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May 10, 2022

VIA ELECTRONIC MAIL


Vanessa Countryman, Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Room 10915
Washington, D.C. 20549-1090

Re: FINRA's Statement in Support of Proposed Rule Change to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (File No. SR-FINRA-2021-010)

Dear Secretary Countryman,

Enclosed is the Financial Industry Regulatory Authority, Inc.'s ("FINRA") Statement in Support of Proposed Rule Change to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (File No. SR-FINRA-2021-010).

Respectfully submitted,


Nowell D. Bamberger

Enclosure

cc: Cooper & Kirk, PLLC and Olshan Frome Wolosky LLP, counsel for Bond Dealers of America and Brean Capital, LLC

**BEFORE THE
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C.**

In the Matter of)	
)	
Proposed Rule Change, as Modified by)	File No. SR-FINRA-2021-010
Amendment No. 1, to Amend the Requirements)	
for Covered Agency Transactions under FINRA)	
Rule 4210 (Margin Requirements) as Approved)	
Pursuant to SR-FINRA-2015-036)	

**FINRA’S STATEMENT IN SUPPORT OF PROPOSED RULE CHANGE
TO AMEND THE REQUIREMENTS FOR
COVERED AGENCY TRANSACTIONS UNDER FINRA RULE 4210**

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Dated: May 10, 2022

TABLE OF CONTENTS

I. SUMMARY	1
II. BACKGROUND	6
A. The 2015 Rulemaking and SR-FINRA-2015-036.....	6
B. The 2021 Rulemaking and SR-FINRA-2021-010’s Amendments to the Previously-Approved Margin Requirements for CATs.	9
C. FINRA’s Longstanding Regulation of Margin Requirements for Its Members.	11
III. ARGUMENT	12
A. FINRA’s Statutory Authority to Issue SR-FINRA-2021-010 and SR-FINRA-2015-036 Is Well-Established.	13
B. The Narrow Amendments to FINRA Rule 4210 Set Forth in SR-FINRA-2021-010 Are in Accordance with Section 15A of the Exchange Act and Are Consistent with the Commission’s Previous Grants of Approval to FINRA Rulemaking in This Area.	21
1. The Thorough Factual Record Developed by FINRA and the Division Is More Than Sufficient for the Commission to Conclude That SR-FINRA-2021-010 Satisfies the Requirements of the Exchange Act.	22
2. In Promulgating SR-FINRA-2021-010, FINRA and the Commission Complied with All Applicable Procedural Requirements.	29
3. Petitioners’ Remaining Contentions Are Merely Objections to SR-FINRA-2015-036 and Margin Requirements Generally.	31
C. Even if the Commission Were to Re-Analyze SR-FINRA-2015-036, That Amendment to FINRA Rule 4210 Also Complies with and Is Consistent with FINRA’s Rulemaking Authority.	37
IV. CONCLUSION	43

TABLE OF AUTHORITIES

Cases

<i>FTC v. Ken Roberts Co.</i> , 276 F.3d 583 (D.C. Cir. 2001).....	16
<i>Hall v. United States</i> , 556 U.S. 506 (2012).....	18
<i>Household Credit Servs. v. Pfennig</i> , 541 U.S. 232 (2004).....	18
<i>Mayo v. Dean Witter Reynolds, Inc.</i> , 258 F. Supp. 2d 1097 (N.D. Cal. 2003).....	13
<i>Motor Vehicle Mfrs. Ass’n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.</i> , 463 U.S. 29 (1983).....	31
<i>Myers v. Merrill Lynch & Co.</i> , No. C-98-3532 WHO, 1999 U.S. Dist. LEXIS 22642 (N.D. Cal. Aug. 23, 1999).....	13
<i>Nat’l Mining Ass’n v. Mine Safety & Health Admin.</i> , 512 F.3d 696 (D.C. Cir. 2008).....	31
<i>New York Republican State Comm. v. Sec. & Exch. Comm’n</i> , 927 F.3d 499 (D.C. Cir. 2019).....	13, 16-17
<i>Sharemaster v. Sec. & Exh. Comm’n</i> , 847 F.3d 1059 (9th Cir. 2017)	15

Federal Statutes, Regulations, and Rules

12 C.F.R. § 220.1 (2021)	5, 17
17 C.F.R. § 41.42(c) (2021)	20
17 C.F.R. § 201.430(b)(1).....	21
17 C.F.R. § 201.430(c) (2021).....	21
17 C.F.R. § 240.15c3-1 (2021).....	4, 26-27
17 C.F.R. § 240.17a-4 (2021).....	17

5 U.S.C. § 704.....	22
15 U.S.C. § 78.....	17
15 U.S.C. § 78c.....	22
15 U.S.C. § 78f.....	38
15 U.S.C. § 78g.....	15-16
15 U.S.C. § 78o-3.....	<i>passim</i>
15 U.S.C. § 78s.....	13, 17, 30
15 U.S.C. § 78y.....	22
Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763 (2000)	20
National Securities Markets Improvement Act, Pub. L. No. 104-290, § 101, 110 Stat. 3416 (1996).....	18
Secondary Mortgage Market Enhancement Act, Pub. L. No. 98-440, 98 Stat. 1689 (1984).....	19
FINRA Rule 4210	<i>passim</i>
FINRA Rule 4510	17
FINRA Rule 6710	1
NASD Rule 2520	19
NYSE Rule 431.....	11-12, 15, 19
SEC Rule 15c3-3(k).....	24

Federal Register Releases

<i>Extension and Maintenance of Credit by Brokers, Dealers, and Members of National Securities Exchanges</i> , File No. 43-94, 2 Fed. Reg. 3368 (Dec. 21, 1937)	17-18
<i>Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Extend the Implementation Date of Certain Amendments to FINRA Rule 4210 Approved Pursuant to SR-FINRA-2015-036</i> , Securities Exchange Act Release No. 94356, File No. SR-FINRA-2022-003, 87 Fed. Reg. 13,337 (Mar. 9, 2022)	9

<i>Notice of Filing of a Proposed Rule Change To Amend FINRA Rule 4210 (Margin Requirements) To Establish Margin Requirements for the TBA Market, Securities Exchange Act Release No. 76148, File No. SR-FINRA-2015-036, 80 Fed. Reg. 63,603 (Oct. 20, 2015)</i>	<i>38, 40-42</i>
<i>Notice of Filing of Amendment No. 3 and Order Granting Accelerated Approval to 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, 2, and 3, Securities Exchange Act Release No. 78081, File No. SR-FINRA-2015-036, 81 Fed. Reg. 40364 (June 21, 2016)</i>	<i>passim</i>
<i>Order Approving a Proposed Rule Change to Adopt FINRA Rule 4210 (Margin Requirements), FINRA Rule 4220 (Daily Record of Required Margin) and FINRA Rule 4230 (Required Submissions for Requests for Extensions of Time under Regulation T and SEC Rule 15c3-3) in the Consolidated FINRA Rulebook, Securities Exchange Act Release No. 62482, File No. SR-FINRA-2010-024, 75 Fed. Reg. 41,562 (July 12, 2010)</i>	<i>29</i>
<i>Order Approving Proposed Rule Change and Amendment Nos. 1, 2, and 3 by the New York Stock Exchange, Inc. Relating to Margin Requirements, Securities Exchange Act Release No. 48365, File No. SR-NYSE-98-14, 68 Fed. Reg. 51314 (Aug. 19, 2003).....</i>	<i>19</i>
<i>Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 1 and 2 by the National Association of Securities Dealers, Inc. Relating to Margin Requirements, Securities Exchange Act Release No. 48407, File No. SR-NASD-2000-08, 68 Fed. Reg. 52,259 (Sept. 2, 2003).....</i>	<i>19</i>
<i>Order Granting Approval of a Proposed Rule Change, as Modified by Amend. No. 1, to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (Margin Requirements) as Approved Pursuant to SR-FINRA-2015-036, Securities Exchange Act Release No. 94013, File No. SR-FINRA-2021-010, 87 Fed. Reg. 4,076 (Jan. 26, 2022)</i>	<i>passim</i>
<i>Order Granting Approval of a Proposed Rule Change Relating to Amends. to FINRA Rules 2360 and 4210 in Connection with OCC Cleared Over-the-Counter Options, Securities Exchange Act Release No. 70619, File No. SR-FINRA-2013-027, 78 Fed. Reg. 62,722 (Oct. 7, 2013)</i>	<i>14, 26</i>
<i>Order Granting Approval of a Proposed Rule Change, as Modified by Amend. No. 1, to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (Margin Requirements) as Approved Pursuant to SR-FINRA-2015-036, Securities</i>	

Exchange Act Release No. 94013, File No. SR-FINRA-2021-010, 87 Fed. Reg. 4,076 (Jan. 26, 2022).....	2
<i>Order Granting Approval of Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amend. No. 1 thereto by the Nat’l Ass’n of Sec. Dealers, Inc., Relating to the Amend. of its Margin Rules, Securities Exchange Act Release No. 38729, File No. SR-NASD-97-14, 62 Fed. Reg. 32,669 (June 10, 1997)</i>	14
<i>Order Granting Approval of Proposed Rule Changes, Securities Exchange Act Release No. 24114, File Nos. SR-NYSE-86-4 and -30, 52 Fed. Reg. 7,245 (Mar. 9, 1987).....</i>	19
<i>Order Granting Approval of Proposed Rule Change Relating to Margin Requirements, Securities Exchange Act Release No. 31918, File No. SR-NASD-92-35, 58 Fed. Reg. 12,286 (Mar. 3, 1993)</i>	14, 20
<i>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, Securities Exchange Act Release No. 76908, File No. SR-FINRA- 2015-036, 81 Fed. Reg. 3,532 (Jan. 21, 2016)</i>	40-41
<i>Use of Derivatives by Registered Investment Companies and Business Development Companies, Investment Company Act Release No. 34084, File No. S7-24-15, 85 Fed. Reg. 83,162 (Dec. 21, 2020).....</i>	28
Other Authorities	
Charles F. Rechlin et al., <i>Securities Credit Regulation</i> § 1:5-1:7 (2d ed. 2021).....	11-12
Dep’t of Labor Advisory Op. 2013-01A (Feb. 7, 2013).....	28
<i>FINRA Requests Comment on Proposed Amendments to FINRA Rule 4210 for Transactions in the TBA Market, Regulatory Notice 14-02 (Jan. 2014)</i>	6-7, 40
H.R. Rep. No. 73-1383 (1934)	19-20
James Largay, <i>100% Margins: Combating Speculation in Individual Security Issues</i> , 28 J. Fin. 973 (1973).....	18
Jules I. Bogen & Herman E. Krooss, <i>Security Credit: Its Economic Role and Regulation</i> Ch. 7 (1960)	11
Letter from Adam Arkel, Associate General Counsel, FINRA, to SEC (Sept. 16, 2021)	11

Letter from Chris Killian, Managing Director, SIFMA, to SEC at 1 (June 15, 2021)	24
Letter from J. Matthew DeLesDernier, Assistant Secretary, SEC, to FINRA (Jan. 27, 2022).	10
Letter from Michael Nicholas, Chief Executive Officer, BDA, to FINRA (June 7, 2018), <i>available at</i> https://www.bdamerica.org/news-items/rule-4210-update-bda-submits- capital-charge-letter-to-finra/	9
<i>Notice of Filing of Amend. No. 1 and Order Granting Accelerated Approval of Proposed Rule Change, as Modified by Amend. No. 1, Relating to FINRA Rule 4210 (Margin Requirements)</i> , Securities Exchange Act Release No. 67751, File No. SR-FINRA- 2012-024 (Aug. 29, 2012)	14
<i>Opinion</i> , 1972 Fed. Res. Interp. Ltr. LEXIS 52 (June 28, 1972).....	20
<i>SEC Approval and Effective Date for New Consolidated FINRA Rules Regarding Margin Requirements, Daily Record of Required Margin, and Extension of Time Requests</i> , Regulatory Notice 10-45 (Dec. 2, 2010)	20-21
SR-FINRA-2015-036 (Oct. 6, 2015)	5
SR-FINRA-2015-036, Proposed Amend. No. 1 (Jan. 13, 2016)	5, 8, 41
SR-FINRA-2015-036, Proposed Amend. No. 2 (Mar. 21, 2016).....	5, 8
SR-FINRA-2015-036, Proposed Amend. No. 3 (May 26, 2016)	5, 8-9
SR-FINRA-2021-010 (May 7, 2021)	1, 3
SR-FINRA-2021-010, Proposed Amend. No. 1 (Aug. 9, 2021)	<i>passim</i>
Treasury Market Practice Group, Best Practices for Treasury, Agency Debt, and Agency Mortgage-Backed Securities Markets (May 23, 2013).....	7
Treasury Markey Practice Group, Best Practices for Treasury, Agency, Debt, and Agency Mortgage-Backed Securities Markets (Apr. 4, 2014)	8

**BEFORE THE
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC**

In the Matter of

Proposed Rule Change, as Modified by
Amendment No. 1, to Amend the Requirements
for Covered Agency Transactions under FINRA
Rule 4210 (Margin Requirements) as Approved
Pursuant to SR-FINRA-2015-036

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**FINRA’S STATEMENT IN SUPPORT OF PROPOSED RULE CHANGE
TO AMEND THE REQUIREMENTS FOR
COVERED AGENCY TRANSACTIONS UNDER FINRA RULE 4210**

I. SUMMARY

The action by the Division of Trading and Markets (the “Division”) under review concerns the approval, under delegated authority, of SR-FINRA-2021-010, as amended by Proposed Amendment No. 1 (the original proposed rule change and Proposed Amendment No. 1, as approved by the Division, “SR-FINRA-2021-010”). SR-FINRA-2021-010 is a rulemaking by the Financial Industry Regulatory Authority, Inc. (“FINRA”) amending provisions of a rulemaking previously approved by the Division under which FINRA members are generally required to collect margin on forward-settling To Be Announced (“TBA”) transactions, Specified Pool Transactions, and transactions in Collateralized Mortgage Obligations issued in conformity with a U.S. government agency or government-sponsored enterprise program (such transactions, collectively, “Covered Agency Transactions” or “CATs”).¹ See SR-FINRA-2021-010 (May 7,

¹ TBA, Specified Pool Transactions, and Collateralized Mortgage Obligations are further defined in FINRA Rule 6710.

2021); SR-FINRA-2021-010, Proposed Amend. No. 1 (Aug. 9, 2021); *Order Granting Approval of a Proposed Rule Change, as Modified by Amend. No. 1, to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (Margin Requirements) as Approved Pursuant to SR-FINRA-2015-036*, Securities Exchange Act Release No. 94013, File No. SR-FINRA-2021-010, 87 Fed. Reg. 4,076 (Jan. 26, 2022) (“2022 Approval Order”). On April 19, 2022, the Securities and Exchange Commission (the “Commission”) granted the petition by the Bond Dealers of America (“BDA”) and Brean Capital, LLC (“Brean”) (together, the “Petitioners”) for review of the Division’s 2022 Approval Order, 87 Fed. Reg. 4,076, regarding SR-FINRA-2021-010 (the “Petition”).

SR-FINRA-2021-010 is part of an effort by FINRA to address a significant source of potential systemic risk, and risk to its members: that of exposure to counterparty defaults on the purchase of forward-settling CATs during the often-lengthy period between such CATs’ trade and settlement dates. While market practice has evolved such that parties to forward-settling securities transactions are typically protected by an exchange of variation margin, the practice in the CAT market has been inconsistent and FINRA and others have observed that broker-dealers that participate in CATs are exposed to significant risk of loss in the event that their counterparties prove unable or unwilling to settle transactions when the market value of the relevant securities has moved against them between the trade and settlement dates. FINRA has proposed, and the Division, on behalf of the Commission, has approved proposed rule changes to FINRA Rule 4210, “Margin Requirements” (“FINRA Rule 4210”) that would better align the practices of its members with respect to CATs with those for other forward-settling securities transactions by requiring FINRA members to collect margin corresponding to the mark-to-market losses above a specified threshold.

The rulemaking under review, SR-FINRA-2021-010, is not the rulemaking that adopted the margin requirement for CATs. The underlying change to FINRA Rule 4210 was approved by the Division nearly six years ago. *See Notice of Filing of Amendment No. 3 and Order Granting Accelerated Approval to 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, 2, and 3*, Securities Exchange Act Release No. 78081, File No. SR-FINRA-2015-036, 81 Fed. Reg. 40364 (June 21, 2016) (“2016 Approval Order”), and parts of it are already in effect. SR-FINRA-2021-010, instead, reflects an effort by FINRA to respond to comments and engagement from its members and others—including Petitioners themselves—to amend the previously-approved rule change to provide greater flexibility; a direct response to concerns expressed about potential burdens FINRA Rule 4210, as amended by the 2015 rule change, could place on small and medium-sized broker-dealers. Specifically, SR-FINRA-2021-010:

- Eliminates the obligation on FINRA members to collect two percent maintenance margin on non-exempt accounts—meaning that the only margin required to be collected is an amount corresponding to the counterparty’s actual mark-to-market losses on the securities pre-settlement;
- Permits FINRA members to substitute a capital charge (up to certain limits) in lieu of collecting margin on CATs—addressing potential circumstances in which counterparties are unable or unwilling to post margin; and
- Makes other conforming and streamlining edits to FINRA Rule 4210.

Petitioners do not appear to object to these amendments, *per se*; rather, they acknowledge these changes as important and beneficial (and, in some respects, responsive to their own advocacy), although they argue that the changes may not go far enough. Rather, Petitioners’ real complaint is with the entire concept that FINRA members should be required to collect margin, or take capital charges for unmargined exposures, in connection with CATs. This is clear from their Petition, the majority of which is dedicated to the ultimately unavailing argument that FINRA

lacks authority to establish *any* margin requirements, that the Commission lacks statutory authority to approve such requirements, and that in any event there is no need for such requirements.

Petitioners' argument thus goes far beyond the scope of the 2022 Approval Order before the Commission now. The questions of whether FINRA can regulate the margin practices of its members, and whether FINRA can or should require its members to collect margin in connection with forward-settling CATs, were resolved by Commission action long ago, and are not properly before it now. And the requirement that FINRA members take a capital charge for unmargined mark-to-market losses is longstanding and reflected in the Commission's own rules as well as FINRA's. *See* 17 C.F.R. § 240.15c3-1 (2021) (SEC rule on "[n]et capital requirements for brokers or dealers"). The issue under review by the Commission now is narrow: whether the Division properly approved SR-FINRA-2021-010, on its own merits, taking the existing regulatory backdrop as the status quo. The record, including Petitioners' own comments, strongly supports that action.

On the question of whether FINRA has authority to establish rules governing the collection of margin in connection with securities transactions by its members, the law is clear and there is nothing new about FINRA adopting such requirements. Existing FINRA Rule 4210 imposes margin requirements in connection with a wide variety of securities transactions, and FINRA and other self-regulatory organization ("SROs") have had such rules in place for more than a half-century. The Commission has repeatedly approved such rules. Not only that, but the Board of Governors of the Federal Reserve (the "Federal Reserve Board" or the "Board")—which Petitioners argue has exclusive authority under Section 7 of the Exchange Act to regulate margin on securities transactions—has similarly had a rule in place since the 1930s that expressly reserves to SROs like FINRA the flexibility to "impos[e] additional requirements" beyond those established

by the Federal Reserve Board. *See* 12 C.F.R. § 220.1 (2021). Petitioners’ arguments swim against decades of Commission and Federal Reserve Board practice, FINRA rulemaking, and legislation, and it is therefore not surprising that Petitioners find zero authority to cite in support of their argument.

As for FINRA’s adoption of specific rule changes to FINRA Rule 4210 to govern the margin requirements for CATs, those requirements were introduced by SR-FINRA-2015-036, as amended by Proposed Amendments Nos. 1, 2, and 3, following an exhaustive rulemaking process and approval by the Division under delegated authority in 2016 (the original proposed rule change, as amended and as approved by the Division, “SR-FINRA-2015-036”). *See* SR-FINRA-2015-036 (Oct. 6, 2015); SR-FINRA-2015-036, Proposed Amend. No. 1 (Jan. 13, 2016); SR-FINRA-2015-036, Proposed Amend. No. 2 (Mar. 21, 2016); SR-FINRA-2015-036, Proposed Amend. No. 3 (May 26, 2016); *see also* 2016 Approval Order, 81 Fed. Reg. 40,364. In promulgating SR-FINRA-2015-036, FINRA and the Division recognized the market and systemic threat posed by unsecured credit risk in the CAT market, and concluded that the CAT market was unique—compared to the repo, securities lending, and derivatives markets which are subject to initial, maintenance, or mark-to-market margin requirements—for its lack of margin requirements. Neither Petitioners—who participated fully in that process—nor any other party sought Commission or judicial review of the Division’s approval of SR-FINRA-2015-036, which is now a final rule change, portions of which are already in effect with other requirements slated to take effect in October 2022. In approving SR-FINRA-2015-036, the Division gave a full hearing to all of the arguments Petitioners make now, including the arguments that FINRA lacked the statutory authority to require the collection of margin on CATs at all, and that a rule requiring the margining of such transactions is undesirable and would disadvantage FINRA members (particularly small and medium-sized firms) relative to

other market participants. The Division agreed with FINRA's analysis that SR-FINRA-2015-036 was consistent with the requirements of the Exchange Act, that FINRA had followed a proper rulemaking process to adopt it, that it did not unnecessarily burden competition, and accordingly, granted approval.

To the extent that Petitioners are asking the Commission to use this rulemaking process to re-open and re-litigate the approval of SR-FINRA-2015-036's margin requirements for CATs, under the guise of a petition for review of rule amendments to which they fundamentally do not object, the Commission should reject the invitation. The rulemaking process and the Commission's rules prescribe a process for fair and open hearing and debate on proposed SRO rules, but the Commission, FINRA, FINRA's members, and market participants in general also have an interest in finality once the rulemaking process has been completed. That is why the Commission's rules and the Exchange Act set time limits for Commission and judicial review, respectively, of SRO rules and Division approval orders issued under delegated authority.

In any event, were the Commission to review the underlying merits of the margin requirements created by SR-FINRA-2015-036 for CATs, it should find—as the Division now has done twice—that such requirements are consistent with the Exchange Act and should therefore be approved.

II. BACKGROUND

A. The 2015 Rulemaking and SR-FINRA-2015-036.

In January 2014, FINRA began a formal process of soliciting comments and input on potential rulemaking to clarify the requirements for FINRA members to collect margin on CATs. Regulatory Notice 14-02 (FINRA Requests Comment on Proposed Amendments to FINRA Rule 4210 for Transactions in the TBA Market) (Jan. 2014). That process followed on FINRA's own

observations over a period of years that the rules governing risk management in the CAT market were inconsistently applied by FINRA members and the adoption by the Treasury Market Practice Group (“TMPG”), a voluntary association sponsored by the Federal Reserve Bank of New York, of best practices guidelines (that have been updated periodically) that encouraged the collection of margin in connection with CATs. *See, e.g.*, TMPG, Best Practices for Treasury, Agency Debt, and Agency Mortgage-Backed Securities Markets (May 23, 2013) (last version adopted by TMPG before the start of FINRA CAT-related rulemaking). As FINRA recognized at the time, the CAT market is one of the largest fixed-income markets in the country, featuring, at the time, “approximately \$750 billion to \$1.5 trillion in gross unsettled and unmargined dealer to customer transactions.” Regulatory Notice 14-02, at 2.

In 2015, FINRA proposed changes to its existing margin requirements, FINRA Rule 4210, for securities transactions by members involving CATs. That commenced a formal rulemaking process that lasted for more than a year, and which included three amendments to the proposed rule change and separate requests for public comment. It resulted in SR-FINRA-2015-036, which was approved by the Division under delegated authority in June 2016. *See* 2016 Approval Order, 81 Fed. Reg. 40,364.

SR-FINRA-2015-036, as approved, establishes requirements for FINRA members to collect margin on CATs during the period between the trade dates and the settlement dates of such CATs, a period during which a FINRA member is exposed to otherwise uncollateralized risk of counterparty default. SR-FINRA-2015-036 was informed by, among other things, non-binding guidance published by the TMPG. *See* SR-FINRA-2015-036 at 6; 2016 Approval Order, 81 Fed. Reg. at 40,365. That guidance observed that market practice for CATs, which may settle a month or more after the initial trade date, did not consistently involve an exchange of collateral, exposing

the parties to such transactions to credit risk. TMPG, Best Practices for Treasury, Agency, Debt, and Agency Mortgage-Backed Securities Markets (Apr. 4, 2014). FINRA and the Division also cited concerns that the possibility of unmargined positions in the event of default in the CAT market creates substantial market and systemic risk, *id.*, and observed that the inconsistent market practice with respect to CATs diverged from the more general securities market convention and the rules applicable to other types of markets, including the repo and securities lending markets. *See* SR-FINRA-2015-036 at 6; 2016 Approval Order, 81 Fed. Reg. at 40,365. The margin requirements imposed by SR-FINRA-2015-036 closed that gap.

SR-FINRA-2015-036 was approved by the Division under delegated authority following a robust rulemaking process that considered more than a hundred comment letters over the course of nearly two years, and three amendments to the original proposed rule change published by FINRA. *See* SR-FINRA-2015-036, Proposed Amend. No. 1 (Jan. 13, 2016); SR-FINRA-2015-036, Proposed Amend. No. 2 (Mar. 21, 2016); SR-FINRA-2015-036, Proposed Amend. No. 3 (May 26, 2016). FINRA diligently engaged in extensive outreach with firms throughout the history of this rulemaking, including additional discussions with the Petitioners, who fully participated in that rulemaking process. Collectively, Petitioners submitted eleven comment letters between November 10, 2015 and September 10, 2021, and participated in five meetings or telephone calls with Commission staff between January 7, 2016 and June 14, 2016. After the Division approved SR-FINRA-2015-036, neither of the Petitioners (nor any of the dozens of other parties who commented on SR-FINRA-2015-036) submitted a petition for Commission review of SR-FINRA-2015-036 or sought judicial review. SR-FINRA-2015-036 was promulgated based on robust analyses of SR-FINRA-2015-036's potential effects on competition, SR-FINRA-2015-036's potential burdens on different types of market participants, including mortgage brokers,

broker-dealers, customers and consumers, the economic benefits and costs associated with SR-FINRA-2015-036, and the public comments received throughout the rulemaking process. SR-FINRA-2015-036 at 100-22.

In Proposed Amendment 3 to SR-FINRA-2015-036, FINRA stated that it would monitor the impact of SR-FINRA-2015-036 and whether it proved to be overly onerous or otherwise was shown to negatively impact the market, and, if necessary, consider revisions to SR-FINRA-2015-036 to mitigate any adverse impacts. *See* SR-FINRA-2015-036, Proposed Amend. No. 3 at 9. Consistent with that undertaking, FINRA continued discussions with market participants, including Petitioners. In June 2018, Petitioner BDA submitted a letter to FINRA advocating an amendment to SR-FINRA-2015-036 to permit FINRA members to take a capital charge in lieu of collecting margin, and representing that the views expressed reflected those of its members. Letter from Michael Nicholas, Chief Executive Officer, BDA, to FINRA at 1-2 (June 7, 2018) (“BDA Letter”).² In the meantime, FINRA also extended the implementation of the margin requirements imposed by SR-FINRA-2015-036 (but not the risk management requirements) to October 2022. *Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Extend the Implementation Date of Certain Amendments to FINRA Rule 4210 Approved Pursuant to SR-FINRA-2015-036*, Securities Exchange Act Release No. 94356, File No. SR-FINRA-2022-003, 87 Fed. Reg. 13,337 (Mar. 9, 2022).

B. The 2021 Rulemaking and SR-FINRA-2021-010’s Amendments to the Previously-Approved Margin Requirements for CATs.

In 2021, following the further dialogue and deliberations discussed above, FINRA commenced a new rulemaking process by publishing a proposed rule change limiting certain of

² BDA’s letter is publicly available at <https://www.bdamerica.org/news-items/rule-4210-update-bda-submits-capital-charge-letter-to-finra/>.

SR-FINRA-2015-036's modifications to FINRA Rule 4210. *See* SR-FINRA-2021-010. FINRA published the initial proposed rule change on May 7, 2021, and then published Proposed Amendment No. 1 on August 9, 2021. SR-FINRA-2021-010 is a narrow, limited, proposed rule change that makes three discrete changes to the previously-approved changes in SR-FINRA-2015-036. Specifically:

- Informed by engagement with FINRA members and industry groups, it eliminates the requirement that FINRA members collect two percent maintenance margin on non-exempt accounts under SR-FINRA-2015-036, eliminating one requirement of SR-FINRA-2015-036 and reducing the complexity of the overall rule. As a result, FINRA Rule 4210, as amended by SR-FINRA-2021-010, would *only* require members to collect margin for actual market-to-market losses, and not—as is more typical in the securities markets—to maintain margin to protect against future market movements.
- Subject to specified limits and conditions, SR-FINRA-2021-010 permits (but does not require) FINRA members to take a capital charge in circumstances where margin would otherwise be required under SR-FINRA-2015-036. This change follows directly from BDA's own suggestion. BDA Letter at 1-2 (June 7, 2018).
- It streamlines and consolidates the language of FINRA Rule 4210 to make it more straightforward to administer.

The Division approved SR-FINRA-2021-010 on January 20, 2022. 2022 Approval Order, 87 Fed. Reg. 4076. After Petitioners submitted a notice of intention to petition for review of SR-FINRA-2021-010, the Commission issued a stay of SR-FINRA-2021-010 pending its review. Letter from J. Matthew DeLesDernier, Assistant Secretary, SEC, to FINRA (Jan. 27, 2022).

Petitioners were closely involved in both the rulemaking processes for SR-FINRA-2015-036 and SR-FINRA-2021-010. In addition to their involvement in the SR-FINRA-2015-036 rulemaking process and the 2018 BDA Letter mentioned above, which followed the conclusion of the formal rulemaking process for SR-FINRA-2015-036, BDA and Brean, either individually or jointly, submitted three additional comment letters in connection with SR-FINRA-2021-010, and met (in person or by phone) with Commission staff two additional times (including one call with Commissioner Peirce). FINRA has specifically and explicitly addressed BDA and Brean's

comments on SR-FINRA-2015-036 throughout the rulemaking process. *See generally* SR-FINRA-2021-010, Proposed Amend. No. 1; Letter from Adam Arkel, Associate General Counsel, FINRA, to SEC (Sept. 16, 2021) (“FINRA Letter”).

C. FINRA’s Longstanding Regulation of Margin Requirements for Its Members.

SR-FINRA-2015-036 and SR-FINRA-2021-010 build on FINRA’s long history of regulation in this area. Contrary to Petitioners’ arguments, Petition at 1, there is nothing “unprecedented” about FINRA or other SROs promulgating rules requiring the exchange of collateral when its members enter into securities transactions that expose them to credit risk. Limitations on a broker-dealer’s authority to extend credit to its counterparties, or “margin requirements,” have existed since 1913—predating the Exchange Act itself. *See* Jules I. Bogen & Herman E. Krooss, *Security Credit: Its Economic Role and Regulation* Ch. 7 (1960). Such limitations have several purposes, including protecting the securities markets from fluctuations caused by excessive credit, which can cause upward and downward “spirals” in securities prices; protecting investors from over-leveraging, thereby exposing themselves to potential losses many times greater than their ability to pay; and protecting broker-dealers against excessive credit exposure to counterparties, which in turn, protects counterparties from the increased risk of broker-dealer insolvency arising from such credit exposure. Charles F. Rechlin et al., *Securities Credit Regulation* § 1:5-1:7 (2d ed. 2021).

SROs have imposed margin requirements on their members for more than a half-century. For example, the NYSE has had a rule in place since at least the 1950s, NYSE Rule 431, governing margin requirements for NYSE members.³ Since at least 1974, FINRA (and its predecessor, the

³ NYSE Rule 431 remains in the NYSE rulebook. FINRA Rule 4210 incorporates NYSE Rule 431. *Rechlin et. al.* at § 1:1.

National Association of Securities Dealers, or “NASD”) has had rules in place that establish margin requirements for FINRA members when they extend credit in connection with a securities transaction. What is currently FINRA Rule 4210 was approved by the SEC, and has been amended numerous times prior to the 2015 rulemaking, with Commission approval, pursuant to Section 19(b)(1) of the Exchange Act. *See* FINRA Rules, Section 4210 (last updated Apr. 6, 2022).

III. ARGUMENT

Although Petitioners purport to challenge SR-FINRA-2021-010, Petitioners candidly acknowledge that this proposed rule change in fact reduces the burden of FINRA Rule 4210, as amended by SR-FINRA-2015-036, on them and other FINRA members. Petition at 27. Their complaint is actually with SR-FINRA-2015-036 and extends even further back into FINRA’s rulemaking history on this subject—in fact, Petitioners broadly take issue with the entire concept that FINRA *can* or *should* require FINRA members to collect margin in connection with CATs or (seemingly) any other securities transactions. Petition at 20-26. But insofar as Petitioners challenge the basis for the already-approved SR-FINRA-2015-036, their petition is untimely. Petitioners had an opportunity to request Commission and judicial review of SR-FINRA-2015-036 at the appropriate time and, for whatever reason, chose not to do so. Permitting a post hoc review at this stage would invite serial litigation of SRO rulemaking processes, which would disincentivize SROs from proposing and implementing improvements to their rules via rule changes based on the risk of re-opening already concluded rulemaking processes. Further, it would create significant uncertainty for SRO members, their counterparties, and other market participants, who will not know what rules are truly final and what rules face further review by the Commission. The arguments in the Petition have already been considered and rejected as part of the rulemaking process for SR-FINRA-2015-036, and the time to petition the Commission or a

court to review that rule expired more than five years ago. In any event, Petitioners' contentions lack merit and should be rejected, as set forth below.

A. FINRA's Statutory Authority to Issue SR-FINRA-2021-010 and SR-FINRA-2015-036 Is Well-Established.

Contrary to Petitioners' assertions, Petition at 20-26, the statutory authority for FINRA to set margin requirements for its members—as it did in SR-FINRA-2021-010 and SR-FINRA-2015-036—is well-established and long-standing. Pursuant to Section 15A(b) of the Exchange Act, the Commission “shall approve’ a rule proposed by FINRA . . . if it is ‘consistent with the requirements of [the Act].” *New York Republican State Comm. v. Sec. & Exch. Comm’n*, 927 F.3d 499, 505 (D.C. Cir. 2019) (citing 15 U.S.C. § 78s(b)(2)(C)(i)). The Act in turn requires registered SROs to have rules applicable to its members that, among other things, “protect investors and the public interest” and “do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of [Section 15A of the Exchange Act].” 15 U.S.C. § 78o-3(b)(6); 15 U.S.C. § 78o-3(b)(9); *see also Mayo v. Dean Witter Reynolds, Inc.*, 258 F. Supp. 2d 1097, 1101-02 (N.D. Cal. 2003) (explaining the statutory scheme under which the SEC approves rule changes promulgated by SROs like FINRA); *Myers v. Merrill Lynch & Co.*, No. C-98-3532 WHO, 1999 U.S. Dist. LEXIS 22642, at *27 n.13 (N.D. Cal. Aug. 23, 1999) (same). A FINRA rule governing its members is not an SEC rule, and the Commission’s review is not entirely plenary. Provided that FINRA’s rulemaking is consistent with the objectives in Section 15A(b)(6) and 15A(b)(9) of the Exchange Act, and is not otherwise contrary to a provision of the Exchange Act, it should be approved. *See* 15 U.S.C. § 78s(b)(2)(C).

Section 15A of the Exchange Act does not explicitly or implicitly carve out margin requirements from the scope of FINRA’s rulemaking authority and the Commission has long found FINRA’s rulemakings regarding margin requirements to be within the scope of its statutory

authority under these provisions of the Exchange Act (and consistent with the Commission's rules). See, e.g., *Order Granting Approval of a Proposed Rule Change Relating to Amends. to FINRA Rules 2360 and 4210 in Connection with OCC Cleared Over-the-Counter Options*, Securities Exchange Act Release No. 70619, File No. SR-FINRA-2013-027, 78 Fed. Reg. 62,722 (Oct. 7, 2013) ("2013 Approval Order") (approving the extension of certain margin provisions to "OCC Cleared OTC Options" and concluding that the rule was consistent with Section 15A(b)(6) because, among other things, the existing disparity in the treatment of exchange-listed and OCC Cleared options could not be justified); *Notice of Filing of Amend. No. 1 and Order Granting Accelerated Approval of Proposed Rule Change, as Modified by Amend. No. 1, Relating to FINRA Rule 4210 (Margin Requirements)*, Securities Exchange Act Release No. 67751, File No. SR-FINRA-2012-024 (Aug. 29, 2012) (approving various changes to FINRA Rule 4210 and concluding the rule was consistent with Section 15A(b)(6) because, among other things, that FINRA had "adequately responded" to a comment letter by proposing various amendments to the rule); see also *Order Granting Approval of Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amend. No. 1 thereto by the Nat'l Ass'n of Sec. Dealers, Inc., Relating to the Amend. of its Margin Rules*, Securities Exchange Act Release No. 38729, File No. SR-NASD-97-14, 62 Fed. Reg. 32,669 (June 10, 1997) (approving margin-related rule). And, indeed, the Commission has previously approved, and FINRA's rules currently reflect, margin rules with respect to U.S. government and other types of exempt securities. See, e.g., *Order Granting Approval of Proposed Rule Change Relating to Margin Requirements*, Securities Exchange Act Release No. 31918, File No. SR-NASD-92-35, 58 Fed. Reg. 12,286 (Mar. 3, 1993) ("1993 Approval Order") (approving, in alignment with NYSE Rule 431, the provisions currently designated FINRA rules 4210(e)(2)(A) and (e)(2)(B)).

To accept Petitioners' expansive contention that FINRA lacks statutory authority to regulate margin on securities transactions, Petition at 20-26, would be to accept that the Commission has erred in approving FINRA and other SRO rules for more than a half-century. But as the Division found when it rejected this same argument in approving SR-FINRA-2015-036, FINRA rulemaking in this area is "consistent with the purposes of the Exchange Act and with FINRA's authority to impose margin requirements on its members." *See* 2016 Approval Order, 81 Fed. Reg. at 40,374. That determination was fully supported by the relevant statutory text and legislative history, and it should not be reevaluated now.⁴

Petitioners assert that the history of FINRA Rule 4210 is one of error: that, notwithstanding decades of practice, in fact, the grant of authority to the Federal Reserve Board in Section 7 of the Exchange Act to set margin requirements for non-exempted securities—a provision that has been in the law since 1934—should for the first time now be read to vest *exclusive* authority in the Board. *See* 15 U.S.C. § 78g. Accordingly, Petitioners posit, FINRA's rulemaking authority should not be read to include the setting of margin requirements. Petition at 20-25 (claiming Section 7(b) "clarifies" that the authority to set margin rules "is exclusive with the Board"). That is incorrect. Section 7 of the Exchange Act does not bar action by FINRA. The grant of authority to the Federal Reserve Board sets forth the parameters of the margin setting authority of the Federal Reserve Board with respect to the rules applicable at large.⁵ But it is not exclusive, and does not supplant

⁴ Even if there were an ambiguity, the Commission's judgment in interpreting the scope of the Exchange Act as applied to SRO rules would be entitled to deference on judicial review. *See Sharemaster v. Sec. & Exh. Comm'n*, 847 F.3d 1059, 1062, 1066-68 (9th Cir. 2017) (deferring to SEC's interpretation of Section 19(d)(2) of the Exchange Act).

⁵ *See* 15 U.S.C. § 78g(a) ("For the purpose of preventing the excessive use of credit for the purchase or carrying of securities, the Board of Governors of the Federal Reserve System shall . . . prescribe rules and regulations with respect to the amount of credit that may be initially extended and subsequently maintained on any security (other than an exempted security or a security futures product).").

FINRA’s—or other SROs or market participants’—ability to adopt more restrictive rules for its members. Nor does it purport to limit the authority granted to FINRA in Section 15A of the Exchange Act. *See New York Republican State Comm.*, 927 F.3d at 506 (“[W]hen statutes are capable of coexistence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective.” (internal quotation marks omitted) (quoting *J.E.M. Ag Supply, Inc. v. Pioneer Hi-Bred Int’l, Inc.*, 534 U.S. 124, 143-44 (2001))).

Section 7(b) of the Exchange Act merely provides that the Board may adopt regulations that prescribe higher or lower margin requirements than are specified in Section 7(a), permitting the Board to specify the minimum margin requirements for “all or specified securities transactions,” but not preventing SROs, exchanges or private parties from adopting their own rules that impose greater margin requirements than are required by law.⁶ *See FTC v. Ken Roberts Co.*, 276 F.3d 583, 593 (D.C. Cir. 2001) (“Because we live in an age of overlapping and concurring regulatory jurisdiction, a court must proceed with the utmost caution before concluding that one agency may not regulate merely because another may.”) (citation and internal quotation marks omitted).

That Section 7 affirmatively confers regulatory authority on the Board that is more specific than Section 15A, does not mean—as Petitioners argue, *see* Petition at 23-25—that the Board’s authority supplants FINRA’s rulemaking authority. Where two statutes “can both be fully implemented without conflict . . . it matters not that [one] is more detailed.” *See New York*

⁶ *See* 15 U.S.C. § 78g(b) (“Notwithstanding the provisions of subsection (a) of this section, the Board of Governors of the Federal Reserve System, may, from time to time, with respect to all or specified securities or transactions, or classes of securities, or classes of transactions, by such rules and regulations (1) prescribe such lower margin requirements for the initial extension or maintenance of credit as it deems necessary or appropriate for the accommodation of commerce and industry, having due regard to the general credit situation of the country, and (2) prescribe such higher margin requirements for the initial extension or maintenance of credit as it may deem necessary or appropriate to prevent the excessive use of credit to finance transactions in securities.”).

Republican State Comm., 927 F.3d at 509. Indeed, the Exchange Act expressly contemplates that SROs will make rules for their members that overlap with areas in which the Act confers regulatory powers on government regulators, including the Commission. *See* 15 U.S.C. § 78o-3(d) (defining requirements for SRO rules). As just one among many examples, Section 17(a)(1) of the Exchange Act, 15 U.S.C. § 78(a)(1), vests the Commission with the authority to prescribe rules regarding broker-dealer record-keeping, which it has done. *See, e.g.*, 17 C.F.R. § 240.17a-4 (2021). Yet few would question the validity of FINRA’s own rules governing its members’ books and records, *see* FINRA Rule 4510 *et seq.*, which have been repeatedly approved by the Commission. The Exchange Act addresses the possibility that SRO rules could conflict with the Exchange Act or rules adopted thereunder by requiring the Commission to find that the rule is consistent with the Act. *See* 15 U.S.C. § 78s(c)(1).

Consistent with the statutory structure, the Commission and the Federal Reserve Board have *both* long interpreted Section 7 of the Exchange Act to establish a floor—not a ceiling—and to permit SROs like FINRA to promulgate margin rules for their members that are more restrictive than those generally applicable under Section 7 or the Board’s regulations.

Since 1937, Federal Reserve Board regulations have codified a recognition that SROs like FINRA or national securities exchanges may adopt their own margin-related rules for their members. *See* Regulation T, 12 C.F.R. § 220.1 (providing that the regulation “does not preclude any exchange, national securities association, or creditor from imposing additional requirements or taking action for its own protection”); *see also Extension and Maintenance of Credit by Brokers, Dealers, and Members of National Securities Exchanges*, File No. 43-94, 2 Fed. Reg. 3368, 3373 (Dec. 21, 1937) (adopting rule). This language specifically contemplates the setting of margin requirements by a national securities association such as FINRA or an exchange such as NYSE,

as well as the setting of “house” margin requirements by the broker-dealers (or “creditors”) themselves—a routine practice for many broker-dealers. And, indeed, at the time FINRA Rule 4210 was first introduced in the 1970s, it was generally understood that the Board’s authority with respect to margin was non-exclusive. *See, e.g.,* James Largay, *100% Margins: Combating Speculation in Individual Security Issues*, 28 J. Fin. 973 (1973) (“Margin regulation . . . is not wholly vested in the FED as Regulation T (covering brokers and dealers) is quite clear in permitting securities exchanges and creditors to impose additional margin requirements.”).⁷

Contrary to Petitioners’ assertion, Petition at 22-23, the history of legislation around Section 7 of the Exchange Act suggests that Congress *did not* intend to divest SROs of the authority to regulate margin requirements for their members. For example, Congress overhauled Sections 7 and 8 of the Exchange Act in the 1996 National Securities Markets Improvement Act to modify the margin rules applicable to broker-dealers, at a time when NASD had margin rules in place. Pub. L. No. 104-290, § 101, 110 Stat. 3416 (1996). Yet, the amendments did not interfere with those rules and the version of Regulation T promulgated by the Board in response to those amendments included the express recognition that NASD had authority to set margin requirements to for its members. *See also Hall v. United States*, 556 U.S. 506, 516 (2012) (“We assume that Congress is aware of existing law when it passes legislation.” (quoting *Miles v. Apex Marine Corp.*, 498 U.S. 19, 32 (1990))).

None of the legislative materials cited by Petitioners suggest otherwise. The Secondary Mortgage Market Enhancement Act of 1984 (“SMMEA”), does not “prohibit” the requirement of

⁷ To the extent there were any ambiguity on the point (and there is not), the Board’s interpretation of Section 7 would be given deference because that Section of the Act is itself a delegation of rulemaking authority to the Board. *See Household Credit Servs. v. Pfennig*, 541 U.S. 232, 238 (2004) (Where “Congress has expressly delegated to the Board the authority to prescribe regulations” its regulations are “given controlling weight unless [they are] arbitrary, capricious, or manifestly contrary to statute.” (quoting *Chevron USA, Inc. v. Nat. Res. Defense Council, Inc.*, 467 U.S. 837, 842 (1984))).

margin for private label MBS as Petitioners suggest. Petition at 4. Rather, it clarifies that, for purposes of Section 7, such transactions are not deemed to be an extension of credit. And, indeed, the existing FINRA and NYSE margin rules—adopted after SMMEA, and approved by the Commission—specifically establish requirements with respect to mortgage-related securities transactions, including those governed by SMMEA. *See* FINRA Rule 4210(e)(2)(F); *see also* *Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 1 and 2 by the National Association of Securities Dealers, Inc. Relating to Margin Requirements*, Securities Exchange Act Release No. 48407, File No. SR-NASD-2000-08, 68 Fed. Reg. 52,259 (Sept. 2, 2003) (approving amendments to NASD Rule 2520); *Order Approving Proposed Rule Change and Amendment Nos. 1, 2, and 3 by the New York Stock Exchange, Inc. Relating to Margin Requirements*, Securities Exchange Act Release No. 48365, File No. SR-NYSE-98-14, 68 Fed. Reg. 51314 (Aug. 19, 2003) (approving amendments to NYSE Rule 431); *Order Granting Approval of Proposed Rule Changes*, Securities Exchange Act Release No. 24114, File Nos. SR-NYSE-86-4 and -30, 52 Fed. Reg. 7,245 (Mar. 9, 1987) (approving requirements for mortgage related securities under NYSE Rule 431 shortly after the passage of SMMEA).

The House Report that Petitioners cite as purportedly confirming that agency mortgage transactions are outside the scope of the Rule, Petition at 22, simply noted that such transactions fall outside of the extension of credit subject to Board regulation under Section 7, *see* H.R. Rep. No. 73-1383, at 7703 (1934). It did not make findings that such regulation by an SRO is either undesirable or prohibited.

Likewise, the Commodity Futures Modernization Act of 2000 (“CFMA”), enacted in 2000, Petition at 22, supports the conclusion that the Board’s authority to set margin rules for securities

transactions is non-exclusive. Notably, the relevant provision of the CFMA, codified in Section (c)(2) of Section 7, is very different from Section 7(a) insofar as it actually does prohibit a “broker” or “dealer” from “collect[ing] margin from any customer ... unless such activities comply with the regulations” promulgated by the Board or the SEC and CFTC jointly. But the CFMA applies to securities futures products, and the regulations adopted by the CFTC and SEC govern transactions in the market more generally, and exempt FINRA members from their requirements on the basis of the rules that already govern those members. *See* 17 C.F.R. § 41.42(c) (2021).

Petitioners’ final assertion regarding statutory authority is that, whatever FINRA’s authority more generally, CATs cannot be subject to margin requirements because they are “exempted securities” under Section 7 of the Exchange Act. Petition at 25-26. But that exemption only excludes CATs from the scope of Section 7 and regulations promulgated under it—it does not constrain FINRA’s authority to adopt rules applicable to its members rather than the public at large. The Federal Reserve Board made this clear in a 1972 interpretive ruling, finding that “[a]lthough the Board does not have authority to set requirements on exempted securities, brokers and national securities exchanges can establish margin requirements on exempted securities and they can also set initial margin requirements which would be more restrictive than those of the Board.” *See Opinion*, 1972 Fed. Res. Interp. Ltr. LEXIS 52 (June 28, 1972). And, indeed, FINRA Rule 4210 has historically included a margin requirement for a variety of “exempted securities.” *See* 1993 Approval Order, 58 Fed. Reg. 12,286; *SEC Approval and Effective Date for New Consolidated FINRA Rules Regarding Margin Requirements, Daily Record of Required Margin, and Extension of Time Requests*, Regulatory Notice 10-45 (Dec. 2, 2010). Petitioners’ assertion is, in substance, that *nobody*—not the Federal Reserve and not FINRA—can regulate margin with respect to exempted securities sold by FINRA members. If that were the law, one would expect

that Petitioners could find something to cite to support it—but they offer nothing: no cases, no interpretive guidance, no historical regulatory practice, no secondary commentary or guidance. Indeed, all indications and sources are to the contrary.

B. The Narrow Amendments to FINRA Rule 4210 Set Forth in SR-FINRA-2021-010 Are in Accordance with Section 15A of the Exchange Act and Are Consistent with the Commission’s Previous Grants of Approval to FINRA Rulemaking in This Area.

Petitioners’ challenge to SR-FINRA-2021-010 has nearly nothing to do with the requirements or substance of this specific rulemaking, which they acknowledge reduces the burdens on FINRA members and promotes competition. Petition at 26-27. Instead, Petitioners wish to reopen a rulemaking process that has already concluded and in which they participated, including by submitting numerous comment letters and participating in multiple meetings and telephone calls with Commission staff. *See* 2022 Approval Order, 87 Fed. Reg. at 4,082 (“The Commission agrees with FINRA that some comments have been previously addressed in the [SR-FINRA-2015-036] rulemaking, including whether to impose any margin requirements on [CATs] or exclude certain products from the scope of the rule, such as Specified Pools and CMOs.”). Petitioners’ efforts are, at best, untimely. At this stage, the scope of review of SR-FINRA-2021-010 must be confined to this specific rulemaking. Petitioners cannot demand a Commission review of a previously-approved rule having not sought Commission review at the appropriate time, nor are they entitled to a second bite at the apple every time an already-approved rule is amended. *See* 17 C.F.R. §§ 201.430(b)(1); (c) (2021) (requiring a party challenging an action made pursuant to delegated authority to file a notice of intention to petition for review within five days of receiving actual notice of the action and a petition for review within five days of filing the notice of intention to petition for review and precluding judicial review in the absence of an application to the Commission pursuant to 5 U.S.C. § 704); 15 U.S.C. § 78y(b)(1) (prescribing the mechanism for

judicial review of SRO rulemaking, which requires a party seeking such review to file a written petition within sixty days after the promulgation of the rule).

In any event, the record—and BDA’s own letter from June 2018 supporting certain elements of SR-FINRA-2021-010—fully supports the Division’s approval of SR-FINRA-2021-010. Rather than imposing new requirements, the narrow amendments to FINRA Rule 4210 in SR-FINRA-2021-010 address—and in fact reduce the potential burden of—amendments to FINRA Rule 4210 included in SR-FINRA-2015-036, as set forth above and consistent with FINRA’s and the Division’s findings. *See* SR-FINRA-2021-010, Proposed Amend. No. 1 at 8; 2022 Approval Order, 87 Fed. Reg. at 4,083-84. The Commission should approve a proposed rule change where, as here, the proposed rule change is consistent with FINRA’s rulemaking objectives under Section 15A of the Exchange Act and “is necessary or appropriate in the public interest,” contributes to “the protection of investors,” and promotes “efficiency, competition, and capital formation.” 15 U.S.C. § 78c(f).

1. The Thorough Factual Record Developed by FINRA and the Division Is More Than Sufficient for the Commission to Conclude That SR-FINRA-2021-010 Satisfies the Requirements of the Exchange Act.

As described above, SR-FINRA-2021-010 includes three changes to FINRA Rule 4210, as amended by SR-FINRA-2015-036: (1) the elimination of the two percent maintenance margin requirement that previously applied to non-exempt accounts; (2) the allowance of FINRA members to take a capital charge in lieu of collecting margin for excess net mark-to-market losses on CATs subject to specified conditions and limitations, including, most notably, the lesser of \$30 million or 25% of the FINRA member’s tentative net capital (the “25% TNC/\$30MM Threshold”);

and (3) certain definitional and other conforming language changes to streamline and consolidate FINRA Rule 4210 in light of the recent rule changes.

By reducing compliance and administrative costs for FINRA members, further mitigating any disparity in the treatment of FINRA members compared to non-FINRA members and of small or medium-sized FINRA members compared to larger FINRA members, and promoting regulatory clarity, *see* 2022 Approval Order, 87 Fed. Reg. at 4,080, SR-FINRA-2021-010's amendments promote just and equitable principles of trade, remove impediments to the mechanism of a free and open market and a national market system, protect investors and the public interests, do not impose any burden on (and in fact decreases potential burdens on) competition, and promote efficiency and competition in the market, consistent with the statutory requirements of the Exchange Act, *see* 15 U.S.C. §§ 78o-3(b)(6); (b)(9). The rationale for SR-FINRA-2021-010 is clearly supported in the administrative record by detailed and rigorous assessments of any burden imposed on competition (including thorough analysis of economic impact assessments, anticipated benefits, anticipated costs, and alternative approaches). *See* SR-FINRA-2021-010 at 25-33.

First, in eliminating the two percent maintenance margin requirement for non-exempt accounts, FINRA and the Division recognized that it could simplify the requirements of SR-FINRA-2015-036 by eliminating the need to differentiate between exempt and non-exempt accounts to determine the applicability of the maintenance margin requirement. Instead, FINRA removed the requirement altogether—reducing the margin requirement to only the actual mark-to-market losses over the specified threshold. Among other things, this amendment is intended to reduce cost for FINRA members and address any perceived competitive disadvantage to such FINRA members compared to non-FINRA-member banks, to which FINRA Rule 4210 does not apply. SR-FINRA-2021-010 at 12-14; 2022 Approval Order, 87 Fed. Reg. at 4,083. In addition

to eliminating that administrative cost, FINRA recognized that SR-FINRA-2021-010 will provide operational relief with respect to obtaining custody and related agreements in connection with the need to collect maintenance margin; in other words, it will reduce the need for FINRA members to enter into separate custodial agreements with third-party banks to hold the maintenance margin for counterparties that cannot custody assets directly with broker-dealers. SR-FINRA-2021-010 at 29. By eliminating the requirement to collect two percent maintenance margin on all CATs, SR-FINRA-2021-010 also permits introducing broker-dealers to maintain their exemptive status under SEC Rule 15c3-3(k) while complying with FINRA Rule 4210.

By mitigating concerns about regulatory compliance costs and allowing FINRA members to compete in the market more equally with non-FINRA members, the elimination of the two percent maintenance margin requirement for non-exempt accounts promotes a more just and equitable market by promoting competition and efficiency, which will benefit investors and the public interest. *See* 15 U.S.C. § 78o-3(b)(6). This conclusion is supported by public comments received during the SR-FINRA-2021-010 rulemaking process. *See* Letter from Chris Killian, Managing Director, SIFMA, to SEC at 1 (June 15, 2021) (“SIFMA Letter”) (“[Commenter] previously requested that FINRA eliminate the maintenance margin provisions of the rules. FINRA has proposed to eliminate these provisions, and we support that change.”) (internal citation omitted).

Second, permitting FINRA members to take a capital charge in lieu of collecting maintenance margin was a change to SR-FINRA-2015-036 specifically motivated by FINRA’s efforts to address concerns (including concerns voiced by various industry participants and commenters) that SR-FINRA-2015-036 could create an unfair disparity between small and medium-sized broker-dealers and larger broker-dealers. SR-FINRA-2021-010 at 7-8; SR-FINRA-

2021-010, Proposed Amend. No. 1 at 6-7; 2022 Approval Order, 87 Fed. Reg. at 4,078. The record is clear that this was a central objective of FINRA, and one of the main points considered by the Division in approving SR-FINRA-2021-010. *See* SR-FINRA-2021-010 at 7-8; SR-FINRA-2021-010, Proposed Amend. No. 1 at 6-7; 2022 Approval Order, 87 Fed. Reg. at 4,081. Contrary to Petitioners' arguments, Petition at 29, various smaller broker-dealers commented as part of the rulemaking process that having the option to take a capital charge in lieu of margin would help to alleviate the potential disparity created by SR-FINRA-2015-036 and FINRA and the Division reached the same conclusion. *See* 2022 Approval Order, 87 Fed. Reg. at 4,078 (“Smaller firms told FINRA that having the option to take a capital charge, in lieu of collecting margin, would help alleviate the competitive disadvantage of needing to obtain margining agreements with . . . counterparties because there would be an alternative to collecting margin.”); SR-FINRA-2021-010 at 14-15; SIFMA Letter at 5 (“SIFMA members generally appreciated FINRA’s providing of an exception to permit broker-dealers to take capital charges in lieu of margin for CATs. An exception is appropriate in light of the nature of the products and the transactions in the market. It is further consistent with other provisions in Rule 4210 that permit broker-dealers to take capital charges in lieu of collecting margin for transactions in instruments of high credit quality.”).

Notably, as discussed above, BDA itself petitioned FINRA in 2018 specifically to adopt this aspect of SR-FINRA-2021-010, reciting its own discussions with two smaller broker-dealers who expressed support for a capital charge in lieu of margin option, writing that the two smaller broker-dealers believed “the Capital Charge Proposal would give them many options to remain competitive in [CATs]” and that they were “not concerned that the Capital Charge Proposal [would] be anticompetitive” or force them to “erode away their capital in order to be competitive.” BDA Letter at 2. In its review of prior SRO rulemaking, the Commission has found that

eliminating this kind of disparity is consistent with the SRO rulemaking mandate. *See* 2013 Approval Order, 78 Fed. Reg. at 62,725 (approving the application of certain margin provisions to options trading cleared by the Office of the Comptroller of the Currency based on the conclusion that the rule amendment was consistent with Section 15A(b)(6) of the Exchange Act because, among other things, the existing disparity in the treatment of exchange-listed and OCC-cleared options could not be justified).

As the Division correctly found, SR-FINRA-2021-010 will promote competition, *see* 15 U.S.C. § 78o-3(b)(9), by leveling the playing field among CAT market participants of all sizes, thereby reducing disruption in the CAT market without the loss of any investor protection. SR-FINRA-2021-010 at 25. SR-FINRA-2021-010 strikes an appropriate balance by providing small and medium-sized FINRA members with an alternative to collecting margin, a requirement which such members have argued before they are less positioned to comply with compared to larger FINRA members. It also ensures that the regulatory objective of FINRA Rule 4210, as amended by SR-FINRA-2015-036, is not undermined by limiting the ability to rely on capital charge to the 25% TNC/\$30MM Threshold.

To the extent that Petitioners now argue that the problem with SR-FINRA-2021-010 is that it sets limits for taking a capital charge above which margin must be collected, FINRA respectfully disagrees that is a defect. The objective of SR-FINRA-2021-010 remains to encourage the collection of margin. The amendment to permit substitution of a capital charge up to certain limits, including the 25% TNC/\$30MM Threshold, is meant to add flexibility to SR-FINRA-2015-036, not to supplant it. The requirement to take a capital charge against net capital for the mark-to-market losses associated with forward-settling securities transactions already exists. *See* 17 C.F.R. § 240.15c3-1(c)(2)(iv) (2021). Thus, permitting a capital charge to wholly substitute for collection

of margin would be no change at all, and would undermine the core regulatory objectives of not only SR-FINRA-2021-010 but the entire margin requirements regime as applied to CATs. It would also, in FINRA’s judgment, exacerbate rather than address the potential disparate impact on small and medium-sized firms by permitting their larger competitors to use their larger balance sheets to effectively avoid the margin requirement altogether to the disadvantage of small and medium-sized FINRA members. *See* 2022 Approval Order, 87 Fed. Reg. at 4,083. This was a concern raised by small and medium-sized members and specifically addressed by FINRA and the Division. *See id.* at 4,078 (“[T]he proposed rule change includes conditions and limitations that FINRA believes are designed to help protect the financial stability of members that opt to take capital charges while restricting the ability of the larger members to use their capital to compete unfairly with smaller members.”); SR-FINRA-2021-010 at 15.

Further, under SR-FINRA-2021-010, taking a capital charge is optional, so FINRA members will only commit capital in lieu of margin when they believe it appropriately balances applicable benefits and risks. In other words, SR-FINRA-2021-010 does not impose a “one-size-fits-all” solution on FINRA members. FINRA intended to keep strong incentives to collect margin and use the amendments only to allow flexibility in complying with the rule.

Petitioners argue that certain entities, such as pension funds and state agencies, may be unable to post margin. *Petition* at 8. Petitioners then say that “[s]imilarly, registered investment companies cannot re-pledge collateral.” *Id.* They argue that, partially as a result of counterparties who are unable to post margin, because of the limitation imposed by the 25% TNC/\$30MM Threshold, the ability of FINRA members to introduce liquidity into the market during periods of unusual volatility will be drastically limited. *Id.* at 30, 33. FINRA does not accept Petitioners’ assessment of the inadequacy of the 25% TNC/\$30MM Threshold or the supposed “disastrous

consequences for the [CAT] market” in the event of a market dislocation under SR-FINRA-2021-010. *Id.* at 5. Petitioners do not explain why registered investment companies could not re-pledge collateral subject to appropriate custody arrangements.

And to the extent they assert that registered investment companies or pension plans cannot post margin, they are incorrect. Registered investment companies can post margin, they are simply required to account for the obligation to post margin as part of their potential exposures with respect to derivative transactions, as a condition to their derivative obligations not being subject to more general restrictions on such companies’ ability to incur debt. This is a position the Commission has re-affirmed in its recent rule on the Use of Derivatives by Registered Investment Companies and Business Development Companies, including specifically in the context of TBAs. *See Use of Derivatives by Registered Investment Companies and Business Development Companies*, Investment Company Act Release No. 34084, File No. S7-24-15, 85 Fed. Reg. 83,162, 83,175 (Dec. 21, 2020) (“TBAs and dollar rolls are included in the final rule’s derivatives transaction definition because we believe they are forward contracts or ‘similar instruments.’”). Likewise, under a 2013 Advisory Opinion from the Department of Labor, ERISA pension plans can post both initial and variation margin, and the assets deposited with the counterparty “to support payment obligations that may become necessary for the plan” “would not be plan assets for the purposes of Title I of ERISA.” *See* Dep’t of Labor Advisory Op. 2013-01A (Feb. 7, 2013). In any event, the provision of this rulemaking that would permit FINRA members to substitute a capital charge for the collection of margin is intended to provide the very flexibility Petitioners seek to continue to deal with counterparties who are unable or unwilling to post margin, while maintaining the overall effectiveness of the rule.

Petitioners have not challenged any of SR-FINRA-2021-010's definitional and related language changes and clarifications, and accordingly, the Commission need not consider that aspect of SR-FINRA-2021-010 in its review. In any event, the Division has thoroughly and appropriately addressed those changes and clarifications in the 2022 Approval Order and it is clearly established that FINRA members will benefit from such clarification to FINRA Rule 4210. *See* 2022 Approval Order, 87 Fed. Reg. at 4,084; SR-FINRA-2021-010 at 30. The Commission has previously recognized that the benefits of such rule clarifications satisfy the statutory requirements of the Exchange Act for FINRA rulemaking. *See, e.g., Order Approving a Proposed Rule Change to Adopt FINRA Rule 4210 (Margin Requirements), FINRA Rule 4220 (Daily Record of Required Margin) and FINRA Rule 4230 (Required Submissions for Requests for Extensions of Time under Regulation T and SEC Rule 15c3-3) in the Consolidated FINRA Rulebook*, Securities Exchange Act Release No. 62482, File No. SR-FINRA-2010-024, 75 Fed. Reg. 41,562, 41,564 (July 12, 2010) (approving the adoption of certain NASD and NYSE rules as part of the FINRA Rulebook finding the adoption was consistent with Section 15A(b)(6) citing only the rationale that the adoption would “[clarify] and [streamline] the margin requirements applicable to [FINRA’s] members”).

2. *In Promulgating SR-FINRA-2021-010, FINRA and the Commission Complied with All Applicable Procedural Requirements.*

Petitioners try to have it both ways by focusing their procedural arguments on the record supporting SR-FINRA-2021-010, while substantively taking issue with FINRA's adoption of the underlying margin requirements in SR-FINRA-2015-036, and then arguing that the record in support of the former does not support the latter. *See* Petition at 43-44. But FINRA was not required to re-do the entire rulemaking process that led to the approval of SR-FINRA-2015-036 just to make some relatively minor adjustments to it; nor was the Division required to re-canvass

a rulemaking process that stretches back to 2014 to approve an amendment to the already-approved rule change.

Petitioners' suggestion that FINRA did not disclose those with whom it consulted in the development of SR-FINRA-2021-010 mischaracterizes the record. In fact, FINRA specifically set out the process it undertook to develop these amendments, which included receiving comments and having meetings with industry participants, as well as outreach and consultation with the Commission and the Federal Reserve System in connection with the rulemaking. SR-FINRA-2021-010 at 7; FINRA Letter at 3. Petitioners' argument also fails to reconcile itself to the lengthy administrative record before FINRA and the Division both in connection with SR-FINRA-2021-010 and the previously-approved SR-FINRA-2015-036. *See* 2016 Approval Order, 81 Fed. Reg. 40,364; 2022 Approval Order, 87 Fed. Reg. 4,076. Consistent with FINRA's practice for significant rulemakings, before commencing the rulemaking and throughout the rulemaking process, FINRA had informal discussions with other regulatory agencies and industry participants—including Petitioners themselves—to gather information to inform its rulemaking. Not all such discussions were formally recorded, but the input is reflected in the administrative record, which Petitioners' have had ample opportunity to review and comment on. FINRA's rulemaking processes have been fully consistent with the rulemaking requirements applicable to SROs. *See* 15 U.S.C. § 78s(b)(1).

Nor is there merit to the suggestion that FINRA's only response to concerns raised by commenters consists of *ipse dixit* statements of its "beliefs." In fact, the record is replete with lengthy and detailed analysis by FINRA and the Division addressing the comments submitted. As relevant here, that includes a point-by-point analysis of the concerns raised by Petitioners themselves in the rulemaking process, with detailed responses to Petitioners' hypothetical

scenarios and explanations of why, in the exercise of its judgment and on the basis of evidence, FINRA concluded that SR-FINRA-2021-010 was appropriate. SR-FINRA-2021-010, Proposed Amend. No. 1 at 4-13, 19-20; 2022 Approval Order, 87 Fed. Reg. at 4,085-86; *see also Nat'l Mining Ass'n v. Mine Safety & Health Admin.*, 512 F.3d 696, 700 (D.C. Cir. 2008) (“It is enough if the agency’s statement identifies the major policy issues raised in the rulemaking and coherently explains why the agency resolved the issues as it did.”). Likewise, the record shows that FINRA considered alternatives—and, indeed, adopted them when appropriate. *Cf. Motor Vehicle Mfrs. Ass’n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 51 (1983). For example, as FINRA explained, it considered imposing consequences as soon as a firm’s capital charges for its counterparties’ unmargined excess net mark to market losses exceeded \$25MM. SR-FINRA-2021-010 at 32-33. Instead, however, FINRA responded to industry concerns by requiring notice to FINRA after that threshold had been exceeded for five consecutive business days, and by applying the more significant consequences only when a firm exceeds the 25% TNC/\$30MM Threshold for five consecutive business days. *Id.* Particularly when considered against the robust rulemaking process that led to the adoption of SR-FINRA-2015-036 in the first place, and the commentary received by FINRA as part of that rulemaking process and which informed its adoption of SR-FINRA-2021-010, Petitioners’ suggestion that SR-FINRA-2021-010 rests on nothing more than FINRA’s say-so is demonstrably erroneous.

3. *Petitioners’ Remaining Contentions Are Merely Objections to SR-FINRA-2015-036 and Margin Requirements Generally.*

Unable to dispute that SR-FINRA-2021-010’s narrow amendments to FINRA Rule 4210 are consistent with FINRA’s statutory rulemaking authority and the standards the Commission is required to consider when reviewing FINRA rulemaking, Petitioners recycle their objections to SR-FINRA-2015-036 and the margin requirements regime generally. *Petition.* at 26-28, 31-40.

Those objections—addressed in detail *infra* at Section III.C—have already been heard, considered, and addressed by FINRA and the Division. *See* FINRA Letter at 3. Petitioners offer only three objections that are arguably specific to SR-FINRA-2021-010’s limited amendments to FINRA Rule 4210, but these too have been thoroughly addressed in the administrative record.

First, Petitioners again complain, as did some other commenters, that SR-FINRA-2021-010’s amendments do not go far enough, in that they do not sufficiently alleviate the disparity between broker-dealers with bank affiliates and broker-dealers without bank affiliates (which are not subject to FINRA Rule 4210) because counterparties (*e.g.*, pension funds and other institutional investors that Petitioners claim are prohibited from providing margin) will still have an economic incentive to favor non-FINRA members over broker-dealers subject to FINRA Rule 4210. Petition at 27-29. According to Petitioners, this impact will fall disproportionately on small, women-owned or minority owned businesses, and may cause some such businesses to exit the CAT market. Petition at 41-43 (citing letters to the SEC submitted by Ginnie Mae (Jan. 20, 2022) and the Federal Home Loan Banks (Jan. 18, 2022)); 2022 Approval Order, 87 Fed. Reg. at 4,081.

But SR-FINRA-2015-036 was approved with a series of amendments aimed at mitigating any potential impact of SR-FINRA-2015-036 on smaller firms. 2022 Approval Order, 87 Fed. Reg. at 4,081. Those amendments included (1) increasing the threshold for the exception for gross open positions, (2) creating an exception to the two percent maintenance margin requirement for cash investors, (3) creating an exception for multifamily housing securities and project loan program securities, and (4) creating an exception for \$250,000 *de minimis* transfers. Petitioner BDA expressed explicit support for some of these measures, noting that they “are vital for mid-size fixed-income dealers.” BDA Letter at 5. To the extent these measures did not completely resolve any disparity between small and medium-sized and larger FINRA members, FINRA and

the Division concluded, reasonably, that such disparity was justified in order to address the risk created by unsecured credit exposures in the CAT market. Moreover, FINRA preserved all of the above-described exceptions in promulgating SR-FINRA-2021-010. 2022 Approval Order, 87 Fed. Reg. at 4,084.

And the whole purpose of SR-FINRA-2021-010 is to respond to these types of concerns, building on the provisions in SR-FINRA-2015-036, by providing FINRA members with even greater flexibility than they have under FINRA Rule 4210, as amended by SR-FINRA-2015-036, by permitting them to engage in margining rather than committing capital, allowing such members to better compete in the CAT market and attract and retain counterparties. For example, the elimination of the two percent maintenance margin requirement for non-exempt accounts will eliminate an indirect cost that some small and medium-sized FINRA members have said will reduce, or already is reducing, the number of broker-dealers counterparties interact with. SR-FINRA-2021-010 at 29. Further, SR-FINRA-2021-010 permits FINRA members a limited capacity to take capital charges in lieu of collecting margin and thereby assume the risk of counterparty default, and that could help FINRA members to establish (or maintain) relationships with counterparties who are not willing to post margin. SR-FINRA-2021-010 at 30 (the rule transfers risk from the counterparties to the FINRA member, which could serve as “an additional incentive to establishing trading relationships” with counterparties).⁸

⁸ Both FINRA and the Commission have acknowledged and addressed at length in connection with SR-FINRA-2015-036 the concerns raised by some commenters that non-FINRA members may be advantaged by being able to conduct transactions without collecting margin from counterparties. FINRA believes that collecting margin on forward-settling securities transactions, as the TMPG guidance also states, is a best practice. FINRA’s rules apply only to its members, but FINRA supports the collection of margin in all such transactions. As commenters have noted, in a number of contexts the collection of margin is already required; for example, in agency MBS transactions cleared through FICC and under the commercial rules imposed by many clearing broker-dealers.

Notably, in response to comments, FINRA sought to identify and discuss SR-FINRA-2021-010 with small firms who feel they may be forced from the market by the as-amended FINRA Rule 4210; FINRA has stated that it intends to monitor SR-FINRA-2021-010's implementation and its impact. 2022 Approval Order, 87 Fed. Reg. at 4,081-82. FINRA remains committed to ensuring that FINRA Rule 4210, as amended, in practice, does not disadvantage "smaller broker-dealers who are most focused on community institutions," including those owned by women, minorities and veterans. Petition at 41. The SR-FINRA-2021-010 rulemaking demonstrates FINRA's commitment to these parties in action, as FINRA is pro-actively responding to concerns raised by market participants and proposing appropriate adjustments to FINRA Rule 4210.

FINRA and the Division explicitly considered suggestions from commenters, including Petitioners, that there should be no margin requirements applicable to CATs and that FINRA members should be required to take capital charges for only ten percent of their counterparties' unmargined mark-to-market losses. FINRA concluded, and the Division agreed, that these suggestions would undercut the objectives of the CAT margin requirements. 2022 Approval Order, 87 Fed. Reg. at 4,084. And of course, the same factors that make smaller firms more sensitive to the margin requirements also make them more vulnerable to the risk of counterparty default, which such firms may be less able to absorb, underscoring the need for the CAT margin requirements regime. In promulgating SR-FINRA-2021-010, FINRA and the Division affirmed "the regulatory need for attention to this area." *Id.* at 4,082.

Second, Petitioners object that the 25% TNC/\$30MM Threshold does not alleviate the disparity between small or medium-sized FINRA members and larger FINRA members, and that it creates additional problems because (i) it limits the benefits of the capital charge alternative to the 25% TNC/\$30MM Threshold, creating an imbalance between FINRA members and non-

FINRA members, and (ii) it reduces the ability of FINRA members to introduce liquidity into the market once the 25% TNC/\$30MM Threshold is crossed. Petition at 29-31. As discussed above, however, the 25% TNC/\$30MM Threshold is responsive to the concern expressed by small and medium-sized members that larger broker-dealers would use their larger balance sheets to avoid collecting margin and thereby obtain a competitive advantage. SR-FINRA-2021-010 at 32-33; SR-FINRA-2021-010, Proposed Amend. No. 1 at 17-19; 2022 Approval Order, 87 Fed. Reg. at 4,088-89. By limiting the ability of such larger members to do so, FINRA's proposal promotes competition in the market, particularly for smaller broker-dealers. SR-FINRA-2021-010 at 29. In effect, the 25% TNC/\$30MM Threshold is a risk management mechanism given the introduction of the capital charge option. The purpose of FINRA Rule 4210, as amended by SR-FINRA-2015-036 and SR-FINRA-2021-010, is to shore up the practices in the CAT market by encouraging the margining of CATs—not to allow members to avoid such requirements through the taking of a large net capital charge. For some FINRA members, the volume of business may reach the threshold where further capital charges cannot be taken, and at that point, the 25% TNC/\$30MM Threshold would then prevent the member from entering into new CATs with any counterparty that cannot or will not post margin. While the ability of the FINRA member to inject liquidity into the CAT market could potentially be reduced, raising the threshold for permitted capital charges would reduce the effectiveness of SR-FINRA-2021-010 by increasing the FINRA member's exposure to the risk of counterparty default and would undermine the goal of promoting and supporting competition in the market by allowing larger FINRA members that are more able to commit capital to avoid collecting margin.⁹

⁹ The largest participants in this market are FINRA members, reflecting the fact that broker-dealers have certain advantages over banks. For example, when the transactions are margined to the extent required

Third, Petitioners argue that SR-FINRA-2021-010 fails to address the risk of “daisy chain” fails in the event that a counterparty to a “chain” transaction, which is a common transaction structure in the CAT market, is unable or unwilling to satisfy a margin call. Petition at 35-40. FINRA and the Division have carefully analyzed comments regarding the possibility of such failures and addressed them in SR-FINRA-2021-010, which includes amendments to SR-FINRA-2015-036 designed specifically to address that issue. Under FINRA Rule 4210 as amended by SR-FINRA-2015-036 FINRA members are obligated to liquidate a counterparty’s position if the net mark-to-market loss exceeds \$250,000 and it is not margined or eliminated within five business days. SR-FINRA-2021-010 at 16. SR-FINRA-2021-010 gives members alternatives to liquidation, including taking a capital charge up to the 25% TNC/\$30MM Threshold. *Id.* And the liquidation requirement would only apply if (i) the member has exceeded that threshold for five consecutive business days, (ii) the counterparty’s unmargined net mark-to-market loss on CATs has exceeded \$250,000 for five consecutive business days, (iii) the member has a contractual right to liquidate, and (iv) no extension is granted by FINRA (extensions would be expected to be granted, for example, in the case of operational issues).

Petitioners overstate the risk of a daisy chain of fails. As FINRA and the Division have explained—and Petitioners do not dispute, *see* Petition at 36—the only reasonable circumstance in which liquidation would be required under the existing rule is one in which the FINRA member has an undisputed right to call margin from the counterparty and the counterparty is unwilling or unable to post additional collateral. *See* SR-FINRA-2021-010, Proposed Amend. No. 1 at 10-13; 2022 Approval Order, 87 Fed. Reg. at 4,085. FINRA reasonably believes that in such

by the rule, a broker-dealer running a matched book generally has no capital requirements, while banks generally do have capital requirements even on margined transactions.

circumstances the risk of default is particularly acute, that it is prudent in those circumstances to require the member to liquidate the position, and that it is likely that there would be a “daisy chain failure” regardless of the liquidation requirement because the counterparty would likely be unable to pay or deliver on the CAT’s settlement date. *See* SR-FINRA-2021-010, Proposed Amend. No. 1 at 12-13; 2022 Approval Order, 87 Fed. Reg. at 4,085-86. FINRA explicitly considered three other circumstances in which a member may be unable to obtain margin from a counterparty (the lack of an obligation, an operational issue, and disagreement over the amount of the counterparty’s mark-to-market loss) and found that in each circumstance it is unlikely the liquidation requirement would be triggered under SR-FINRA-2021-010. *See* SR-FINRA-2021-010, Proposed Amend. No. 1 at 10-13; 2022 Approval Order, 87 Fed. Reg. at 4,085-86. To the extent that the liquidation requirement does result in a chain of fails, that outcome is potentially more orderly and less likely to result in market dislocation than the chain of fails that would result from a counterparty default. FINRA’s analysis that, on balance, the benefits of the margin requirement outweigh a risk that is only likely to manifest in a scenario that raises a high probability of the very type of default that the margin requirements are designed to protect against is a valid and reasonable conclusion. And the net capital aspect of the 25% TNC/\$30MM Threshold in SR-FINRA-2021-010, as previously discussed, is intended to limit FINRA members’ risk exposure, with the goal of ensuring that a counterparty default does not cause a firm to fail and therefore be unable to meet its obligations to customers and counterparties, potentially triggering a cascade of failures among firms and their counterparties.

C. Even if the Commission Were to Re-Analyze SR-FINRA-2015-036, That Amendment to FINRA Rule 4210 Also Complies with and Is Consistent with FINRA’s Rulemaking Authority.

SR-FINRA-2015-036 was previously and correctly approved by the Division, a decision that petitioners did not seek Commission or judicial review of despite their participation in the

rulemaking process. Accordingly, any arguments against SR-FINRA-2015-036 that should have been raised in such review, and should not be considered now. But even if the Commission were to consider the amendments to FINRA Rule 4210 in SR-FINRA-2021-010 and SR-FINRA-2015-036 together, those amendments remain consistent with the factors and objectives in the Exchange Act.

As described *supra*, Section 15A(b)(6) establishes that FINRA rules should 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.” 15 U.S.C. § 78f(b)(6). FINRA promulgated SR-FINRA-2015-036 in accordance with these factors, determining that it would “help to reduce the risk of loss due to counterparty failure in one of the largest fixed income markets and thereby help protect investors and the public interest.” *See Notice of Filing of a Proposed Rule Change To Amend FINRA Rule 4210 (Margin Requirements) To Establish Margin Requirements for the TBA Market*, Securities Exchange Act Release No. 76148, File No. SR-FINRA-2015-036, 80 Fed. Reg. 63,603, 63,609 (Oct. 20, 2015) (“Notice”). FINRA further determined that “unsecured credit exposures that exist in the TBA market today can lead to financial losses by members. Permitting members to deal with counterparties in the TBA market without collecting margin can facilitate increased leverage by counterparties, thereby potentially posing a risk to FINRA members that extend credit and to the marketplace as a whole.” *Id.*

Petitioners make various assertions against SR-FINRA-2015-036, all of which have been addressed, previously and repeatedly, through the SR-FINRA-2015-036 and SR-FINRA-2021-010 rulemaking processes.

First, Petitioners assert that the rule changes are unnecessary, including due to purported redundancy with contractual margin requirements that are commonly imposed by clearing firms,

and that FINRA has presented no evidence that the rule changes are necessary. Petition at 34-35, 43. That is incorrect. FINRA has consistently stated the rationale for the CAT margin regime: to address the risk arising from unsecured credit exposure that exists in the CAT market and the risk posed by counterparties' increased use of leverage in the CAT market if no margin requirements were applicable. SR-FINRA-2021-010 at 5-6; FINRA Letter at 4-6.¹⁰ Most firms that have participated in FINRA's outreach efforts have indicated that they have the ability—through margining agreements—to collect the margin necessary to comply with the CAT margin regime, and, as a practical matter, have begun adjusting to the requirements of SR-FINRA-2015-036 as if it was currently in effect. SR-FINRA-2021-010 at 27-28. Indeed, as discussed above, FINRA's pre-existing rules already impose requirements on firms to monitor and provide for mark-to-market losses through capital charges under Rule 4210(e)(2)(F).

As to Petitioners' claim that FINRA failed to account for the fact that clearing firms, including Pershing, already impose margin requirements by contract, Petition at 34, if anything, this fact undermines Petitioners' argument that margining CATs is unnecessary. In any event, under SR-FINRA-2015-036, to the extent that the clearing broker-dealer is required to collect margin it is required to collect it from its counterparty, and Petitioners fail to address why in that framework the clearing broker-dealer would also collect margin from the end counterparty as a commercial matter. *See* SR-FINRA-2021-010 at 13-14.

¹⁰ The 2016 Approval Order endorsed this rationale. *See* 2016 Approval Order, 81 Fed. Reg. at 40375 (“The Commission agrees with FINRA that imposing mandatory margin requirements on FINRA members transacting business with counterparties in the TBA market addresses a gap between margining in the TBA market and margin practices and regulatory developments in other markets. Margin collateral collected by a FINRA member may mitigate a broker-dealer's financial losses in the event of a counterparty default, and, in turn, serve to protect the broker-dealer's other customers. Consequently, the Commission believes that the proposed rule change would further the purposes of the Exchange Act as it is reasonably designed to protect investors and the public interest.”).

Moreover, SR-FINRA-2015-036 imposes a very conservative requirement on CATs, requiring members to collect margin for *existing* mark-to-market losses, without any provision for margin to provide for potential future market movements—more favorable treatment than applies to other types of forward-settling securities, for which “maintenance margin” is generally required even before any mark-to-market loss is recognized. *Cf.* FINRA Rule 4210(b).

Second, Petitioners are wrong to claim that FINRA has not adequately considered the potential market dislocation effects of the changes to FINRA Rule 4210, *i.e.*, (i) the purported competitive advantage on broker-dealers with bank affiliates (who are not subject to FINRA Rule 4210) compared to broker-dealers without bank affiliates, Petition at 27-29, and (ii) the disparate effects on small or medium-sized broker-dealers, including minority and female-owned broker-dealers, Petition at 29-31. To the contrary, commenters specifically raised these issues, FINRA considered and responded to them, and the Division found FINRA’s responses to be adequate.

Specifically, FINRA considered these arguments in each of the four rounds of comments it offered to the public regarding SR-FINRA-2015-036, starting with its initial proposal in Regulatory Notice 14-02, issued in January 2014. Following that notice, FINRA received comments that raised arguments about the risks SR-FINRA-2015-036 posed to smaller entities. *See* Notice, 80 Fed. Reg. at 63,615 (“Commenters suggested that imposing margin requirements on these types of products would have detrimental effects on various market participants, in particular smaller member firms, mortgage bankers, investors and consumers of mortgages, and that these detrimental effects would outweigh the regulatory benefit.”); *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*, Securities Exchange Act Release No. 76908, File No.

SR-FINRA-2015-036, 81 Fed. Reg. 3,532, 3,538 (Jan. 21, 2016) (“Order Instituting Proceedings”) (stating that SR-FINRA-2015-036 “would increase costs on various participants in the mortgage market, including small, medium or regional participants,” or how “all but the largest firms would be driven out of the market”).

SR-FINRA-2015-036 was then accompanied by an “economic analysis of the proposed rule change’s potential impact,” and FINRA specifically revised SR-FINRA-2015-036:

so as to ameliorate the proposed rule change’s impact on business activity and to address the concerns of smaller customers that do not pose material risk to the market as a whole. These revisions include[d] among other things the establishment of an exception from the proposed margin requirements for any counterparty with gross open positions amounting to \$2.5 million or less, subject to specified conditions, as well as specified exceptions to the proposed maintenance margin requirement and modifications to the de minimis transfer provisions.

Notice, 80 Fed. Reg. at 63,609. FINRA acknowledged that SR-FINRA-2015-036 would “likely impose direct and indirect costs,” but it ultimately determined that “the proposed requirements are needed because the unsecured credit exposures that exist in the TBA market today can lead to financial losses by members.” Order Instituting Proceedings, 81 Fed. Reg. at 3,539.¹¹ In its approval of SR-FINRA-2015-036, the Division recognized the kind of arguments that Petitioners are making—and “that FINRA responded appropriately to their concerns.” *See* 2016 Approval Order, 81 Fed. Reg. at 40,374-75.¹²

¹¹ *See also* Notice, 80 Fed. Reg. at 63,611 (recognizing that “[s]ome parties who currently transact in the TBA market may choose to withdraw from or limit their participation in the TBA market,” and that “[r]educed participation may lead to decreased liquidity in the market for certain issues or settlement periods,” but nevertheless noting that “[t]hese market-wide impacts on liquidity would be limited if exiting market participants represent a small proportion of market transactions while market participants that choose to remain, or new participants that choose to enter the market, increase their activities and thereby offset the impact of participants that exit the market”).

¹² FINRA also addressed liquidation concerns. *See* SR-FINRA-2015-036, Proposed Amend. No. 1 at 17 (“With respect to position liquidation, while it is true that longstanding language under FINRA Rule 4210(f)(6) sets forth a 15-day period, more recent requirements adopted under the portfolio margin rules, which have been in widespread use among members, set forth a three-day time frame. FINRA believes that, with respect to Covered Agency Transactions, the five-day period should provide sufficient time for

Finally, contrary to Petitioners’ assertions, FINRA has not failed to consider systemic risk in promulgating SR-FINRA-2015-036, Petition at 40-41, including any alleged risk SR-FINRA-2015-036 creates for the MBS “chain” transaction structure, Petition at 35-40. Far from it, systemic risk was one of the reasons that FINRA promulgated SR-FINRA-2015-036 in the first place. *See* Notice, 80 Fed. Reg. at 63,610 (noting FINRA’s specific concern that “unmargined positions in the TBA market” could “raise systemic concerns”: “[w]ere one or more counterparties to default, the interconnectedness and concentration in the TBA market may lead to potentially broadening losses and the possibility of substantial disruption to financial markets and participants”). And to the extent that certain market participants are no longer able to take on the same amount of risk that they were prior to SR-FINRA-2015-036, that will reduce systematic risk rather than increasing it.

Petitioners are also wrong to say that FINRA has not addressed the concern about “chain” transactions in significant detail, Petition at 35, considering the different scenarios Petitioners presented in their comment letters. *See* SR-FINRA-2021-010, Proposed Amend. No. 1 at 7, 9-13. Petitioners suggest that the requirement for multiple parties in a chain of CATs to collect margin or take a capital charge is a flaw. *See* Petition at 35-40. But SR-FINRA-2021-010 is designed to protect FINRA members against the risk of counterparty default. In that context, a given broker-dealer is not protected by the fact that another broker-dealer “up the chain” has already collected margin or taken a capital charge. Rather, that broker-dealer is exposed to the contractual obligation to buy the securities on the settlement date and the credit risk that its counterparty will default on

members to resolve issues. Further, as FINRA noted in the original filing, FINRA believes the five-day period is appropriate in view of the potential counterparty risk in the TBA market. Consistent with longstanding practice under FINRA Rule 4210(f)(6), the proposed rule allows FINRA to specifically grant the member additional time. FINRA maintains, and regularly updates, the Regulatory Extension System for this purpose.”) (footnotes omitted). FINRA further addressed liquidation concerns in the 2021 rulemaking, as noted above.

such purchase. These transactions are not, as Petitioners argue, “riskless,” Petition at 35, and the requirement that *each* FINRA member manage that risk by collecting margin or taking a capital charge is necessary for the safeguards in the CAT margin regime to work.

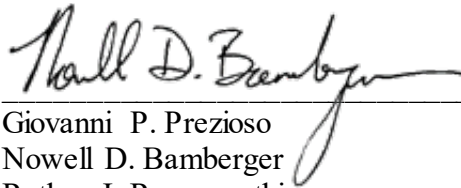
IV. CONCLUSION

For the foregoing reasons, the Commission should find that SR-FINRA-2021-010 is consistent with the Exchange Act and Commission rules, and accordingly, it should be approved.

Dated: May 10, 2022
Washington, D.C.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Nowell D. Bamberger, counsel for the Financial Industry Regulatory Authority, Inc. (“FINRA”), hereby certify that on May 10, 2022:

I caused a copy of FINRA’s Statement in Support of Proposed Rule Change to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (File No. SR-FINRA-2021-010) to be filed with the U.S. Securities and Exchange Commission by electronic mail at Secretarys-Office@sec.gov.

I also caused a copy of FINRA’s Statement in Support of Proposed Rule Change to Amend the Requirements for Covered Agency Transactions Under FINRA Rule 4210 (File No. SR-FINRA-2021-010) to be served on the following parties by electronic mail and U.S. mail:

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Dated: May 10, 2022



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