OMB APPROVAL
OMB Number: 3235-0045 Estimated average burden hours per response............38

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2015 - * 036
Amendment No. (req. for Amendments *) 2

Filing by Financial Industry Regulatory Authority

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * ☐ Amendment * ☑ Withdrawal ☐

Section 19(b)(2) * ☑ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

19b-4(f)(1) 19b-4(f)(4)
19b-4(f)(2) 19b-4(f)(5)
19b-4(f)(3) 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document

Exhibit 3 Sent As Paper Document

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Adam Last Name * Arkel
Title * Associate General Counsel
E-mail * adam.arkel@finra.org
Telephone * (202) 728-6961 Fax (202) 728-8264

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 03/21/2016

By Philip Shaikun

(Name *)

(Title *)

Vice President and Associate General Counsel

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Philip Shaikun, Philip.Shaikun@Finra.org

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information * Add Remove View	The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.
Exhibit 1 - Notice of Proposed Rule Change * Add Remove View	The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)
Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies * Add Remove View	The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)
Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications Add Remove View Exhibit Sent As Paper Document ☐	Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.
Exhibit 3 - Form, Report, or Questionnaire Add Remove View Exhibit Sent As Paper Document ☐	Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.
Exhibit 4 - Marked Copies Add Remove View	The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.
Exhibit 5 - Proposed Rule Text Add Remove View	The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.
Partial Amendment Add Remove View	If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

On October 6, 2015, Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission (the "Commission" or "SEC") proposed rule change SR-FINRA-2015-036 (the "original filing," "proposal," or "proposed rule change"), pursuant to which FINRA proposed to amend FINRA Rule 4210 (Margin Requirements) to establish margin requirements for (1) To Be Announced ("TBA") transactions, inclusive of adjustable rate mortgage ("ARM") transactions; (2) Specified Pool Transactions; and (3) transactions in Collateralized Mortgage Obligations ("CMOs"), issued in conformity with a program of an agency or Government-Sponsored Enterprise ("GSE"), with forward settlement dates, as defined more fully in the original filing (collectively, "Covered Agency Transactions," also referred to, for purposes of the original filing, Partial Amendment No. 1 and this Partial Amendment No. 2, as the "TBA market"). The Commission published the proposed rule change for public comment in the Federal Register on October 20, 2015[1] and received 109 comment letters in response to the proposed rule change, including 54 form letter comments and 55 individual letter comments.

On January 13, 2016, FINRA filed Partial Amendment No. 1 to the proposed rule change to (1) respond to the comments the Commission received on the Federal Register publication; (2) add to the proposed rule language, in response to comments, proposed paragraph (e)(2)(H)(ii)a.2.; and (3) propose that the rule change become effective 18 months from the date the proposed rule change is approved by the Commission, except that the risk limit determination requirements as set forth in paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H) of Rule 4210 and proposed Supplementary Material .05 would become effective six months from the date the proposed rule change is approved by the Commission.[2] On January 21, 2016, the Commission published in the Federal Register a notice and order to solicit comments on Partial Amendment No. 1 from interested persons and to institute proceedings pursuant to Section 19(b)(2)(B) of the Securities Exchange Act of 1934 ("SEA") to determine whether to approve or disapprove the proposed rule change, as modified by Partial Amendment No. 1.[3] The Commission received 23

1 Securities Exchange Act Release No. 76148 (October 14, 2015), 80 FR 63603 (October 20, 2015) (Notice of Filing of Proposed Rule Change; File No. SR-FINRA-2015-036).

2 See Partial Amendment No. 1 to SR-FINRA-2015-036, available at: <www.finra.org>.

3 Securities Exchange Act Release No. 76908 (January 14, 2016), 81 FR 3532 (January 21, 2016) (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; File No. SR-FINRA-2036-036) ("Order Instituting Proceedings").

comments in response to the Order Instituting Proceedings.[4]

As discussed more fully below, FINRA is filing this Partial Amendment No. 2 to respond to the comments the Commission received on the Order Instituting Proceedings and to propose, in response to comments, revisions to proposed paragraph (e)(2)(H)(ii)a.2. as set forth in Partial Amendment No. 1. Not in response to comment, FINRA is also proposing a conforming formatting revision to proposed paragraph (e)(2)(H)(ii)a.1. of the rule.

With this Partial Amendment No. 2, FINRA is including (1) Exhibit 2 (see below); (2) Exhibit 4 (see below), which reflects changes to the text of the proposed rule change pursuant to this Partial Amendment No. 2, marked to show additions to the text as proposed in the original filing and Partial Amendment No. 1; and (3) Exhibit 5 (see below), which reflects the changes to the current rule text that are proposed in the original filing and Partial Amendment No. 1, as amended by this Partial Amendment No. 2.

A. Multifamily and Project Loan Securities

As set forth more fully in the original filing, the margin requirements set forth in the proposed rule change would apply to "Covered Agency Transactions." To recap, "Covered Agency Transactions" means:

- TBA transactions, as defined in FINRA Rule 6710(u),[5] inclusive of ARM transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;[6]

---

4 A list of written comments is attached with this Partial Amendment No. 2 as Exhibit 2. Unless noted otherwise, all references to commenters in this Partial Amendment No. 2 are to the commenters as listed in Exhibit 2.

5 FINRA Rule 6710(u) defines "TBA" to mean a transaction in an Agency Pass-Through Mortgage-Backed Security ("MBS") or a Small Business Administration ("SBA")-Backed Asset-Backed Security ("ABS") where the parties agree that the seller will deliver to the buyer a pool or pools of a specified face amount and meeting certain other criteria but the specific pool or pools to be delivered at settlement is not specified at the Time of Execution, and includes TBA transactions for good delivery and TBA transactions not for good delivery. Agency Pass-Through MBS and SBA-Backed ABS are defined under FINRA Rule 6710(v) and FINRA Rule 6710(bb), respectively. The term "Time of Execution" is defined under FINRA Rule 6710(d).

6 See proposed FINRA Rule 4210(e)(2)(H)(i)c.1. in Exhibit 5 in this Partial Amendment No. 2.

- Specified Pool Transactions, as defined in FINRA Rule 6710(x),[7] for which the difference between the trade date and contractual settlement date is greater than one business day;[8] and

- CMOs, as defined in FINRA Rule 6710(dd),[9] issued in conformity with a program of an agency, as defined in FINRA Rule 6710(k),[10] or a GSE, as defined in FINRA Rule 6710(n),[11] for which the difference between the trade date and contractual settlement date is greater than three business days.[12]

---

7 FINRA Rule 6710(x) defines Specified Pool Transaction to mean a transaction in an Agency Pass-Through MBS or an SBA-Backed ABS requiring the delivery at settlement of a pool or pools that is identified by a unique pool identification number at the Time of Execution.

8 See proposed FINRA Rule 4210(e)(2)(H)(i)c.2. in Exhibit 5 in this Partial Amendment No. 2.

9 FINRA Rule 6710(dd) defines CMO to mean a type of Securitized Product backed by Agency Pass-Through MBS, mortgage loans, certificates backed by project loans or construction loans, other types of MBS or assets derivative of MBS, structured in multiple classes or tranches with each class or tranche entitled to receive distributions of principal or interest according to the requirements adopted for the specific class or tranche, and includes a real estate mortgage investment conduit ("REMIC").

10 FINRA Rule 6710(k) defines "agency" to mean a United States executive agency as defined in 5 U.S.C. 105 that is authorized to issue debt directly or through a related entity, such as a government corporation, or to guarantee the repayment of principal or interest of a debt security issued by another entity. The term excludes the U.S. Department of the Treasury in the exercise of its authority to issue U.S. Treasury Securities as defined under FINRA Rule 6710(p). Under 5 U.S.C. 105, the term "executive agency" is defined to mean an "Executive department, a Government corporation, and an independent establishment."

11 FINRA Rule 6710(n) defines GSE to have the meaning set forth in 2 U.S.C. 622(8). Under 2 U.S.C. 622(8), a GSE is defined, in part, to mean a corporate entity created by a law of the United States that has a Federal charter authorized by law, is privately owned, is under the direction of a board of directors, a majority of which is elected by private owners, and, among other things, is a financial institution with power to make loans or loan guarantees for limited purposes such as to provide credit for specific borrowers or one sector and raise funds by borrowing (which does not carry the full faith and credit of the Federal Government) or to guarantee the debt of others in unlimited amounts.

12 See proposed FINRA Rule 4210(e)(2)(H)(i)c.3. in Exhibit 5 in this Partial Amendment No. 2.

FINRA noted that the scope of "Covered Agency Transactions" is intended to be congruent with the scope of products addressed by the Treasury Market Practices Group ("TMPG") best practices and related TMPG updates and includes within its scope multifamily housing and project loan program securities such as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, and Ginnie Mae Construction Loan or Project Loan Certificates (collectively, for purposes of Partial Amendment No. 1 and this Partial Amendment No. 2, "multifamily and project loan securities").[13] In response to comment on the original filing, in Partial Amendment No. 1 FINRA proposed to add to FINRA Rule 4210 new paragraph (e)(2)(H)(ii)a.2. to provide that a member may elect not to apply the margin requirements of paragraph (e)(2)(H) of the rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided that: (i) such securities are issued in conformity with a program of an agency, as defined in FINRA Rule 6710(k),[14] or a GSE, as defined in FINRA Rule 6710(n),[15] and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade; and (ii) the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b. of Rule 4210.[16]

Commenters expressed support for the proposed exception for multifamily and project loan securities as set forth in proposed paragraph (e)(2)(H)(ii)a.2. in Partial Amendment No. 1.[17] Several commenters[18] asked that FINRA provide guidance to ensure that the risk limit determinations as proposed do not disrupt existing practices or arrangements between mortgage bankers and member firms, are not inconsistently or arbitrarily applied, or are not otherwise interpreted as requiring member firms to impose margin requirements with respect to transactions in the specified products, and called for care in the implementation of the requirement. Forest City asked FINRA to state that there are no conditions at this time that would require margining with respect to such transactions. Forest City and W&D said that FINRA should engage in various forms of communication or outreach to clarify the rule. MBA and Lancaster suggested that FINRA should clarify the intent of the proposed exception by changing "a member may elect not to apply the margin requirements" to "a member is not required to apply the

13 See 80 FR 63603, 63605.

14 See note 10 supra.

15 See note 11 supra.

16 See Exhibit 5 in this Partial Amendment No. 2. Proposed Rule 4210(e)(2)(H)(ii)b. sets forth the proposed rule's requirements as to written risk limits.

17 See CBRE, Forest City, Gershman, Lancaster, M&T Realty, MBA, NorthMarq, and W&D.

18 See CBRE, Forest City, Gershman, Lancaster, MBA, and W&D.

margin requirements." Forest City, Gershman, Lancaster and MBA expressed concern that, because of changes in nomenclature or other future action by the agencies or GSEs, some securities that have the characteristics of multifamily and project loan securities may not be documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, and may thereby inadvertently not be included within the proposed exception. These commenters proffered language so that the scope of the proposed exception would include other multifamily and project loan securities with "substantially similar" characteristics issued in conformity with a program or an agency or GSE.

CHF and Prudential Mortgage opposed the modified rule language in Partial Amendment No. 1 on grounds that the rule should not permit members discretion to impose margin requirements as to multifamily and project loan securities and that such securities should be fully exempted from the proposed rule's application. CHF said that FINRA should confirm that good faith deposits provide sufficient protection to broker-dealers involved in multifamily and project loan securities transactions, that FINRA did not do analysis of good faith deposits, that giving broker-dealers discretion to impose margin in such transactions protects the broker-dealer but not other parties to the trade, and that in the presence of margin lenders in multifamily projects will not be able to structure their mortgage costs confidently. Prudential Mortgage said that multifamily and project loan securities should be fully exempted from the proposed rule because such securities do not present systemic risk. Prudential Mortgage said that there are significant protections in place to insulate purchasers of such securities from credit and counterparty risk, that under the proposed rule margin would depend upon a broker-dealer's risk limit determination, that there would be no objective standard for when margin would be required, and that FINRA offered no clear rationale for including multifamily and project loan securities in any margining regime. Prudential Financial proffered language to fully exempt multifamily and project loan securities from the rule's application and suggested that additional language be added to enable broker-dealers and sellers of multifamily and project loan securities to agree contractually on appropriate margin and to count good faith deposits toward margin.

In response, FINRA is sensitive to commenters' concerns that the proposed rule not disrupt business activity. FINRA stated in Partial Amendment No. 1 that FINRA is not proposing at this time to require that members apply the proposed margin requirements[19] to multifamily and project loan securities, subject to the conditions as specified in proposed paragraph (e)(2)(H)(ii)a.2. of Rule 4210. In the interest of further clarity, FINRA proposes in this Partial Amendment No. 2 to revise the phrase "a member

[19] As FINRA noted in Partial Amendment No. 1, the "proposed margin requirements" refers to the margin requirements as to Covered Agency Transactions as set forth in the original filing, as amended by Partial Amendment No. 1 and this Partial Amendment No. 2. Products or transactions that are outside the scope of Covered Agency Transactions are otherwise subject to the requirements of FINRA Rule 4210, as applicable.

may elect not to apply the margin requirements . . ." in paragraph (e)(2)(H)(ii)a.2. to read "a member is not required to apply the margin requirements . . ."[20] However, while the rule is not intended to require margin as to transactions in multifamily and project loan securities, neither is it intended to prevent members from imposing margin. As FINRA stated in Partial Amendment No. 1, the proposal imposes on members the requirement to make and enforce risk limits as to counterparties in multifamily and project loan securities to help ensure that members are properly monitoring their risk. The rule presumes that risk limits will be a tool that members may employ to exercise sound discretion as to the management of their business. Members need, and under FINRA rules have, discretion to impose margin over and above the requirements under the rules.[21] Though it is possible that members' application of the risk limit requirements may lead to different determinations among members as to multifamily and project loan securities, FINRA notes that members and their counterparties have been transacting in these products for a considerable time and they are well understood to the industry. FINRA will consider further guidance as needed.

FINRA takes note of the concern that, owing to changes in nomenclature or other future action by the agencies or GSEs, some securities that have the characteristics of multifamily and project loan securities may not be documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, and may thereby inadvertently fall outside the scope of the exception proposed under paragraph (e)(2)(H)(ii)a.2. In response, in this Partial Amendment No. 2, FINRA proposes to revise proposed paragraph (e)(2)(H)(ii)a.2.A. to add the phrase "or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory Notice or similar communication." As such, proposed paragraph (e)(2)(H)(ii)a.2.A. as revised would read: ". . . such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade, or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory

---

20 See proposed FINRA Rule (e)(2)(H)(ii)a.2. in Exhibit 4 in this Partial Amendment No. 2.

21 Note that proposed Supplementary Material .05(a)(4) provides that, for purposes of paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of the rule, a member "shall consider whether the margin required pursuant to this Rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements." See Exhibit 5 in this Partial Amendment No. 2.

Notice or similar communication . . ."[22] FINRA believes that the revised language should help promote clarity in the rule's application by ensuring that FINRA has the ability to efficiently include within the scope of the proposed exception, by Regulatory Notice or similar communication, any multifamily and project loan securities, consistent with the rule's intent, that may otherwise inadvertently be omitted.

In response to CHF, Prudential Mortgage and Prudential Financial, FINRA believes that a complete exemption for multifamily and project loan securities, not only with respect to the margin requirements but also the obligation of members to make and enforce risk limits, would not serve the interests of sound regulation. As already noted above and in Partial Amendment No. 1, the rule's risk limit provisions are designed as an appropriately tailored requirement to ensure that members are properly managing their risk. It would undercut the core purposes of the rule to create classes of products within the Covered Agency Transactions category where such monitoring is not required. FINRA does not believe that a separate analysis of good faith deposits is necessary given that, as more fully set forth in Partial Amendment No. 1, FINRA took note of the provision of good faith deposits by the borrower to the lender, among other characteristics of multifamily and project loan securities, in considering the exception set forth in the proposed rule. Nor does FINRA propose to introduce into the rule language providing for negotiation of margin or for recognition of good faith deposits. FINRA does not object to parties engaging in negotiation, provided the margin requirements as set forth under the rule are met. FINRA does not believe it is necessary to separately set forth a rationale for regulation of multifamily and project loan securities for purposes of this Partial Amendment No. 2 given that, in the original filing, FINRA set forth in full the rationale for regulating Covered Agency Transactions and, in Partial Amendment No. 1, FINRA specifically addressed its proposed approach to multifamily and project loan securities.

B. Impact and Costs of the Proposal (Other Than With Respect to Multifamily and Project Loan Securities)

Commenters expressed concerns regarding the proposed rule's potential impact on the market and the costs of implementing the requirements.[23] ACLI said that the comment period has been inadequate and that FINRA did not quantify the proposal's burdens on all broker-dealers and market participants. ACLI said that FINRA's economic impact statement in the proposed rule change was deficient. SIFMA said FINRA should consider the comprehensive costs and burdens of the proposal vis-à-vis the cost of alternatives recommended by SIFMA. SIFMA said its members have observed the shifting of TBA market business to non-FINRA members, who have a

---

22 See proposed FINRA Rule (e)(2)(H)(ii)a.2.A. in Exhibit 4 in this Partial Amendment No. 2.

23 See ACLI, AII, BDA, Coastal, Senator Cotton, JW Korth, SIFMA, and Vining Sparks.

significant competitive advantage over FINRA-regulated broker-dealers. SIFMA said that the proposal would result in a reduction in the number of investors willing to invest in TBA market products, and that it would be willing to work with FINRA to supply market or economic information within the access of its members. AII said that the costs of the proposal would be considerable, that implementation work would be extensive in executing or renegotiating Master Securities Forward Transaction Agreements ("MSFTAs"), and that such requirements as maintenance margin and position liquidation would impose additional costs. JW Korth said the proposal would have an inequitable impact on competition between small dealers and large dealers, that many small dealers would exit the TBA market rather than implement the rule, that large firms might not be willing to deal with small firms, and that liquidity for small firms would be negatively affected. Senator Cotton said that many firms that pose no systemic risk potential and do only a moderate amount of mortgage business may choose to exit the marketplace rather than comply with the rule, which would further harm liquidity in the U.S. fixed income market, with possible adverse effects on the U.S. mortgage market, and that the proposal would require small-to-medium sized dealers to execute margin agreements with all their mortgage counterparties. Senator Cotton said that large investment managers would be unlikely to agree to execute margin agreements with an unlimited number of counterparties. Similarly, BDA said that the proposal would exacerbate a concentration of activity in the largest active firms and that the rule would impose burdens on investment managers, who would enter into margin agreements only with the largest dealer counterparties, thereby negatively impacting smaller firms. Coastal said that as a result of the proposal only FINRA members would be required to impose margin requirements and that non-FINRA member banks that currently are following the TMPG best practices may choose not to do so. Coastal said that smaller members would exit the market rather than implement the required margin. Similarly, Vining Sparks said large firms that already follow the TMPG best practices already have margining mechanisms in place but that smaller firms would be disproportionately affected by the proposal because more TBA market transactions will migrate to non-FINRA member banks. Vining Sparks said the proposal would lead to fewer competitors and higher costs for consumers.

BDA and Vining Sparks proffered estimates as to the cost of implementing the proposal. BDA said the proposal would require members of all sizes, regardless of how active they are in the market, to hire new personnel to comply with the rule. BDA said that hiring three new employees to staff a new margin department would cost an estimated $150,000 per employee per year, that third party vendor technology could cost $625,000 in licensing fees in the first year, and that a competing vendor solution would cost as much as $875,000 over the first two years of use. Vining Sparks said that buying or licensing a system to comply with the rule would cost over $100,000, that there would be costs for development resources, and that cost for implementation could run to $250,000 or more. Vining Sparks said that third party pricing would be between $150,000 and $400,000 per year depending on the vendor, that two or maybe three employees would be needed, and that this could cost an additional $200,000 per year. Vining Sparks said the ongoing cost of the proposal would be in the $300,000 to $400,000 range.

In response, FINRA addressed the commenters' concerns in the original filing and in Partial Amendment No. 1. In the original filing, FINRA set forth an extensive analysis of the proposal's potential impact.[24] FINRA addressed, among other things, the proposal's potential impact on mortgage bankers,[25] broker-dealers, including smaller firms,[26] and retail customers and consumers, and presented quantitative analysis of trade and account data.[27] As discussed in the original filing, and again in response to comment in Partial Amendment No. 1, FINRA noted that there will likely be direct and indirect costs associated with the rule change, and that firms will be impacted.[28] FINRA considered and analyzed alternatives.[29] FINRA also set forth the need for the rule change, including the need to manage the risk to members extending credit and to help maintain a properly functioning retail mortgage market even in stressed market conditions.[30] As such, FINRA has met its burden to analyze the rule change's potential impact and to establish the need for the rule change. FINRA welcomes SIFMA's offer to supply information. However, FINRA notes that comment on the proposed rule change has been solicited on three occasions: first in response to Regulatory Notice 14-02;[31] second in response to the original filing; and third in response to the Order Instituting Proceedings. In three rounds of comment, with a total of 107 individual letter comments,[32] and an additional 54 form letters, a handful of commenters have provided in the public record specific, quantified estimates as to the potential cost of implementing the proposed rule change.[33] FINRA notes SIFMA's and ACLI's concerns as to quantitative analysis. However, FINRA further notes that a key purpose of the comment process is to supply

24 See 80 FR 63603, 63611 through 63615.

25 See 80 FR 63603, 63611.

26 See 80 FR 63603, 63612 through 63613.

27 See 80 FR 63603, 63611 through 63614.

28 See 80 FR 63603, 63611.

29 See 80 FR 63603, 63614 through 63615.

30 See 80 FR 63603, 63604, 63611, 63613.

31 See Regulatory Notice 14-02 (January 2014) (FINRA Requests Comment on Proposed Amendments to FINRA Rule 4210 for Transactions in the TBA Market).

32 FINRA received 29 comments in response to Regulatory Notice 14-02. As discussed above, the SEC received 55 individual letter comments in response to the original filing, and 23 individual letter comments in response to the Order Instituting Proceedings.

33 See note 90 at 80 FR 63603, 63613; see also BDA and Vining Sparks, as discussed above.

the public record with specific information for regulators to consider in the development of rulemaking. FINRA notes that it is of little assistance to the comment process to state in a comment letter that the pertinent information is available, and then not provide such information in the letter for public review.

In response to BDA and Vining Sparks, FINRA has engaged in ongoing discussions with various market participants and providers to understand the potential regulatory costs of compliance with the proposed rule. Similar to the original filing,[34] FINRA believes the commenters' estimates fall toward the higher end of the cost range for building, upgrading, maintaining, licensing or outsourcing the necessary systems and hiring of necessary staff. FINRA understands that estimates will vary depending on the size and business model of a firm and the extent of its current and anticipated involvement in TBA market transactions.

As a result of these ongoing discussions, FINRA understands that some firms have been transacting in the TBA market for years and margining has been a common practice due to the TMPG best practices or prudent counterparty risk management practices at these firms. These firms already have the technology and staffing in place for collateral management in their repo, swap and OTC derivatives transactions and would only have to build into their current systems the exceptions provided for under the proposed rule.[35] Costs associated with such enhancements or additions to the current systems should vary based on the scalability and flexibility of such systems. For instance, sources at one firm estimated that it required approximately 60 hours of programming time, at a cost of approximately $5,000, to build systems to track margin obligations consistent with the TMPG best practices. The same firm did not plan to hire additional staff to track margin obligations pursuant to the proposed rule. However, another firm estimated that its total annual costs to comply with the proposed requirements could run from $60,000 to $100,000, including both staffing and technology costs.

FINRA understands that there are various technology solutions and service providers for firms that have relatively less engagement in TBA market transactions, and therefore would need more affordable and flexible products. One service provider to firms noted that costs could vary widely depending on the level of service that a firm purchases and estimated that it would be typical of its firm customers to pay, in addition to a basic set up fee of $1,000, approximately $1,000 to $2,500 per month for the use of a web-based system to manage margin requirements pursuant to the proposed rule. While this service is purely designed to compute margin obligations, the provider estimated that a firm seeking more robust levels of service, which would include a more sophisticated tracking system of counterparty exposures and margin obligations for all of its asset types, including margining for TBA market transactions, could spend higher amounts on

---

[34] See 80 FR 63603, 63613.

[35] See, e.g., the "cash account" exceptions and the de minimis transfer amount as discussed in Sections F and G, respectively, of this Partial Amendment No.2.

software to manage such systems, and that installation and preparation would require approximately one week.

FINRA understands that firms with significant trading activity in the TBA market may already have the systems built, or the flexibility to enhance current systems, to comply with the proposed rule, whereas firms with relatively little activity in this market, whose business models and trading activity would qualify them for the exceptions as set forth in the proposed rule,[36] can find affordable solutions. One firm that does a significant business in the TBA market said that it has already built systems to reflect the TMPG best practices and estimated it would need to spend $50,000 to $100,000 on additional software and technology costs to reflect the additional requirements under the proposed rule change, and would need to hire two to three additional staff at approximately $70,000 to $100,000 per person to track margin obligations. FINRA acknowledges that there may also be firms whose customers' trading activity in the TBA market may qualify them for the de minimis transfer exception on some days only, and may be at a level that would require a more sophisticated margin tracking system on other days. Implementation costs may be higher for such firms, as they may have to determine the size of their activity in TBA market transactions and hence scale their systems accordingly, or they may choose to implement more rigorous solutions in order to avoid non-compliance. FINRA recognizes that some firms may seek to update existing master agreements or to renegotiate master agreement terms upon the adoption of the proposed rule. Any related costs to these activities will likely vary with the amount of the activity conducted by a member, the number of counterparties and the amount of the activity conducted by its counterparties.

C. Scope of the Proposal

ACLI said that the scope of Covered Agency Transactions should be amended to cover only forward settling TBA market transactions whose settlement dates extend beyond the relevant industry-published standard settlement dates. BDA said the rule should exclude Specified Pool Transactions, ARMs and CMOs on grounds similar to the proposed exception for multifamily and project loan securities. Vining Sparks said that, on similar grounds, SBA securities should be excluded from the proposal. Coastal said that the proposed rule should not include Specified Pool Transactions and CMOs, that these products do not pose systemic risks, that FINRA should analyze the specified pool and CMO markets, and that FINRA should address why the proposed rule requirements are not being imposed on member banks of the Federal Reserve System.

In response, in the original filing,[37] and again in response to comment in Partial Amendment No. 1, FINRA addressed the commenters' concerns as to the scope of Covered Agency Transactions as defined in the rule. FINRA notes that Specified Pool Transactions, ARMs, CMOs and the SBA securities as specified under the rule all share

---

36 See note 35 supra.

37 See 80 FR 63603, 63605, 63615 through 63616.

the type of extended settlement risk that the proposed rule change aims to address, for which reason they are included within the scope of Covered Agency Transactions. FINRA's reasoning and approach as to multifamily and project loan securities, as set forth in Partial Amendment No. 1 and this Partial Amendment No. 2, are designed with a view to those products in the totality of their characteristics, which is distinct from the products raised by the commenters. For the reasons set forth in the original filing and Partial Amendment No. 1, FINRA does not propose to revise the definition of Covered Agency Transactions.

D. Creation of Account Types

SIFMA said that the proposed rule change effectively mandates that members create an account type that would be specific to TBA market transactions. SIFMA said that is because the proposed rule imposes distinct requirements from other types of products, and that the requirements are being imposed at the same time as industry is preparing to expend significant resources to migrate to "T+2" settlement.

In response, FINRA notes that the proposed rule does not mandate the creation of account types dedicated to TBA market transactions. Based on discussions with various market participants and service providers, FINRA believes it is well within the operational and technological ability of firms to appropriately handle margining of TBA market transactions. As discussed above, FINRA has acknowledged that implementation of the proposal will involve costs. FINRA is aware that the proposed rule change is not the only regulatory development that could affect firms. At the same time, however, FINRA notes that regulation, like industry, continually evolves with new and ongoing initiatives. FINRA is aware that the T+2 migration will involve demands on member resources, yet FINRA also notes that the T+2 initiative, with all its attendant resource demands, has been sought and advocated by industry.[38] It would not be consistent with FINRA's mission of investor protection and market integrity, nor could it ever be feasible, for FINRA to refrain from rulemaking until the completion of every initiative by other regulators and by industry that could impose burdens or demands on resources.

E. Maintenance Margin

As set forth more fully in the original filing and again in Partial Amendment No. 1, non-exempt accounts[39] would be required to post two percent maintenance margin plus

---

38 See Letter from Paul Schott Stevens, President & CEO, Investment Company Institute, and Kenneth E. Bentsen, Jr., President and CEO, SIFMA, to Mary Jo White, Chair, U.S. Securities and Exchange Commission, June 18, 2015.

39 The term "exempt account" is defined under FINRA Rule 4210(a)(13). Broadly, an exempt account means a FINRA member, non-FINRA member registered broker-dealer, account that is a "designated account" under FINRA Rule 4210(a)(4) (specifically, a bank as defined under SEA Section 3(a)(6), a savings association as defined under Section 3(b) of the Federal Deposit Insurance Act,

any net mark to market loss on their Covered Agency Transactions.[40] AII, Matrix, SIFMA and SIFMA AMG expressed opposition to the proposed maintenance margin requirement. The commenters said that the proposal is inconsistent with the TMPG best practices, that the requirement would unfairly affect market participants that do not pose systemic risk, and that the requirement places FINRA members at a competitive disadvantage. Matrix said that if FINRA imposes the maintenance margin requirement, the requirement should be revised so as to be easier to implement. Matrix said that FINRA should consider a tiered approach for trades that are under a defined gross dollar amount and that clarification as to the requirement's application to Delivery Versus Payment ("DVP") accounts is needed.

In response, in the original filing,[41] and again in Partial Amendment No. 1, FINRA addressed the commenters' concerns as to the proposed maintenance margin requirement. FINRA noted that maintenance margin is a mainstay of margin regimes in the securities industry, and as such the need to appropriately track transactions should be well understood to market participants. FINRA is sensitive to commenters' concerns as to the potential impact of the requirement on members and their non-exempt customer accounts. For this reason, as set forth more fully in the original filing, and as discussed further below, FINRA revised the proposal to include an exception tailored to customers engaging in non-margined, cash account business. As such, in response to Matrix, FINRA does not believe it is necessary or appropriate to further tier the requirement. With respect to the application of the requirement to DVP accounts, FINRA will consider specific interpretive issues as they are raised and will consider guidance as needed. FINRA does not propose to revise the maintenance margin requirement.

---

the deposits of which are insured by the Federal Deposit Insurance Corporation, an insurance company as defined under Section 2(a)(17) of the Investment Company Act, an investment company registered with the Commission under the Investment Company Act, a state or political subdivision thereof, or a pension plan or profit sharing plan subject to the Employee Retirement Income Security Act or of an agency of the United States or of a state or political subdivision thereof), and any person that has a net worth of at least $45 million and financial assets of at least $40 million for purposes of paragraphs (e)(2)(F) and (e)(2)(G) of the rule, as set forth under paragraph (a)(13)(B)(i) of Rule 4210, and meets specified conditions as set forth under paragraph (a)(13)(B)(ii). As set forth more fully in the original filing, FINRA is proposing a conforming revision to paragraph (a)(13)(B)(i) so that the phrase "for purposes of paragraphs (e)(2)(F) and (e)(2)(G)" would read "for purposes of paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H)." See 80 FR 63603, 63606; see also proposed FINRA Rule 4210(a)(13)(B)(i) in Exhibit 5.

[40] See 80 FR 63603, 63607 through 63608.

[41] See 80 FR 63603, 63616 through 63617.

F. "Cash Account" Exceptions

As set forth more fully in the original filing, the proposed margin requirements would not apply to any counterparty that has gross open positions[42] in Covered Agency Transactions with the member amounting to $2.5 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a DVP basis or for cash. Similarly, a non-exempt account would be excepted from the rule's proposed two percent maintenance margin requirement if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and the customer regularly settles its Covered Agency Transactions on a DVP basis or for cash. The rule uses parallel language with respect to both of these exceptions to provide that they are not available to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in FINRA Rule 6710(z),[43] or "round robin"[44] trades, or that uses other financing techniques for its Covered Agency Transactions. FINRA noted that these exceptions are intended to address the concerns of smaller customers engaging in non-margined, cash account business.[45]

SIFMA said that is was not clear how FINRA had arrived at the $2.5 million exception and suggested that the amount should be raised to $10 million. SIFMA AMG said members should be allowed to negotiate the amount. SIFMA said that it had concerns about how to interpret the term "regularly settles" and that it was skeptical that members would find it worthwhile to build systems to comply with the cash account

---

42 Paragraph (e)(2)(H)(i)e. of the rule defines "gross open position" to mean, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty's contracts with the member and which the counterparty intends to deliver. See Exhibit 5 in this Partial Amendment No. 2.

43 FINRA Rule 6710(z) defines "dollar roll" to mean a simultaneous sale and purchase of an Agency Pass-Through MBS for different settlement dates, where the initial seller agrees to take delivery, upon settlement of the re-purchase transaction, of the same or substantially similar securities.

44 Paragraph (e)(2)(H)(i)i. defines "round robin" trade to mean any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer. See Exhibit 5 in this Partial Amendment No. 2.

45 See 80 FR 63603, 63605. For convenience, the $2.5 million and maintenance margin exceptions are referred to as the "cash account" exceptions for purposes of this Partial Amendment No. 2.

exceptions, thereby making it likely members will not offer them to counterparties. SIFMA said it would take the term “regularly settles” to mean “a substantial portion of the time.”

In response, FINRA addressed commenters’ concerns in Partial Amendment No. 1 and does not propose to modify the cash account exceptions as proposed in the original filing. As noted above, the cash account exceptions are designed to help address the concerns of smaller participants in the market. If members believe that it is too onerous to offer these exceptions to their customers, they are not obligated under the rule to do so. Commenters on the original filing asked for guidance as to the term “regularly settles,”[46] and in response FINRA noted that, as worded, the term “regularly settles” is designed to provide scope for flexibility on members’ part as to how they implement the exceptions. FINRA said that it expects that members are in a position to make reasonable judgments as to the observed pattern and course of dealing in their customers’ behavior by virtue of their interactions with their customers. However, FINRA does not agree with SIFMA’s interpretation that “regularly” is to be equated with “substantial portion of the time.” FINRA views the term “regularly” as conveying the prevailing or dominant pattern and course of the customer’s behavior. FINRA stated in Partial Amendment No. 1 that, in ascertaining the customer’s regular pattern, a member may use the customer’s history of transactions with the member, as well as any other relevant information of which the member is aware, and, further, that members should be able to rely on the reasonable representations of their customers where necessary for purposes of the requirement. As FINRA noted in Partial Amendment No. 1, FINRA will consider issuing further guidance as needed.

With respect to SIFMA’s suggestion to increase the $2.5 million amount to $10 million, FINRA noted in the original filing, and again in Partial Amendment No. 1, that the amount is meant to be appropriately tailored to smaller accounts that are less likely to pose systemic risk.[47] FINRA noted that increasing the amount would undermine the rule’s purpose. FINRA does not object if parties attempt to negotiate thresholds, provided the thresholds are not greater than prescribed by the rule. In that regard, FINRA noted that permitting parties to negotiate higher thresholds by separate agreement, whether entered into before the rule takes effect or afterwards, would only serve to cut against the rule’s objectives.

G. De Minimis Transfer

As set forth more fully in the original filing, the proposed rule sets forth, for a single counterparty, a $250,000 de minimis transfer amount up to which margin need not be collected or charged to net capital, as specified by the rule.[48] SIFMA AMG said

---

[46] See Partial Amendment No. 1.

[47] See 80 FR 63603, 63616.

[48] See 80 FR 63603, 63608.

members should be allowed to negotiate the de minimis transfer amount with their counterparties. ACLI and SIFMA said the de minimis transfer amount should be $500,000, which SIFMA suggested would align with requirements for swaps. BDA said the amount should be $1 million. SIFMA expressed concern that members would end up needing to monitor the $250,000 amount even though it would benefit few if any customers.

In response, FINRA addressed commenters' concerns in Partial Amendment No. 1 and does not propose to modify the de minimis transfer provisions as proposed in the original filing. FINRA noted in the original filing that the de minimis transfer amount is meant to be appropriately tailored to help prevent smaller members from being subject to competitive disadvantage.[49] As discussed above, FINRA noted that increasing the amount would undermine the rule's purpose. Again, as noted above, FINRA does not object if parties attempt to negotiate de minimis transfer thresholds, provided the thresholds are not greater than prescribed by the rule.

H. Timing of Margin Collection and Position Liquidation

As set forth more fully in the original filing, the proposed rule provides that, with respect to exempt accounts, if a mark to market loss, or, with respect to non-exempt accounts, a deficiency, is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member must deduct the amount of the mark to market loss or deficiency from net capital as provided in SEA Rule 15c3-1. Further, unless FINRA has specifically granted the member additional time, the member is required to liquidate positions if, with respect to exempt accounts, a mark to market loss is not satisfied within five business days, or, with respect to non-exempt accounts, a deficiency is not satisfied within such period.[50] SIFMA AMG said the required timing of margin collection should be replaced with a three-day transfer period. SIFMA said that the proposed margin collection timing is operationally impractical for TBA market transactions, that the requirement would create technological difficulties because it deviates from ordinary operational practices, that FINRA's Regulatory Extension System would not be suitable for requirements that are impractical to begin with, and that the portfolio margin provisions under FINRA Rule 4210(g)(10)(B) are not a comparable analogy for purposes of margin collection timing. SIFMA said the Regulatory Extension System is intended to grant waivers from ordinarily applicable requirements arising under unusual circumstances. SIFMA asked whether the Regulatory Extension System would accommodate permanent waivers for certain firms and customers and whether there would be any limit to the number of waivers a firm could obtain either generally or for a particular customer. Matrix suggested the proposed requirement is not consistent with FINRA Rule 4210. With respect to the proposed liquidation requirement, ACLI, Matrix, SIFMA, and SIFMA

[49] See 80 FR 63603, 63608, 63617.

[50] See 80 FR 63603, 63607 through 63608.

AMG said the requirement should be omitted, that five business days is too short, and that parties should be permitted to negotiate the time frames under the rule.

In response, FINRA addressed the commenters' concerns in Partial Amendment No. 1. FINRA does not propose to modify the proposed requirements. As FINRA noted in Partial Amendment No. 1, 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,[51] the Regulatory Extension System for this purpose, which is well understood to industry participants. In response to SIFMA, FINRA notes that the Regulatory Extension System does not grant waivers from requirements under Rule 4210, whether permanent or temporary. Additional time is granted, pursuant to the rule, for meeting specified obligations and, consistent with longstanding practice under the rule, FINRA may limit or restrict the extensions granted for a firm or customer. FINRA will consider additional guidance as needed. FINRA referenced the portfolio margin rules in Partial Amendment No. 1 to illustrate that, with respect to the timing of margin collection, the proposed language "by the close of business on the next business day after the business day" on which the market to market loss or deficiency arises is consistent with existing language under Rule 4210 and is well understood by members.[52] With respect to the liquidation requirement, FINRA noted that the five business day period should provide sufficient time for members to resolve issues. Further, as FINRA noted in the original filing and in Partial Amendment No. 1, FINRA believes the specified period is appropriate in view of the potential counterparty risk in the TBA market.[53]

I. Two-Way (Bilateral) Margin

ACLI, SIFMA AMG and Sutherland said that the proposed rule change should require bilateral, two-way margining. In response, FINRA addressed this in the original filing and in Partial Amendment No. 1. FINRA noted its support for the use of two-way margining as a means of managing risk.[54] However, FINRA noted that it does not propose to address such a requirement at this time as part of the proposed rule change.

J. Third Party Custodians

Sutherland said the proposed rule change should provide for a member's counterparty to have the right to segregate any margin posted with a FINRA member with an independent third party custodian. In response, FINRA addressed this concern in

---

[51] See, e.g., Regulatory Notice 10-28 (June 2010) (Extension of Time Requests); Regulatory Notice 14-13 (March 2014) (Regulatory Extension System Update).

[52] See FINRA Rule 4210(g)(10)(B).

[53] See 80 FR 63603, 63619.

[54] See 80 FR 63603, 63619 through 63620.

Partial Amendment No. 1. FINRA noted that, with respect to third party custodial arrangements, FINRA believes these are best addressed in separate rulemaking or guidance, as appropriate. FINRA welcomes further discussion of these issues, but does not propose to address them as part of the proposed rule change.

K. SEA Rule 15c3-3

SIFMA said that the proposed rule change does not address the treatment of customer margin for purposes of the segregation requirements under SEA Rule 15c3-3. SIFMA suggested that the SEC should issue an interpretation to correspond with the proposed rule change. FINRA notes the suggestion is outside the scope of the proposed rule change and welcomes further discussion of this issue.

L. Sovereign Entities

As set forth more fully in the original filing, the proposed rule provides that, with respect to Covered Agency Transactions with any counterparty that is a federal banking agency, as defined in 12 U.S.C. 1813(z),[55] central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of the proposed rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.[56] SIFMA AMG said that sovereign wealth funds should be excepted from the proposed margin requirements. In response, FINRA addressed this concern in the original filing[57] and again in Partial Amendment No. 1. FINRA believes that to include sovereign wealth funds within the parameters of the proposed exception would create perverse incentives for regulatory arbitrage.

M. Exempt Account Treatment

SIFMA and SIFMA AMG said that the exempt account definition should be expanded as part of the rule change to include foreign equivalent entities and collective investment trusts. Matrix suggested the exempt account definition should be updated. In response, in Partial Amendment No. 1, FINRA noted that, other than for purposes of one conforming revision, as set forth in the original filing,[58] the proposed rule change is not

---

55 12 U.S.C. 1813(z) defines federal banking agency to mean the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, or the Federal Deposit Insurance Corporation.

56 See 80 FR 63603, 63606.

57 See 80 FR 63603, 63619.

58 See 80 FR 63603, 63606.

intended to revisit the definition of exempt accounts for the broader purposes of Rule 4210. FINRA believes that this issue is properly addressed by separate rulemaking or guidance, as appropriate.

N. Third Party Providers

Matrix suggested that FINRA should make clear that members required to collect margin under the proposed rule change may utilize third party service providers and products. FINRA addressed this concern in Partial Amendment No. 1. FINRA believes that third party service providers are permissible provided the member complies with all applicable rules and guidance, including, among other things, the member's obligations under FINRA Rule 3110 and as described in Notice to Members 05-48 (July 2005) (Outsourcing).

O. Netting Services

Brean Capital said that the proposal should not be implemented until the Mortgage-Backed Securities Division ("MBSD") of Fixed Income Clearing Corporation enlarges the universe of transactions for which it provides netting services and that, until MBSD does so, the proposal would unfairly discriminate against mid-sized firms. In Partial Amendment No. 1, FINRA noted that coordination with MBSD is outside the scope of the proposed rule change. FINRA welcomes further discussion of this issue.

P. Scope of FINRA's Authority

BDA, Coastal and Senator Cotton said that the proposed rule change is not consistent with the intent of SEA Section 7 and questioned FINRA's authority to proceed with the proposed rule change. The commenters cited the Senate Report[59] in connection with Congress's adoption of the Secondary Mortgage Market Enhancement Act of 1984[60] ("SMMEA") in support of this view. In response, FINRA notes that SEA Section 7 sets forth the parameters of the margin setting authority of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") and does not bar action by FINRA. The SMMEA does not address FINRA's authority as the statute was designed, among other things, to level the competitive playing field between issuers of private-label MBS (defined under the SMMEA as "mortgage related securities" under SEA Section 3(a)(41)) vis-à-vis agency and GSE MBS.[61] As FINRA noted in the original filing[62] and

---

59 See S. Rep. No. 293, 98th Cong., 2d Session (1983).

60 Pub. L. No. 98-440, 98 Stat. 1689 (1984).

61 See David Abelman, The Secondary Mortgage Market Enhancement Act, 14 Real Estate Law Journal 136, 138 (1985) (noting that Congress sought to encourage private issuance by eliminating competitive advantages in favor of government issued securities); Edward L. Pittman, Economic and Regulatory Developments Affecting Mortgage Related Securities, 64 Notre Dame Law Review 497, 537

Partial Amendment No. 1, the proposed rule change is consistent with the provisions of SEA Section 15A(b)(6).

Q. Implementation Period

In Partial Amendment No. 1, FINRA stated that it believes that a phased implementation should be appropriate. FINRA proposed that the risk limit determination requirements as set forth in paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H) of Rule 4210 and proposed Supplementary Material .05 of the rule become effective six months from the date the proposed rule change is approved by the Commission. FINRA proposed that the remainder of the proposed rule change become effective 18 months from the date the proposed rule change is approved by the Commission. ACLI said 18 months represents a reasonable time frame. AII said that the implementation time frame as proposed in Partial Amendment No. 1 is sufficiently reasonable. SIFMA AMG said that compliance with the proposed requirements would be difficult to complete and that it would prefer a time frame of 24 months, but that its members could aim to complete their implementation work within 18 months. SIFMA said that an implementation period of at least 18 months would be appropriate and that two years would be more practical. SIFMA said that the proposed six-month period for implementation of the risk limit requirements would effectively require broker-dealers to complete their diligence as to their customers within six months even though the proposed rule does not take effect in full until a year after that six-month period. Vining Sparks said that it would need 18 to 24 months to complete implementation of the proposed requirements and suggested that FINRA should not have a separate time frame for the risk limit requirements.

In response, FINRA does not propose to change the implementation periods as set forth in Partial Amendment No. 1. FINRA does not believe it would serve the public interest to extend implementation of the rule beyond 18 months once approved by the Commission. FINRA believes the six-month time frame for the risk limit requirements is appropriate given that members engaging in business in the TBA market should undertake the effort to understand their counterparties.

R. Other

Not in response to comment, FINRA has made a conforming formatting revision to proposed paragraph (e)(2)(H)(ii)a.1. of the rule so that the phrase "paragraph (e)(2)(H)(ii)b; and . . ." reads "paragraph (e)(2)(H)(ii)b.; and . . ."[63]

(noting that the SMMEA amendments to SEA Section 7 were intended to facilitate the creation of mortgage related securities).

[62] See 80 FR 63603, 63609. SEA Section 15A(b)(6) requires, among other things, that FINRA rules must 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.

[63] See Exhibit 4 in this Partial Amendment No. 2.

EXHIBIT 2

List of Written Comments

1. James M. Cain, Sutherland Asbill & Brennan LLP ("Sutherland") (February 11, 2016) (on behalf of the Federal Home Loan Banks)

2. Timothy W. Cameron, Esq. and Laura Martin, Securities Industry and Financial Markets Association, Asset Management Group ("SIFMA AMG") (February 11, 2016)

3. U.S. Senator Tom Cotton, ("Senator Cotton") (February 11, 2016)

4. Tari Flannery, M&T Realty Capital Corporation ("M&T Realty") (February 9, 2016)

5. John R. Gidman, Association of Institutional INVESTORS ("AII") (February 11, 2016)

6. Christopher B. Killian, Securities Industry and Financial Markets Association ("SIFMA") (February 11, 2016)

7. Robert T. Kirkwood, Lancaster Pollard Holdings, LLC ("Lancaster") (February 11, 2016)

8. Blake Lanford, Walker & Dunlop ("W&D") (February 11, 2016)

9. Rodrigo Lopez, CMB, NorthMarq Capital Financial, LLC ("NorthMarq") (February 10, 2016)

10. Tony Love, Forest City Capital Corporation ("Forest City") (February 11, 2016)

11. Holly MacDonald-Korth, JW Korth & Company ("JW Korth") (February 9, 2016)

12. Matrix Applications ("Matrix") (February 9, 2016)

13. Mike McRoberts, Prudential Mortgage Capital Company ("Prudential Mortgage") (February 11, 2016)

14. Chris Melton, Coastal Securities ("Coastal") (February 10, 2016)

15. Mike Nicholas, Bond Dealers of America ("BDA") (February 11, 2016)

16. Roderick D. Owens, Committee on Healthcare Financing ("CHF") (February 11, 2016)

17. Allen Riggs, Vining Sparks IBG, LP ("Vining Sparks") (February 11, 2016)

18. Bruce Sandweiss, Gershman Mortgage ("Gershman") (February 11, 2016)

19. Lauren Eardensohn Sarper, Prudential Financial, Inc. (“Prudential Financial”) (March 1, 2016)

20. David H. Stevens, CMB, Mortgage Bankers Association (“MBA”) (February 11, 2016)

21. Robert Tirschwell, Brean Capital, LLC (“Brean Capital”) (February 17, 2016)

22. Steve Wendel, CBRE Inc. (“CBRE”) (February 11, 2016)

23. Carl B. Wilkerson, American Council of Life Insurers (“ACLI”) (February 11, 2016)

EXHIBIT 4

Exhibit 4 shows the changes proposed in this Partial Amendment No. 2, with the proposed changes in the original filing and Partial Amendment No. 1 shown as if adopted. Proposed new language in this Partial Amendment No. 2 is underlined; proposed deletions in this Partial Amendment No. 2 are in brackets.

* * * * *

4000. FINANCIAL AND OPERATIONAL RULES

* * * * *

4210. Margin Requirements

(a) through (d) No Change.

(e) Exceptions to Rule

The foregoing requirements of this Rule are subject to the following exceptions:

(1) No Change.

(2) Exempted Securities, Non-equity Securities and Baskets

(A) through (G) No Change.

(H) Covered Agency Transactions

(i) No Change.

(ii) Margin Requirements for Covered Agency Transactions

a. All Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, shall be subject to the provisions of paragraph (e)(2)(H) of this Rule, except:

1. with respect to Covered Agency Transactions with any counterparty that is a Federal

banking agency, as defined in 12 U.S.C. 1813(z), central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.; and

2. a member [may elect] is not required to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided:

A. such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project

Loan Certificates, as commonly known to the trade, or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory Notice or similar communication; and

B. No Change.

b. through g. No Change.

(I) No Change.

* * * * *

(f) through (h) No Change.

• • • Supplementary Material: ---------------

.01 through .05 No Change.

* * * * *

EXHIBIT 5

Exhibit 5 shows the text of the proposed rule change, as amended by this Partial Amendment No. 2. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

4000. FINANCIAL AND OPERATIONAL RULES

* * * * *

4210. Margin Requirements

(a) Definitions

For purposes of this Rule, the following terms shall have the meanings specified below:

(1) through (12) No Change.

(13) The term “exempt account” means:

(A) No Change.

(B) any person that:

(i) has a net worth of at least $45 million and financial assets of at least $40 million for purposes of paragraphs (e)(2)(F), [and] (e)(2)(G)[,] and (e)(2)(H), and

(ii) No Change.

(14) through (16) No Change.

(b) through (d) No Change.

(e) Exceptions to Rule

The foregoing requirements of this Rule are subject to the following exceptions:

(1) No Change.

(2) Exempted Securities, Non-equity Securities and Baskets

(A) through (E) No Change.

(F) Transactions with Exempt Accounts Involving Certain "Good Faith" Securities

Other than for Covered Agency Transactions as defined in paragraph (e)(2)(H) of this Rule, [O]on any "long" or "short" position resulting from a transaction involving exempted securities, mortgage related securities, or major foreign sovereign debt securities made for or with an "exempt account," no margin need be required and any marked to the market loss on such position need not be collected. However, the amount of any uncollected marked to the market loss shall be deducted in computing the member's net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)([H]I) [below] of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

(G) Transactions With Exempt Accounts Involving Highly Rated Foreign Sovereign Debt Securities and Investment Grade Debt Securities

On any “long” or “short” position resulting from a transaction made for or with an “exempt account” (other than a position subject to paragraph (e)(2)(F) or (e)(2)(H) of this Rule), the margin to be maintained on highly rated foreign sovereign debt and investment grade debt securities shall be, in lieu of any greater requirements imposed under this Rule, (i) 0.5 percent of current market value in the case of highly rated foreign sovereign debt securities, and (ii) 3 percent of current market value in the case of all other investment grade debt securities. The member need not collect any such margin, provided the amount equal to the margin required shall be deducted in computing the member’s net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)([H]I) [below] of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(G) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member’s written risk policies and procedures.

(H) Covered Agency Transactions

(i) Definitions

For purposes of paragraph (e)(2)(H) of this Rule:

a. The term “bilateral transaction” means a Covered Agency Transaction that is not cleared through a registered clearing agency as defined in paragraph (f)(2)(A)(xxviii) of this Rule.

b. The term “counterparty” means any person that enters into a Covered Agency Transaction with a member and includes a “customer” as defined in paragraph (a)(3) of this Rule.

c. The term “Covered Agency Transaction” means:

1. To Be Announced (“TBA”) transactions, as defined in Rule 6710(u), inclusive of adjustable rate mortgage (“ARM”) transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;

2. Specified Pool Transactions, as defined in Rule 6710(x), for which the difference between the trade date and contractual settlement date is greater than one business day; and

3. Transactions in Collateralized Mortgage Obligations (“CMOs”), as defined in Rule 6710(dd), issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), for which the difference between the trade date and

contractual settlement date is greater than three business days.

d. The term "deficiency" means the amount of any required but uncollected maintenance margin and any required but uncollected mark to market loss.

e. The term "gross open position" means, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty's contracts with the member and which the counterparty intends to deliver.

f. The term "maintenance margin" means margin equal to 2 percent of the contract value of the net "long" or net "short" position, by CUSIP, with the counterparty.

g. The term "mark to market loss" means the counterparty's loss resulting from marking a Covered Agency Transaction to the market.

h. The term "mortgage banker" means an entity, however organized, that engages in the business of providing real estate financing collateralized by liens on such real estate.

i. The term "round robin" trade means any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer.

j. The term "standby" means contracts that are put options that trade OTC, as defined in paragraph (f)(2)(A)(xxvii) of this Rule, with initial and final confirmation procedures similar to those on forward transactions.

(ii) Margin Requirements for Covered Agency Transactions

a. All Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, shall be subject to the provisions of paragraph (e)(2)(H) of this Rule, except:

1. with respect to Covered Agency Transactions with any counterparty that is a Federal banking agency, as defined in 12 U.S.C. 1813(z), central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified

in paragraph (e)(2)(H) of this Rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.; and

2. a member is not required to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided:

A. such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade, or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory Notice or similar communication; and

B. the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.

b. A member that engages in Covered Agency Transactions with any counterparty shall make a determination in writing of a risk limit for each such counterparty that the member shall enforce. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

c. The margin requirements specified in paragraph (e)(2)(H) of this Rule shall not apply to:

1. Covered Agency Transactions that are cleared through a registered clearing agency, as defined in paragraph (f)(2)(A)(xxviii) of this Rule, and are subject to the margin requirements of that clearing agency; and

2. any counterparty that has gross open positions in Covered Agency Transactions with the member amounting to $2.5 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a Delivery Versus Payment ("DVP") basis or for "cash"; provided, however, that such exception from the margin requirements shall not apply to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in Rule 6710(z), or "round robin" trades, or that uses other financing techniques for its Covered Agency Transactions.

d. Transactions with Exempt Accounts: On any net "long" or net "short" position, by CUSIP, resulting from bilateral transactions with a counterparty that is an "exempt account" no maintenance margin shall be required. However, such transactions shall be marked to the market daily and the member shall collect any net mark to market loss, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of this Rule. If the mark to market loss is not satisfied by the close of business on the next business day after the business day on which the mark to market loss arises, the member shall be required to deduct the amount of the mark to market loss from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss is satisfied. If such mark to market loss is not satisfied within five business days from the date the loss was created, the member shall promptly liquidate positions to satisfy the mark to market loss, unless FINRA has specifically granted the member additional time. Members may treat mortgage bankers that use Covered Agency Transactions to hedge their pipeline of mortgage commitments as exempt accounts for purposes of paragraph (e)(2)(H) of this Rule.

e. Transactions with Non-Exempt Accounts: On any net "long" or net "short" position, by CUSIP, resulting from bilateral transactions with a counterparty that is not an "exempt account," maintenance margin, plus any net mark to market loss on such transactions, shall be required margin, and the member shall collect the deficiency, as defined in paragraph (e)(2)(H)(i)d. of this Rule, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of this Rule. If the deficiency is not satisfied by the close of business on the next business day after the business day on which the deficiency arises, the member shall be required to deduct the amount of the deficiency from net capital as provided in SEA Rule 15c3-1 until such time the deficiency is satisfied. If such deficiency is not satisfied within five business days from the date the deficiency was created, the member shall promptly liquidate positions to satisfy the deficiency, unless FINRA has specifically granted the member additional time. No maintenance margin is required if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and the customer regularly settles its Covered Agency Transactions on a DVP basis or for “cash”; provided, however, that such exception from the required maintenance margin shall not apply to a non-exempt account that, in its transactions with the member, engages in dollar rolls, as defined in Rule 6710(z), or “round robin” trades, or that uses other financing techniques for its Covered Agency Transactions.

f. Any aforementioned deficiency, as set forth in paragraph (e)(2)(H)(ii)e. of this Rule, or mark to market losses, as set forth in paragraph (e)(2)(H)(ii)d. of this Rule, with a single counterparty shall not give rise to any margin requirement, and as such need not be collected or charged to net capital, if the aggregate of such amounts with such counterparty does not exceed $250,000 (“the de minimis transfer amount”). The full amount of the sum of the required maintenance margin and any mark to market loss must be collected when such sum exceeds the de minimis transfer amount.

g. Unrealized profits in one Covered Agency Transaction position may offset losses from other Covered Agency Transaction positions in the same counterparty’s account and the amount of net unrealized profits may be used to reduce margin requirements. With respect to standbys, only profits (in-the-money amounts), if any, on “long” standbys shall be recognized.

([H]I) Limits on Net Capital Deductions [for Exempt Accounts]

[(i) Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) and (e)(2)(G) which shall be made available to FINRA upon request.]

([ii]i) In the event that the net capital deductions taken by a member as a result of deficiencies or marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) of this Rule (exclusive of the percentage requirements established thereunder), plus any mark to market loss as set forth under paragraph (e)(2)(H)(ii)d. of this Rule and any deficiency as set forth under paragraph (e)(2)(H)(ii)e. of this Rule, and inclusive of all amounts excepted from margin requirements as set forth under paragraph (e)(2)(H)(ii)c.2. of this Rule or any de minimis transfer amount as set forth under paragraph (e)(2)(H)(ii)f. of this Rule, exceed:

a. [on] for any one account or group of commonly controlled accounts, 5 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), or

b. [on] for all accounts combined, 25 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), and,

c. such excess as calculated in paragraphs (e)(2)(I)(i)a. or b. of this Rule continues to exist[s] on the fifth business day after it was incurred,

the member shall give prompt written notice to FINRA and shall not enter into any new transaction(s) subject to the provisions of paragraphs (e)(2)(F), [or] (e)(2)(G) or (e)(2)(H) of this Rule that would result in an increase in the amount of such excess under, as applicable, [subparagraph (ii)] paragraph (e)(2)(I)(i) of this Rule.

* * * * *

(f) Other Provisions

(1) through (5) No Change.

(6) Time Within Which Margin or "Mark to Market" Must Be Obtained

The amount of margin or "mark to market" required by any provision of this Rule, other than that required under paragraph (e)(2)(H) of this Rule, shall be obtained as promptly as possible and in any event within 15 business days from the date such deficiency occurred, unless FINRA has specifically granted the member additional time.

(7) through (10) No Change.

(g) through (h) No Change.

• • • Supplementary Material: ---------------

.01 No Change.

.02 Monitoring Procedures. For purposes of paragraph (e)(2)(H)(ii)d. of this Rule, members shall adopt written procedures to monitor the mortgage banker's pipeline of mortgage loan commitments to assess whether the Covered Agency Transactions are being used for hedging purposes.

.03 Mark to Market Loss/Deficiency. For purposes of paragraph (e)(2)(H) of this Rule, to the extent a mark to market loss or deficiency is cured by subsequent market movements prior to the time the margin call must be met, the margin call need not be met and the position need not be liquidated; provided, however, if the mark to market loss or deficiency is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member shall be required to deduct the amount of the mark to market loss or deficiency from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss or deficiency is satisfied.

.04 Determination of Exempt Account. For purposes of paragraph (e)(2)(H) of this Rule, the determination of whether an account qualifies as an exempt account shall be made based upon the beneficial ownership of the account. Sub-accounts managed by an investment adviser, where the beneficial owner is other than the investment adviser, shall be margined individually.

.05 Risk Limit Determination.

(a) For purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of this Rule:

(1) If a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level, except with respect to any account or group of commonly controlled accounts whose assets managed by that investment adviser constitute more than 10 percent of the investment adviser's regulatory assets under management as reported on the investment adviser's most recent Form ADV;

(2) Members of limited size and resources that do not have a credit risk officer or credit risk committee may designate an appropriately registered principal to make the risk limit determinations;

(3) The member may base the risk limit determination on consideration of all products involved in the member's business with the counterparty, provided the member makes a daily record of the counterparty's risk limit usage; and

(4) A member shall consider whether the margin required pursuant to this Rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements.

* * * * *