

Sharon Zackula
Associate Vice President
and Associate General Counsel

Direct: (202) 728-8985
Facsimile: (202) 728-8264

December 22, 2009

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File No. SR-FINRA-2009-065: Response to Comments

Dear Ms. Murphy:

This letter responds to comments received by the Securities and Exchange Commission ("SEC" or "Commission") to the above-referenced rule filing, a proposal to add Asset-Backed Securities to TRACE as "TRACE-Eligible Securities" and to require members to report transactions in such securities to TRACE.¹ The proposed rule change was published for comment in the Federal Register on October 28, 2009.² The Commission received 4 comments in response to the proposed rule change.³

¹ For purposes of this letter, "Asset-Backed Security" is used as that term is defined in Rule 6710(m), as proposed for amendment in SR-FINRA-2009-065. Rule 6710(m) was approved by the SEC as part of SR-FINRA-2009-010, the amendments to the Rule 6700 Series to add Agency Debt Securities and primary market transactions to TRACE. See Exchange Act Release No. 60726 (September 28, 2009), 74 FR 50991 (October 2, 2009) (Order approving SR-FINRA-2009-010); see also Regulatory Notice 09-57 (September 2009) (announcing the effective date of March 1, 2010).

² Securities Exchange Act Release No. 60860 (October 21, 2009), 74 FR 55600 (October 28, 2009). The comment period closed on November 18, 2009.

³ Comments filed with the SEC are from: Beth N. Lowson, The Nelson Law Firm, dated November 13, 2009 ("Lowson Letter"); Willard Stein, Ph.D., CFA, dated November 15, 2009 ("Stein Letter"); John Hogue, Alexandria Capital Management, dated November 17, 2009 ("Hogue Letter"); and George P. Miller, American Securitization Forum ("ASF") and Randolph C. Snook, Securities Industry and Financial Markets Association ("SIFMA"), dated November 18, 2009 ("SIFMA/ASF Letter").

The commenters express general support for adding Asset-Backed Securities to TRACE, but raise concerns regarding the reporting period for Asset-Backed Securities, the non-dissemination of Asset-Backed Securities transaction information, several proposed reporting requirements, operational issues, implementation and fees.

End-of-Day Reporting.

For Asset-Backed Securities transactions, in proposed Rule 6730(a)(6) FINRA proposed that the reporting period be extended to no later than the close of business on the date of trade (“T”), and, for such transactions executed after 5:00 p.m. Eastern Time, to the close of business on T + 1. Two commenters express reservations regarding the proposed extension of the reporting period. One commenter states that transaction information on Asset-Backed Securities must be submitted simultaneously with the appropriate benchmarks used for pricing it, and if the information is delayed as proposed, the information will have little use or meaning, especially in liquid markets.⁴ The second commenter criticizes the delays imbedded in proposed Rule 6730(a)(6) for reporting Asset-Backed Securities transactions together with the proposal not to disseminate transaction information on Asset-Backed Securities, stating that such provisions left the U.S. taxpayer at risk because, if volatility returns and investors fear that such assets will again become “impossible” to value, the financial system will be vulnerable to another panic.⁵ In contrast, a third commenter requests that FINRA further extend the proposed reporting period for Asset-Backed Securities transactions to the close of business on T + 1 given the operational complexity of reporting such securities, or, at least, amend the “cutoff time” for when trades may be reported on T + 1 (e.g., permit transactions executed after 12:00 p.m. Eastern Time to report on T + 1).⁶

In response to the two commenters that are opposed to the longer reporting period for Asset-Backed Securities transaction reporting, FINRA notes that since the data is not subject to dissemination, the extension of the reporting period for Asset-Backed Securities transactions does not impact transparency with respect to this class of debt securities. If, after a sufficient period of studying reportable data with respect to Asset-Backed Securities, FINRA proposes dissemination, there will be opportunity to comment on the timeliness of data submission and its impact, if any, on transparency. Recognizing a commenter’s concern about the difficulties of implementing the reporting of Asset-Backed Securities, especially the most complex of such instruments, in Amendment No. 1 to SR-FINRA-2009-065 FINRA will propose to amend to extend the proposed reporting period for Asset-Backed Securities to no later than T+1 during

⁴ See Hogue Letter.

⁵ See Stein Letter.

⁶ See SIFMA/ASF Letter.

TRACE System Hours. The proposed amendment reflects FINRA's commitment to work with the industry to insure effective and efficient implementation of the expansion of TRACE to include Asset-Backed Securities. However, the extended T+1 reporting period will be proposed as a six month pilot program, and, upon its expiration, the reporting requirement will revert to reporting no later than the date of trade during TRACE System Hours (with standard exceptions set forth in Rule 6730(a)(6)(B) for Asset-Backed Securities transactions that occur near or at the end of the TRACE System Hours, or when the TRACE system is closed).

Dissemination.

Two commenters oppose FINRA's proposal not to disseminate transaction information on Asset-Backed Securities under proposed Rule 6750(b)(4). As noted above, one commenter stated that the failure to provide information to market participants, if combined with market volatility, may leave the financial system vulnerable to another panic due to investors' fears that Asset-Backed Securities again might be difficult to value.⁷ Another commenter stated that such transactions should be disseminated to the fullest extent possible, and also urged FINRA to reduce or eliminate the existing limitations in TRACE market data that mask the total size of a trade –the “dissemination caps.”⁸ In contrast, a commenter supported FINRA's decision not to disseminate transaction information in Asset-Backed Securities at the time that the proposed reporting requirements will take effect (if approved by the SEC), and to study data collected on the volume and trading in various types of Asset-Backed Securities prior to making any determinations regarding dissemination.⁹ Although noting that the membership of the commenter has a divergence of opinion on the dissemination of transaction prices, the commenter urges that decisions regarding public post-trade price dissemination be carefully approached, and designed to avoid the possibility that any such requirements would hamper a return to normal market conditions, liquidity in such instruments, the government's efforts to safeguard financial stability and greater access to credit and lending.¹⁰ FINRA continues to believe that information on Asset-Backed Securities transactions should be collected and analyzed before a decision regarding dissemination of transaction information is made by FINRA as to the utility of such information for transparency purposes as well as other consequences to this spectrum of

⁷ See Stein Letter.

⁸ See Lowson Letter. Under TRACE dissemination protocols, the TRACE market data does not indicate the actual numbers of bonds traded in investment grade debt if the par value exceeds \$5 million and in non-investment grade debt if the par value exceeds \$1 million.

⁹ See SIFMA/ASF Letter, pp. 2-3, 11-13.

¹⁰ Id.

the debt market from dissemination. After a period of study, a separate proposed rule change will be filed if FINRA determines that its study of the trading data provides a reasonable basis to seek dissemination of transaction information on Asset-Backed Securities, and market participants and the public will have an additional opportunity to comment on dissemination at that time.

New Issue Asset-Backed Securities.

According to one commenter, the new issue process for many private label mortgage-backed securities (“MBSs”) and collateralized debt obligations (“CDOs”) differs significantly from that of many other fixed income markets, and a single class of an issuance may be sold to more than one investor on different days, rather than sold in multiple executions to more than one investor on a single day.¹¹ The commenter notes that under FINRA’s definitions of “List or Fixed Offering Price Transaction” and “Takedown Transaction,” which are limited to transactions executed at a uniform, fixed price in a new offering that occur during the first day of an offering, members offering such Asset-Backed Securities will not qualify for reporting under Rule 6730(a)(5) (and two other provisions that are beneficial to members set forth below), even if multiple new issue transactions are executed at a fixed price, because such trades usually occur over multiple days. The commenter suggests that FINRA expand the defined terms.

Under Rule 6730, transactions that are List or Fixed Offering Price Transactions or Takedown Transactions under Rule 6710(q) and Rule 6710(r), respectively, may be reported as late as close of business on T + 1 (and must be identified with the appropriate indicator), and, under Rule 6750, such transactions are not disseminated. In addition, members do not pay a reporting fee for timely reporting of such transactions under Rule 7730(b). In the proposed rule change as initially filed, FINRA proposed that a subset of Asset-Backed Securities – Agency Pass Through Mortgage-Backed Securities – would be excluded from the provisions permitting members to report List or Fixed Offering Price Transactions or Takedown Transactions no later than T + 1 and a second proposed rule change providing fee relief.

As discussed above, FINRA proposes to amend the proposed rule change to permit members to report *all* transactions in Asset-Backed Securities as late as the close of business on T + 1 for a pilot period. In addition, FINRA previously proposed that *all* transactions in Asset-Backed Securities not be disseminated. At this time, FINRA declines to expand the definitions of List or Fixed Offering Price Transaction or Takedown Transaction in Rule 6710(q) and (r), respectively, to extend them to transactions that occur beyond the first day of a primary offering for certain transactions in Asset-Backed Securities. However, FINRA intends to review reported Asset-Backed Securities transactions and determine if any amendments to the definitions are appropriate. In addition, FINRA has determined that, at this time, all

¹¹ See SIFMA/ASF Letter, pp. 8-9.

primary market transactions in any type of Asset-Backed Security should be excluded from the definitions of List or Fixed Offering Price Transactions or Takedown Transactions, and will propose amendments to Rule 6710(q) and Rule 6710(r) accordingly. At this time, this approach strikes the appropriate balance among competing concerns. Although FINRA declines to expand Rule 6710(q) and Rule 6710(r) at this time, after FINRA has an opportunity to study transaction data for Asset-Backed Securities, FINRA will review the commenter's suggestion to expand the definitions of List or Fixed Offering Price Transaction or Takedown Transaction to extend them to certain transactions that occur on the second day of a primary offering and also will review the proposed general exclusion of Asset-Backed Securities.

Operational Issues.

One commenter raises a number of operational issues, including those relating to the unique data requirements of reporting Asset-Backed Securities (e.g., factors and settlement), and security identification (e.g., Asset-Backed Securities not assigned CUSIPs, use of mortgage pool numbers, and development of FINRA symbols with internal logic and the process of assigning such symbols).¹²

a. *Factor Reporting.* The commenter suggests that FINRA modify the proposed requirement that a member report the specific Factor used to price an Asset-Backed Security transaction.¹³ The commenter recommends that FINRA instead obtain and maintain Factor information from master data files that are commercially available and also modify the proposed reporting requirement to require dealers to report the actual Factor only if the Factor used to price the transaction is not the most current Factor that is publicly available at the time.¹⁴ FINRA believes that this modification proposed by the commenter will increase the accuracy of trade reporting of Asset-Backed Securities transactions and eliminate certain reporting and compliance burdens, and will propose an amendment that is consistent with the above comment.

b. *Date of Settlement.* In amendments to Rule 6730(d)(4)(B), FINRA proposed two amendments regarding the reporting of settlement terms. First, FINRA proposed a technical revision to substitute the term "T + 3" for the term "regular way" regarding the settlement of securities other than Asset-Backed Securities. Second, in recognition of certain settlement conventions for Asset-Backed Securities, FINRA proposed: (1) for the settlement of Agency Pass-Through Mortgage-Backed Securities done in conformity with the uniform practices established as "good delivery" for such

¹² See SIFMA/ASF Letter.

¹³ See SIFMA/ASF Letter, pp. 3-6.

¹⁴ Id. (In addition, the commenter suggests that FINRA incorporate indicators to identify the trade as one executed using the current factor or a different factor.)

transactions on the next occurring monthly date announced for settlement, that no settlement-related indicator or modifier would be necessary; and (2) for all other Asset-Backed Securities transactions, that members report the number of days to settlement. The commenter suggests that FINRA amend Rule 6730(d)(4)(B) to require members to report the actual date of settlement (e.g., March 17, 2010) for all Asset-Backed Securities and also to indicate that the transaction will be settled: (i) “regular way” (i.e., T + 3 or in conformity with the uniform practices established as “good delivery” for the type of Asset-Backed Security traded); or (ii) not “regular way” (i.e., not T + 3 or not in conformity with the uniform practices established as “good delivery” for the type of Asset-Backed Security traded).¹⁵ FINRA agrees and will propose an amendment to Rule 6730(d)(4)(B) accordingly.

c. *TBA CUSIPs*. FINRA agrees with the comment regarding the reporting of Asset-Backed Security transactions where a TBA CUSIP is used to identify the trade, and confirms that (1) under the proposed rule change, dealers will be able to report trades to FINRA using these generic CUSIPs as identifiers, and (2) dealers will not be expected to amend TBA trades with mortgage pool numbers when allocations are made in the settlement process, in conformity with conventions regarding permitted variances, as such allocations do not impact price and are solely a settlement function.¹⁶

d. *Securities without CUSIPs or Other “Streetwide” Identifiers*. The commenter notes that in cases where CUSIPs are not being used to identify a security or have not yet been assigned, if security identifiers are created and used that are not recognized generally by the street, confusion will result.¹⁷ As noted above, FINRA is aware of the intricacies of the Asset-Backed Securities market, and, in particular, the origination process, and knows that in many cases uniform security identifiers may not be available at issuance. FINRA is working to develop a process for the efficient and timely identification of such securities and to provide a security identifier when necessary. FINRA will continue to consult with market participants regarding operational and technological issues during the development of the process.

e. *Implementation*. The commenter raises implementation concerns, noting the substantial increase in the number of securities and transactions that will become reportable, competing technology demands, and the scope of changes that will be needed to comply with Asset-Backed Security reporting.¹⁸ The commenter also urges FINRA to provide for adequate testing prior to implementation.¹⁹

¹⁵ See SIFMA/ASF Letter, p. 11.

¹⁶ See SIFMA/ASF Letter, p. 3.

¹⁷ See SIFMA/ASF Letter, pp. 4-5.

¹⁸ See SIFMA/ASF Letter, pp. 9-11.

¹⁹ *Id.* at p. 10.

FINRA believes that the implementation period of the proposed rule change will provide firms with ample time to take the steps necessary for successful implementation, and there are several steps FINRA is taking to facilitate implementation for members. FINRA will obtain security information from various data sources to update the TRACE Issue Master file for all available outstanding Asset-Backed Securities before reporting is implemented, which will substantially reduce firms' reporting and notification burdens regarding the volume of new securities to be added to the system both during implementation and thereafter. In addition, the modifications FINRA proposes to the TRACE rules and system generally take into account the unique characteristics and complexities of Asset-Backed Securities, and while FINRA recognizes that firms will be required to modify systems and procedures to reflect, for reporting purposes, some of the unique aspects of Asset-Backed Securities, not all of the specific or unique aspects of Asset-Backed Securities are implicated in the reporting of such transactions. Also, FINRA recognizes that a reasonable test period will facilitate efficient implementation of the proposed rule change and will endeavor to provide technical specifications and testing opportunities to members in a timely manner before the proposed rule change becomes effective. Moreover, FINRA has consulted and will continue to reach out to Asset-Backed Securities market participants to insure an effective and efficient transition to the reporting of such securities.

The commenter also urges FINRA to phase-in the reporting of Asset-Backed Securities transactions, starting with secondary market transactions, and after six months, adding primary market transactions.²⁰ FINRA declines to separate or phase-in the implementation of the reporting of primary and secondary market transactions in Asset-Backed Securities. Many Asset-Backed Securities are sold in a primary market transaction and thereafter may not trade or trade very infrequently.²¹ If FINRA delayed the reporting of primary market transactions as requested, it is likely that FINRA would not be aware of many of the Asset-Backed Securities sold into the market during that period as no transaction report would be required. Also, by requiring that all transactions in Asset-Backed Securities begin reporting on the same date, FINRA eliminates the implementation issue and any compliance burden associated with determining if a transaction is a primary or secondary market transaction.

f. *Trade Modifications.* Regarding specific ABS trade modification issues, a commenter raises concerns related to certain scenarios.²² In connection with one scenario discussed, FINRA notes that it does not interpret Rule 6730 as requiring a member to modify a previously reported TBA transaction to include the relevant

²⁰ Id.

²¹ See e.g., SIFMA/ASF Letter, pp. 3, 12 -13.

²² See SIFMA/ASF Letter, pp. 7-8.

mortgage pool numbers when allocations are made in the settlement process, if the pools are allocated and delivered to conform to the conventions of good delivery for such type of Asset-Backed Security, including the “variance” permitted for good delivery (*i.e.*, if delivered in conformity with the permitted variance, price is not affected). Generally, amended transaction reports will not be required when modifications occur relating to delivery of assets/collateral and/or settlement of a transaction.

The commenter also raises issues regarding other modifications of trade reports (*i.e.*, “cancels and corrects” that are not specific to Asset-Backed Securities transactions).²³ The comments regarding this type of modification of trade reports are not relevant to the proposed rule change. However, FINRA has reviewed this operational issue and the related fee issue with member firms on an ongoing basis and continues to take the issues raised by members firms under consideration.

g. *Updating TRACE Issue Master/TRACE Daily List.* The commenter requests that FINRA develop a methodology for more rapidly updating the TRACE Issue Master and/or the TRACE Daily List and communicating such updates to members intraday because many Asset-Backed Securities must be added to TRACE. The commenter notes that members will be able to more efficiently and timely report TRACE-Eligible Securities that previously have not been listed on the TRACE Issue Master if FINRA improves the processes for such updates and notifying members frequently during a trading day of new securities (or securities not previously included).²⁴ As noted above, to prepare for the addition of many Asset-Backed Securities to the system, FINRA is securing reference data from various data sources, and will populate the TRACE system with outstanding eligible securities prior to implementation. In addition, FINRA is working with firms to facilitate the more rapid incorporation of new securities information provided to FINRA Operations during TRACE System Hours and the more rapid dissemination during the business day of such new information to TRACE participants and data vendors. However, FINRA notes that members are in the best position to provide information, such as CUSIPs and pool numbers, regarding new Asset-Backed Securities and other securities not in the TRACE System, and are required to provide such information to FINRA Operations under Rule 6760 or, if attempting to report a transaction, under Rule 6730.

Fees.

A commenter states that FINRA should review TRACE fees to take into account the additional costs to broker-dealers of incorporating Asset-Backed Securities into TRACE, and should reduce TRACE fees “to the extent the additional TRACE fees

²³ See SIFMA/ASF Letter, pp. 7-8.

²⁴ See SIFMA/ASF Letter, pp. 3-4, 9.

are not reflective of the economies of scale this expansion will present to FINRA.”²⁵ The commenter notes that FINRA also will receive additional TRACE reporting fees when members begin to report Agency Debt Securities and primary market transactions.²⁶ In addition, the commenter states that modifications and adjustments to trades in certain types of Asset-backed Securities are common, and asks FINRA to consider eliminating the fees for modifying TRACE transaction reports.²⁷ FINRA does not believe that, as a general matter, it is axiomatic that the increase in regulatory costs to broker-dealers due to compliance with additional reasonable regulation is necessarily a basis for a reduction in fees or other assessments charged by FINRA to its members. Indeed, as a general matter, as regulation is amended or broadened in scope, FINRA may incur greater costs in its programmatic oversight of that regulation through analysis, examination and enforcement. Accordingly, we believe it is premature at this time to consider any fee adjustments as a result of this program.

Regarding the fees charged for the modification of trade reports, FINRA has addressed above the circumstances particular to certain transactions where modification of certain transaction information occurs or new information is exchanged between the parties (e.g., pools to be delivered), but a new report (and an additional fee) would not be required.²⁸ However, the commenter also raises issues regarding other modifications of trade reports (i.e., “cancels and corrects” that are not specific to Asset-Backed Securities transactions), for which the commenter seeks relief from both fee liability and FINRA’s determination that such modified trade reports are late. The comments regarding this type of modification of trade reports and the fee charged for such modified reports are not relevant to the specific issues of raised in the proposed rule change. However, FINRA has the operational and regulatory issues regarding modifications, and related fees under review and will continue to consider the issues raised by the commenter.

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²⁵ See SIFMA/ASF Letter, p. 11.

²⁶ Id. See also FINRA Regulatory Notice 09-57 (September 2009).

²⁷ See SIFMA/ASF Letter, p. 11.

²⁸ Variance is defined as the permitted maximum over- or under-allocation of securities or other assets, such as mortgages, that can be delivered to satisfy an outstanding commitment.

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FINRA believes that the foregoing responds to the material issues raised by the commenters to this rule filing. If you have any questions, please contact me at (202) 728-8985; email: sharon.zackula@finra.org. The fax number of the Office of General Counsel is (202) 728-8264.

Sharon K. Zackula

Associate Vice President and
Associate General Counsel
Office of General Counsel