated to be material and would be incurred only at the discretion of the ATS.

In developing this proposal, FINRA considered the potential impacts on competition, both among firms and ATSs. Specifically, FINRA considered the potential that market participants could reverse engineer the aggregated trade counts and volume data. Such data could potentially be analyzed to infer whether there was a single counterparty to an ATS trade in a given CUSIP, in a given month, on an ATS. In such a case, it may be possible for a participant to take advantage of such information when the same counterparty tries to take a position on the opposite side of the trade. However, the publication would be subject to a three month delay, which could mitigate such potential impact.
The analysis of the trade data between August 2016 and November 2018 indicated that, in the sample period, aggregate monthly trade counts and volume data at the CUSIP and ATS level would include trading activity of, at the median, two (one) broker-dealers in corporate (agency) TRACE-eligible securities on a given ATS. Over the sample period, 38 percent (66 percent) of the transactions in the monthly reports would be associated with a single broker-dealer, assuming no de minimis threshold on the number of parties to transactions on an ATS.

However, in the sample period, 50 percent of those broker-dealers would have trading activity with at least one other counterparty (for corporate bonds), whereas the same figure is only 19 percent for the broker-dealers in agencies, in a given CUSIP. Furthermore, CUSIPs that traded on at least one ATS in a given month, traded, on average, four to ten times more than CUSIPs that did not trade on at least one ATS. This finding implies that the proposed ATS reports would contain trade information for relatively more liquid securities where reverse engineering of trading patterns would be potentially less likely. Therefore, the proposed ATS reports are not likely to be useful in estimating the trading strategies or complete inventories of broker-dealers.

FINRA also considered the direct competitive effects on ATSs that may potentially arise from disseminating the proposed trade data. To the extent that this information is not already observed by market participants, ATS subscribers who discover that trading had been concentrated—due to relatively higher liquidity or other reasons—in a single ATS or a few ATSs in a given CUSIP may choose to send orders exclusively to those ATSs. As a result, other ATSs that have relatively smaller trading volume may lose some market share in that CUSIP. Similarly, new ATSs may potentially find it harder to enter the market due to the heightened barriers to entry caused by the disclosure of information regarding concentration of trading in certain ATSs.

Alternatives Considered
FINRA will consider alternatives based on the feedback to the proposal.

Request for Comment
FINRA seeks comments on the proposal outlined above regarding publication of fixed income ATS volume information. FINRA requests that commenters provide empirical data or other factual support for their comments wherever possible. In addition to general comments, FINRA specifically requests comments on the following questions:

▶ Would expansion of individual ATS volume data to include information on corporate and agency debt securities provide valuable information to the marketplace?
▶ What, if any, benefits would commenters anticipate if FINRA were to begin publishing ATS volume data for corporate and agency debt instruments on its website?
What, if any, concerns, including potential information leakage and reverse engineering concerns, would commenters have if FINRA were to begin publishing this ATS volume data on its website?

Are there any potential competitive advantages or disadvantages to attributing corporate and agency debt transaction volume by ATS?

Could the proposed publication of ATS corporate and agency debt volume data create barriers to entry for new ATSs, and if so, please describe?

Should FINRA consider a de minimis activity threshold under which an ATS would not be identified in the published reports with respect to a security or would be aggregated with the volume of other ATSs, and, if so, what would be an appropriate threshold?

FINRA proposes that the ATS volume and trade count data would reflect the sell-side of trades reported by an ATS and the sell side of inter-dealer trades where the ATS is identified on the trade report pursuant to Rule 6730(c)(13). Do commenters agree that this approach is the most appropriate? If not, what other approach would be more appropriate and why?

FINRA proposes to publish volume and trade count data by ATS and CUSIP for corporate and agency debt securities on a monthly aggregation schedule with a three-month delay. Do commenters agree with this approach?

Is there an alternative schedule that might be more appropriate than monthly aggregation, and, if so, why?

Is there an alternative delay period that might be more appropriate than three months, and, if so, why?

Should aggregation periods or publication delays differ for corporates versus agencies, and, if so, why?

Are there other types of tiering of the aggregation period or publication delays, based on volume, number of trades or some other factor, FINRA should consider? If so, what are they and why?

Should FINRA consider groupings other than by CUSIP, such as by investment rating (e.g., investment grade rated and high yield categories by trade size), or some other factor?

FINRA proposes initially to limit publication of ATS data to corporates and agencies. FINRA intends in the future to reconsider the appropriateness of including other types of disseminated TRACE-Eligible Securities.

Do commenters agree with this approach? Would commenters suggest that FINRA include any different assets classes for initial publication, and, if so, why?
What, if any, issues do commenters anticipate if FINRA were to expand publication of fixed income ATS volume data to include other asset classes in the future, such as Securitized Products?

How would commenters like to see corporate and agency debt ATS volume data displayed; e.g., what categories or groupings of data would be most helpful?

FINRA proposes to limit the current fixed income publication initiative to data on transactions that occur within an ATS. However, as noted above, FINRA is aware that there are other types of fixed income electronic trading platforms that are not ATSs. Should FINRA consider broadening the scope of the website publication initiative to include transactions on other fixed income trading mechanisms, such as RFQ platforms? If so, what types of platforms should be included, why, and how should they and/or the transactions executed on those platforms be defined and identified?

Are there any other issues specific to the fixed income markets that FINRA should consider in connection with publishing aggregate ATS corporate and agency debt volume data?
**Endnotes**

1. FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. See *NTM 03-73* (November 2003) (NASD Announces Online Availability of Comments) for more information.

2. See Section 19 of the Securities Exchange Act of 1934 (SEA) and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the *Federal Register*. Certain limited types of proposed rule changes, however, take effect upon filing with the SEC. See SEA Section 19(b)(3) and SEA Rule 19b-4.

3. See *OTC Transparency Data* (for the best experience, please view this site using the latest version of Chrome, Firefox, Safari or Internet Explorer).


5. Rule 6710(a) 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).


7. The published ATS data would include the CUSIPs that are disseminated as part of FINRA’s Corporate Bond Data Set and Agency Data Set.

8. See *OTC Transparency Data* (for the best experience, please view this site using the latest version of Chrome, Firefox, Safari or Internet Explorer).

9. By contrast, ATS data for equity securities is aggregated on a weekly basis and publication delays vary from two weeks for Tier 1 NMS stocks to four weeks for OTC equities. See Rules 6110 and 6610.

10. FINRA would not include within the published ATS data any information on transactions in corporate or agency debt securities that FINRA does not disseminate pursuant to Rule 6750.

11. “Securitized Product” generally includes a security collateralized by any type of financial asset, such as a loan, a lease, a mortgage, or a secured or unsecured receivable, and includes but is not limited to an asset-backed security as defined in SEA Section 3(a)(79)(A), a synthetic asset-backed security, and any residual tranche or interest of any such security, which tranche or interest is a debt security for purposes of Rule 6710(a) and the Rule 6700 Series.

13. Where the ATS is a reporting party and stands in between a trade on its platform (either between two members or between a member and a non-member), the published data will reflect only the ATS sale in connection with the overall transaction.

14. Rule 6730(c)(13) requires that, where a member is reporting a transaction that occurred on an exempt ATS (pursuant to an exemption granted under Rule 6732), the member must include the ATS’s separate MPID. FINRA would not require exempt ATSs that currently report trade data on a monthly basis under Rule 6732 to separately self-report volume and trade count data for exempt transactions.

15. The published data would not include the buy-side of any member subscriber trades, or the sell-side of trades by a member subscriber against an ATS.
