

Notice to Members

APRIL 2003

SUGGESTED ROUTING

Corporate Finance
Legal and Compliance
Operations
Senior Management
Technology
Trading and Market Making
Training

KEY TOPICS

Debt Securities
Dissemination
Operations
Rule 6200 Series
Transaction Reporting

INFORMATIONAL

Corporate Debt Securities

Dissemination of Additional Corporate Debt Securities
Will Begin on April 14, 2003

Executive Summary

On January 31, 2003, the Securities and Exchange Commission (SEC or Commission) approved an amendment to Rule 6250 of the Trade Reporting and Compliance Engine (TRACE) Rules, the Rule 6200 Series, to require dissemination of transaction information on 90 Investment Grade securities that are rated "Baa/BBB."¹ Rule 6250(a)(4), as approved on January 31, required NASD to select the 90 bonds. During the selection process, NASD determined that if an incremental, additional number of "Baa/BBB" bonds were disseminated, the quality of information NASD would collect would improve substantially. On March 17, 2003, NASD filed an amendment to Rule 6250(a)(4) to allow NASD to select up to 120 bonds rated "Baa/BBB" for dissemination. The proposed increase was effective upon filing with the SEC.

NASD has identified the 120 "Baa/BBB" TRACE-eligible securities for which transaction information will be disseminated, and will implement dissemination on April 14, 2003, at 8:00 a.m., Eastern Time. The text of Rule 6250(a)(4), as amended on March 17, 2003, is set forth in Attachment A.

Questions/Further Information

Questions concerning this *Notice* should be directed to tracefeedback@nasd.com; Justin Tubiolo, Vice President, Fixed Income, Regulatory Services and Operations, at (212) 858-4419; Elliot Levine, Chief Counsel, Market Operations, Regulatory Services and Operations, at (212) 858-4174; or Sharon K. Zackula, Assistant General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8985.

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Background and Discussion

NASD began requiring members to report transaction information on all TRACE-eligible corporate debt securities on July 1, 2002. Those transactions that are subject to dissemination are a smaller group. First, on July 1, 2002, NASD began disseminating information on transactions occurring in two types of securities: (1) TRACE-eligible securities that have an initial issuance size of \$1 billion or greater and are Investment Grade at the time of receipt of the transaction report; and (2) 50 TRACE-eligible securities that are actively traded, Non-Investment Grade,² and meet other criteria set forth in Rule 6250(a)(2). Under these provisions, approximately 540 securities were subject to dissemination. Second, on March 3, 2003, NASD began disseminating information on transactions occurring in a third group of securities, which includes all TRACE-eligible securities that are Investment Grade, are rated by Moody's as "A3" or higher, and by S&P as "A-" or higher, and have an original issue size of \$100 million or greater.³ With the implementation of this provision, NASD currently disseminates transaction information on more than 4,200 TRACE-eligible securities.

Dissemination of Additional TRACE-Eligible Securities Rated "Baa/BBB"

In *Notice to Members 03-12*, NASD indicated that it would announce the dissemination of a fourth category of securities, a designated group of "Baa/BBB"-rated TRACE-eligible securities, upon completing the process of identifying the securities. During the selection process, NASD, based on

guidance from independent economists, determined that the database of disseminated transaction data on "Baa/BBB" TRACE-eligible securities should be incrementally increased to include transaction information on up to 120 securities. This modest increase in the transparency of "Baa/BBB" securities would improve significantly the quality of the data to be collected. The increased transparency would provide a better foundation for determining the effect, if any, of transparency on liquidity.

On March 17, 2003, NASD modified Rule 6250(a)(4) by filing a rule change that became effective when filed with the SEC. The modification allows NASD to select up to 120 securities, which is a maximum increase of 30 securities.⁴ Specifically, NASD must designate the "triple-B-" rated securities using three groups, Group 1, Group 2, and Group 3. Each of the three groups is to be composed of not more than 50 securities. At the time of designation, each TRACE-eligible security in Group 1 must be rated "Baa1/BBB+" and each TRACE-eligible security in Groups 2 and 3 must be rated, respectively, "Baa2/BBB" and "Baa3/BBB-." In addition, if a TRACE-eligible security has a rating from only one rating agency, it may not be designated.

NASD has designated the securities, and is now able to establish the effective date. NASD will begin dissemination of transaction information in 120 "triple-B"-rated TRACE-eligible securities on April 14, 2003.

Endnotes

- 1 See Securities Exchange Act Release No. 47302 (January 31, 2003), 68 FR 6233 (February 6, 2003) (File No. SR-NASD-2002-174) (Approval Order). "Investment Grade" is defined in Rule 6210(h) to mean "any TRACE-eligible security rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories." In the Approval Order, the SEC also approved proposed changes to disseminate a new and large class of additional TRACE-eligible Investment Grade securities. Specifically, under Rule 6250(a)(3), any TRACE-eligible security rated A3/A- or better and having an initial issuance size of \$100 million or greater became subject to dissemination. NASD implemented dissemination of the A3/A- securities on March 3, 2003. See *Notice to Members 03-12* (February 2003).
- 2 "Non-Investment Grade" is defined in Rule 6210(i) to mean "any TRACE-eligible security that is unrated, non-rated, split-rated (where one rating falls below Investment Grade), or otherwise does not meet the definition of Investment Grade...."
- 3 In addition, a security that is required to be disseminated under this criteria, on or after the effective date of the provision, will continue to be subject to dissemination unless the security is downgraded below "Baa3/BBB-."
- 4 See Securities Exchange Act Release No. 47566 (March 25, 2003) 68 FR 15490 (March 31, 2003) (File No. SR-NASD-2003-41) (notice of filing and immediate effectiveness of proposed rule to disseminate up to 30 additional corporate bonds). In this filing to amend Rule 6250(a)(4), NASD proposed that not more than 120 TRACE-eligible bonds rated "Baa/BBB" at the time of designation would be designated and disseminated.

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ATTACHMENT A

6250. Dissemination of Corporate Bond Trade Information

(a) General Dissemination Standard

Immediately upon receipt of transaction reports received at or after 8:00 a.m. through 6:29:59 p.m. Eastern Time, NASD will disseminate transaction information (except that market aggregate information and last sale information will not be updated after 5:15 p.m. Eastern Time) in the securities described below.

- (1) No Change.
- (2) No Change.
- (3) No Change.
- (4) Ninety to 120 TRACE-eligible securities designated by NASD that are rated “Baa/BBB” at the time of designation, according to the following standards.

(A) Three groups, each composed of up to 50 [30]TRACE-eligible securities (Group 1, Group 2, and Group 3), but collectively not exceeding 120, shall be designated by NASD. At the time of designation, each TRACE-eligible security in Group 1 must be rated “Baa1/BBB+[,]” and each TRACE-eligible security in Group 2 and Group 3 must be rated, respectively, “Baa2/BBB[,]” and “Baa3/BBB-[,]” [provided that if]If a TRACE-eligible security is rated one of the “Baa” ratings by Moody’s and one of the “BBB” ratings by S&P and the ratings indicate two different levels of credit quality, the lower of the two ratings will be used to determine the group to which a debt security will be assigned under this paragraph (a)(4).

- (B) No Change.
- (C) No Change.
- (b) through (d) No Change.