

# Notice to Members

FEBRUARY 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

SEC Approves Amendments to TRACE Rule 6250 and Other TRACE Rules: Transaction Information to be Disseminated on More than 4,000 Corporate Debt Securities

#### Executive Summary

On January 31, 2002, the Securities and Exchange Commission (SEC or Commission) approved amendments to Rule 6250 of the Trade Reporting and Compliance Engine (TRACE) rules, the Rule 6200 Series.<sup>1</sup> The amendments to TRACE Rule 6250 will allow NASD to begin disseminating transaction information on more than 4,000 qualifying Investment Grade corporate debt securities.<sup>2</sup> The SEC also approved minor changes to Rule 6210(e), the definition of "customer to a transaction," and Rule 6260. The rules, as amended, are set forth in Attachment A.

The amendments to the TRACE Rules will become effective on March 3, 2003, with one exception. New paragraph (a)(4) of Rule 6250, providing for the dissemination of 90 corporate debt securities that are rated "triple-B," will become effective shortly thereafter, on a date to be announced in a future *Notice to Members*. Currently, NASD is in the process of identifying the 90 specific securities that will be subject to dissemination, and will announce the effective date of Rule 6250(a)(4) when the process is complete.

#### Questions/Further Information

Questions concerning this *Notice* should be directed to [tracefeedback@nasd.com](mailto:tracefeedback@nasd.com); 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. At that time, NASD also began disseminating information on transactions occurring in approximately 540 TRACE-eligible securities. Specifically, under Rule 6250, transactions in two types of securities were subject to the TRACE dissemination requirements that took effect on July 1, 2002: (1) those transactions in a TRACE-eligible security having an initial issuance size of \$1 billion or greater that is Investment Grade at the time of receipt of the transaction report as set forth in Rule 6250(a)(1); and (2) those transactions in 50 TRACE-eligible securities that are actively traded, Non-Investment Grade,<sup>3</sup> and meet other criteria set forth in Rule 6250(a)(2). At the time that TRACE began, NASD also was obligated and intended to require the dissemination of additional securities in the future.

## Amendments to Increase Dissemination

NASD formed an advisory committee, the Bond Transaction Reporting Committee (BTRC), composed of 10 representatives, to study issues relating to transparency and increased dissemination of the universe of TRACE-eligible securities. With the concurrence of the BTRC, in early December 2002, NASD proposed to add the following two groups of securities to the list of securities that are subject to dissemination under Rule 6250. The SEC approved the proposed rule change on January 31, 2003.

First, in Rule 6250(a)(3), as approved, NASD will disseminate transaction information on any TRACE-eligible security that is Investment Grade; is rated by Moody's Investors Service, Inc. as "A3" or higher,<sup>4</sup> and by Standard & Poor's, a division of McGraw Hill Co., Inc., as "A-" or higher;<sup>5</sup> and has an original issue size of \$100 million or greater. In addition, a security that is required to be disseminated under the criteria above, on or after the effective date of this provision, will continue to be subject to dissemination unless the security is downgraded below "Baa3/BBB-."

Second, in Rule 6250(a)(4), as approved, NASD is required to disseminate transaction information on 90 TRACE-eligible securities designated by NASD that are rated "Baa/BBB" at the time of designation. As discussed in greater detail below, NASD will announce the effective date of this provision in a future *Notice to Members*, upon completing the process of identifying the 90 securities to be disseminated according to the criteria set forth in the Rule.

## Other Changes

The SEC also approved two additional minor rule changes to the TRACE Rules. First, in Rule 6210(e), NASD clarified the term "party to the transaction" to mean a customer, in addition to an introducing broker/dealer, if any, and an executing broker/dealer. Also, for the purposes of Rule 6210(e), "customer" includes a broker/dealer that is not an NASD member.<sup>6</sup>

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Rule 6260 generally requires a managing underwriter of a new TRACE-eligible security to provide to the TRACE Operations Center, within certain deadlines established in the rule, the following six types of information with respect to the new security: (1) a CUSIP number identifying the security; (2) the issuer name; (3) the coupon rate; (4) the maturity; (5) whether Rule 144A applies; and (6) a brief description of the issue. The SEC approved minor changes to clarify that if any of items (2) through (6) have not been determined at the time that the managing underwriter is required to submit the information, the managing underwriter may discuss with NASD submitting such other information "as NASD deems necessary." However, a managing underwriter must always submit the CUSIP number. Other minor changes are set forth in Attachment A.

### Effective Date

The amendments to the TRACE Rules will become effective on March 3, 2003, with one exception. New paragraph (a)(4) of Rule 6250, providing for the dissemination of 90 TRACE-eligible corporate debt securities that are rated "triple-B," will become effective shortly thereafter.

Extending the effective date for Rule 6250(a)(4) allows NASD to appropriately identify the 90 securities that will become subject to dissemination in accordance with the criteria in the Rule. Under paragraph (a)(4) of Rule 6250, NASD is required to identify 90 securities, by identifying three groups of 30 TRACE-eligible securities (Group 1, Group 2, and Group 3). 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. When the process of identification and designation is complete, NASD will announce the effective date of Rule 6250(a)(4) in a subsequent *Notice to Members* and transaction information on the 90 securities will begin to be disseminated.

### Endnotes

- 1 See Securities Exchange Act Release No. 47302 (January 31, 2003), 68 Fed. Reg. 6233 (February 6, 2003) (File No. SR-NASD-2002-174).
- 2 "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."
- 3 "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...."
- 4 Moody's Investor Service, Inc. (Moody's) is a nationally recognized statistical rating organization. Moody's is a registered trademark of Moody's Investors Service. Moody's ratings are proprietary to Moody's and are protected by copyright and other intellectual property laws. Moody's licenses ratings to NASD. Ratings may not be copied or otherwise reproduced, repackaged, further transmitted, transferred, disseminated, redistributed or resold, or stored for subsequent use for any purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person without Moody's prior written consent.

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- 5 Standard & Poor's, a division of the McGraw-Hill Companies, Inc. (S&P), is a nationally recognized statistical rating organization. S&P's ratings are proprietary to S&P and are protected by copyright and other intellectual property laws. S&P licenses ratings to NASD. Ratings may not be copied or otherwise reproduced, repackaged, further transmitted, transferred, disseminated, redistributed or resold, or stored for subsequent use for any purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person without S&P's prior written consent.
  - 6 In contrast, in Rule 0120(g), NASD defines the term "customer" to exclude a broker or a dealer.

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## ATTACHMENT A

### Text of Rule Changes.

Note: New language is underlined; deletions are in brackets.

#### 6200. TRADE REPORTING AND COMPLIANCE ENGINE (TRACE)

##### 6210. Definitions

The terms used in this Rule 6200 Series shall have the same meaning as those defined in [the Association's]NASD's By-Laws and Rules unless otherwise specified.

(a) through (d) No change.

(e) The term "party to the transaction" ["parties to the transaction"] shall mean [the]an introducing broker-dealer, if any, [and the]an executing broker-dealer, or a customer. For purposes of this Rule, customer includes a broker-dealer that is not an NASD member.

(f) through (i) No change.

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##### 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, [the Association]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) [relating to transactions] in[:] the securities described below.

(1) [a]A TRACE-eligible security [having an initial issuance size of \$1 billion or greater ]that is Investment Grade at the time of receipt of the transaction report and has an initial issuance size of \$1 billion or greater.[; and]

(2) [a]A TRACE-eligible security that is[ designated for dissemination according to the following criteria and is] Non-Investment Grade at the time of receipt of the transaction report and is designated by NASD for dissemination according to the following criteria.

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(A) through (B) No change.

(3) A TRACE-eligible security that is Investment Grade, is rated by Moody's Investors Service, Inc. as "A3"<sup>1</sup> or higher, and by Standard & Poor's, a division of McGraw Hill Co., Inc., as "A-"<sup>2</sup> or higher, and has an original issue size of \$100 million or greater. If a security is rated under this provision to qualify for dissemination at any time on or after the effective date of the rule, dissemination of transaction information on the security will continue under this paragraph unless the security is downgraded below Baa3/BBB-.

(4) Ninety TRACE-eligible securities designated by NASD that are rated Baa/BBB at the time of designation, according to the following standards.

(A) Three groups composed of 30 TRACE-eligible securities (Group 1, Group 2, and Group 3) 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 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 paragraph (a)(4).

(B) A TRACE-eligible security that has a rating from only one rating agency will not be designated under paragraph (a)(4).

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1. Moody's Investors Service, Inc. ("Moody's") is a nationally recognized statistical rating organization. Moody's is a registered trademark of Moody's Investors Service. Moody's ratings are proprietary to Moody's and are protected by copyright and other intellectual property laws. Moody's licenses ratings to NASD. Ratings may not be copied or otherwise reproduced, repackaged, further transmitted, transferred, disseminated, redistributed or resold, or stored for subsequent use for any purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person without Moody's prior written consent.

2. Standard & Poor's, a division of the McGraw-Hill Companies, Inc. ("S&P"), is a nationally recognized statistical rating organization. S&P's ratings are proprietary to S&P and are protected by copyright and other intellectual property laws. S&P's licenses ratings to NASD. Ratings may not be copied or otherwise reproduced, repackaged, further transmitted, transferred, disseminated, redistributed or resold, or stored for subsequent use for any such purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person without S&P's prior written consent.

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(C) Dissemination of transaction information on a TRACE-eligible security that is designated under paragraph (a)(4) will not be discontinued if one rating is, or both ratings, are downgraded or upgraded.

(b) through (d) No change.

**6260. Managing Underwriter Obligation To Obtain CUSIP**

(a) No change.

(b) For such TRACE-eligible securities, the managing underwriter must provide to the TRACE Operations Center: (1) the CUSIP number; (2) the issuer name; (3) the coupon rate; (4) the maturity; (5) whether Rule 144A applies; and (6) a brief description of the issue (e.g., senior subordinated note, senior note), or if any of items (2) through (6) [such information] has not been determined, such other information as [the ]NASD deems necessary. The managing underwriter must obtain the CUSIP number and provide it and the information listed as (2) through (6) not later than 5:00 p.m. on the business day preceding the day that the registration statement becomes effective, or, if registration is not required, the day before the securities will be priced. If an issuer notifies [an] managing underwriter, or the issuer and the managing underwriter determine, that the TRACE-eligible securities of the issuer shall be priced, offered and sold the same business day in an intra-day offering under Rule 415 of the Securities Act of 1933 or Rule 144A of the Securities Act of 1933, the [member] managing underwriter shall provide the information not later than 5:00 p.m. on the day that the securities are priced and offered, provided that if such securities are priced and offered on or after 5:00 p.m., the [member]managing underwriter shall provide the information not later than 5:00 p.m. on the next business day. [A member] The managing underwriter must make a good faith determination that the security is a TRACE-eligible security before submitting the information to the TRACE Operations Center.