FINRA

Financial Industry Regulatory Authority

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Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File No. SR-FINRA-2016-027 – Response to Comments

Dear Mr. Fields,

This letter responds to comments received by the Securities and Exchange Commission ("SEC") to the above-referenced rule filing, which relates to a proposed rule change to expand the Trade Reporting and Compliance Engine ("TRACE") reporting rules to include most secondary market transactions in U.S. Treasury Securities.[1]

Background

FINRA is proposing to amend the TRACE rules to require FINRA members to report transactions in U.S. Treasury Securities, as that term is defined in the TRACE rules. Under the Proposal, members would be required to report to TRACE most secondary market transactions in Treasury bills, notes, and bonds[2] on a same-day or next-day basis, depending upon when the transaction was executed.[3] The proposed reporting requirement would apply to secondary market transactions in U.S. Treasury Securities as well as transactions executed on a "when-issued" basis before the security is auctioned, but would not apply to purchases by firms in an auction. As a general matter, the Proposal leverages the existing TRACE format and requirements; however, FINRA proposed adopting one new trade indicator for when-issued transactions and two new trade modifiers for certain types of transactions that are part

1 See Securities Exchange Act Release No. 78359 (July 19, 2016), 81 FR 48465 (July 25, 2016) (SR-FINRA-2016-027) ("Proposal").

2 The proposed reporting requirement would not apply to savings bonds. See id. at 48466.

3 In general, transactions executed before 5:00 p.m. Eastern Time must be reported on the same day as the transaction while transactions after that time may be reported on a next-day basis. See id. at 48467.

of a series of transactions and may be priced away from the market. Under the Proposal, FINRA would not disseminate any transaction-level information on U.S. Treasury Security transactions, and FINRA noted that, at this time, it is not proposing to charge fees (e.g., trade reporting fees, Trading Activity Fee) on such transactions.[4]

The SEC received twelve comment letters on the Proposal.[5] Numerous commenters expressed overall support for the Proposal, including noting that having more comprehensive Treasury market transaction data available to regulators will be beneficial.[6] However, many commenters sought clarification on specific aspects of the Proposal or made suggestions for ways in which the Proposal could be amended. FINRA's responses to the issues raised in the letters are below.

Discussion

Non-FINRA Member Market Participants

Seven commenters noted that the Proposal does not offer a comprehensive solution to the need for official sector access to trading information in the Treasury cash market because not all participants in that market are FINRA members.[7] Several

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4 See Proposal, supra note 1, at 48468-69.

5 See Letters to Brent J. Fields, Secretary, SEC from Mike Nicholas, Chief Executive Officer, Bond Dealers of America, dated August 15, 2016 ("BDA"); Jane Carson, dated August 5, 2016 ("Carson"); Adam C. Cooper, Senior Managing Director and Chief Legal Officer, Citadel LLC, dated August 15, 2016 ("Citadel"); Shane O'Cuinn, Managing Director, Credit Suisse, dated August 15, 2016 ("Credit Suisse"); Marc R. Bryant, Senior Vice President, Fidelity Investments, dated August 15, 2016 ("Fidelity"); David W. Blass, General Counsel, Investment Company Institute, dated August 15, 2016 ("ICI"); John A. McCarthy, General Counsel, KCG Holdings, Inc., dated August 15, 2016 ("KCG"); Robert Toomey, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association, dated August 15, 2016 ("SIFMA"); Douglas Friedman, General Counsel, Tradeweb Markets LLC, dated August 15, 2016 ("Tradeweb"); Letters to Robert W. Errett, Deputy Secretary, SEC from Mary Lou Von Kaenel, Managing Director, Financial Information Forum, dated August 15, 2016 ("FIF"); Manisha Kimmel, Chief Regulatory Officer, Wealth Management, Thomson Reuters, dated August 15, 2016 ("Thomson Reuters"); John Shay, Senior Vice President, Virtu Financial, Inc., dated August 15, 2016 ("Virtu").

6 See BDA at 1; Carson; SIFMA at 1; Credit Suisse at 1; ICI at 1-2; KCG at 2; Tradeweb at 2, 4.

7 See BDA; Credit Suisse at 3; Fidelity at 2-5; KCG at 5; SIFMA at 3; Tradeweb at 2 n.3; Virtu at 2.

commenters suggested that moving forward with the Proposal may be premature without implementation of a similar reporting requirement for non-FINRA member market participants.[8] For example, some commenters suggested that FINRA members could be placed at a competitive disadvantage in the Treasury cash market through the use of regulatory arbitrage by market participants and by the imposition of increased costs on FINRA members that are not imposed on other market participants.[9]

FINRA recognizes that the Proposal will not capture the entire universe of trades and data for the Treasury cash market due to FINRA's jurisdictional limitations. Similarly, FINRA recognizes that the proposed trade reporting rules will impose costs and burdens on its members—costs and burdens that the Proposal will not place on other, non-FINRA member market participants. As discussed below, FINRA offers firms several methods to report to TRACE and would require same-day, rather than real-time, reporting in order to provide cost-effective alternatives to reporting firms. FINRA believes, however, that the Proposal represents a significant and important first step in this process and notes that the U.S. Department of the Treasury, the SEC, the Federal Reserve Bank of New York, and the CFTC have stated that they are assessing effective means to ensure the collection of data regarding Treasury cash securities market transactions is comprehensive and includes information from institutions that are not FINRA members.[10]

Dissemination

As noted in the Proposal, FINRA is not proposing to disseminate transaction information on U.S. Treasury Securities at this time; therefore, the Proposal excludes these transactions from the dissemination requirement. Eight commenters addressed the issue of whether FINRA should disseminate U.S. Treasury Security transaction information.[11] Six commenters supported the approach set forth in the Proposal not to disseminate transaction information.[12] KCG suggested that FINRA amend the

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8 See, e.g., BDA at 1-2; Credit Suisse at 3; Fidelity at 2-5; KCG at 5; SIFMA at 3; Tradeweb at 2 n.3; Virtu at 1-2.

9 See Fidelity at 4.

10 See Joint Press Release, U.S. Department of the Treasury, et. al., Statement Regarding Progress on the Review of the U.S. Treasury Market Structure since the July 2015 Joint Staff Report (August 2, 2016), available at https://www.sec.gov/news/pressrelease/2016-155.html; see also Joint Press Release, U.S. Department of the Treasury, et. al., Statement on Trade Reporting in the U.S. Treasury Market (May 16, 2016), available at https://www.sec.gov/news/pressrelease/2016-90.html.

11 See BDA, Citadel, Credit Suisse, Fidelity, ICI, KCG, SIFMA, Tradeweb.

12 BDA at 1, Credit Suisse at 7; Fidelity at 5; ICI at 2-3; SIFMA at 4-5; Tradeweb at 2-3.

Proposal to include a dissemination component,[13] and Citadel suggested that FINRA require transaction-by-transaction reporting on a more immediate timeframe to more easily accommodate the potentiality that more timely transaction reporting is required in connection with a future decision to disseminate U.S. Treasury Security transaction information.[14]

For the reasons set forth in the Proposal, FINRA is not proposing to disseminate transactions in U.S. Treasury Securities at this time.[15] FINRA believes that careful consideration of the potential benefits of public dissemination as well as the concerns raised by the commenters should be undertaken after a reporting requirement is already in place. Consequently, FINRA is not amending the Proposal to include public dissemination of transaction information regarding U.S. Treasury Securities.

Scope of Securities

Two commenters requested clarification on whether transactions in Treasury Inflation-Protected Securities, commonly referred to as TIPS, must be reported under the Proposal and, if so, how they should be reported.[16] Thomson Reuters requested clarification on whether TIPS are within the scope of the Proposal, and both commenters asked how the factor associated with TIPS should be reported. FIF assumed that the factor for TIPS "will be handled in a similar manner to reporting of securitized products."[17]

The Proposal amends the definitions of "TRACE-Eligible Security" and "U.S. Treasury Security" in Rule 6710 so that secondary market transactions in all marketable Treasury securities, including notes, bills, and bonds (with the exception of

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13 KCG at 3-4.

14 Citadel at 3-6. Citadel states in its letter that "it has been made clear to market participants that any policy decision regarding public reporting would only be taken after implementation of an official sector reporting regime"; however, Citadel's letter in response to the Request for Information published earlier in 2016 demonstrates support for the public dissemination of transaction information in U.S. Treasury Securities. See Letter to David R. Pearl, Office of the Executive Secretary, U.S. Department of Treasury, from Citadel LLC (April 22, 2016), available at https://www.regulations.gov/document?D=TREAS-DO-2015-0013-0045. Because Citadel's comment is focused more specifically on the proposed same-day or next-day reporting requirement, the comment is addressed below.

15 See Proposal, supra note 1, at 48468.

16 See FIF at 2; Thomson Reuters at 2.

17 FIF at 2.

savings bonds), must be reported to TRACE.[18] This requirement would include reportable transactions in TIPS. FINRA clarifies that at this time it is not providing, nor requiring reporting of, factor information in TIPS transactions.

Scope of Transactions

Under the Proposal, secondary market transactions in U.S. Treasury Securities are reportable to TRACE unless they are specifically exempted from the requirement. FINRA proposed to exempt purchases of U.S. Treasury Securities in an auction and to codify FINRA's longstanding exemption for repurchase and reverse repurchase transactions.[19] All other secondary market transactions in U.S. Treasury Securities, including those conducted on a "when-issued" basis before the auction is conducted, are reportable to TRACE.

Credit Suisse and FIF requested guidance on the application of the reporting requirement to reopenings,[20] and Credit Suisse noted that the definition of "when-issued" currently differs across firms and suggested clarification would be appropriate. Credit Suisse stated that some participants treat transactions as "when-issued" up until the night of the auction for the security while other participants treat them as such only until the day before the auction.[21]

The Proposal defines a "When-Issued Transaction" for purposes of the reporting requirement as "a transaction in a U.S. Treasury Security that is executed before the Auction for the security."[22] Under this definition, FINRA believes that any transaction in a U.S. Treasury Security to be sold in an Auction that occurs before the Auction takes place, including transactions the day of the Auction, would be considered a "When-Issued Transaction" for purposes of the reporting rule. For transaction reporting purposes, reopening transactions in a security that is the subject

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18 SIFMA notes in its letter that it "assume[s] that all applicable TRACE rules will apply to in-scope transactions in Treasuries, unless otherwise explicitly exempted." SIFMA at 6. FINRA agrees with SIFMA's statement and notes that, because U.S. Treasury Securities are now included within "TRACE-Eligible Securities," any rule applicable to "TRACE-Eligible Securities" would apply to U.S. Treasury Securities unless specifically exempted.

19 One commenter specifically expressed support for the exemption for repurchase and reverse repurchase transactions. See SIFMA at 5-6.

20 Credit Suisse at 4; FIF at 1.

21 Credit Suisse at 4.

22 An "Auction" is defined as "the bidding process by which the U.S. Department of the Treasury sells marketable securities to the public pursuant to part 356 of Title 31 of the Code of Federal Regulations."

of an Auction, effected prior to that Auction, would also be treated as "When-Issued Transactions."

Transaction Information

Like current TRACE requirements, the Proposal requires any FINRA member that is a "Party to a Transaction" in a U.S. Treasury Security to report the transaction to TRACE; thus, a transaction involving two FINRA members is reported by each member. In addition, the Proposal establishes a same-day reporting requirement for transactions before 5:00 p.m. Eastern Time and permits next-day reporting for transactions after 5:00 p.m. Eastern Time.

Citadel objected to dual reporting and suggested that only one side of a transaction be required to report. Citadel suggested that single-sided reporting could reduce implementation costs and would "allow the methodology to more easily be applied to other market participants as the official sector reporting regime is expanded to include trading activity between non-FINRA member firms."[23]

For the reasons set forth in the Proposal, FINRA continues to believe that a two-sided reporting requirement, like that currently in place for all TRACE transactions, is appropriate for transactions in U.S. Treasury Securities as well. As noted in the Proposal, a reporting structure requiring both sides to report helps to ensure the accuracy of reported transactions because it allows FINRA to compare the information reported by each party to identify discrepancies or potential non-reporting by one party, thereby enhancing the quality of the audit trail.[24] Moreover, altering TRACE requirements to accommodate single-sided reporting would necessitate changes to TRACE's existing infrastructure that could affect all TRACE-reporting firms and significantly reduce the benefits to using the TRACE system for U.S. Treasury Security reporting.[25]

Five letters commented on the timing requirements for transaction reports: two commenters supported the proposed same day or an extended reporting requirement,[26] and three firms suggested more immediate reporting requirements.[27] Credit Suisse suggested that allowing next-day trade reporting for all transactions in U.S. Treasury Securities "may alleviate the reporting challenges posed by the limited TRACE hours."[28] As noted above, Citadel expressed concern that permitting same-day or

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23 Citadel at 3.

24 Proposal, supra note 1, at 48473.

25 Id. at 48472.

26 See Credit Suisse at 6; Tradeweb at 2.

27 See Citadel at 4; KCG at 4; Virtu at 2.

28 Credit Suisse at 6.

next-day reporting would result in some market participants designing operational workflows to support batch reporting that could need to be altered if a shorter reporting timeframe were required in the future.[29] KCG supported real-time reporting in connection with its recommendation that the Proposal be amended to include public dissemination,[30] and Virtu expressed the view that "for surveillance to be effective, the underlying data collection should be both comprehensive and immediate with very few exceptions."[31]

As FINRA noted in the Proposal, the primary reason it is not requiring prompt transaction reporting is that it believes that, because the transaction information is not being disseminated, it is preferable to provide firms with the flexibility to report as appropriate for their current operations (e.g., on a trade-by-trade basis or at the end of the day) rather than to mandate prompt reporting at this time. In addition, FINRA believes that this flexibility may ease the compliance burden on some firms. Firms that wish to report on an immediate basis may do so; however, FINRA does not believe it is necessary at this time to require such reporting for those firms that may find it more cost effective or beneficial to report on an end-of-day basis. As Citadel notes, the timeframe requirements for reporting U.S. Treasury Security transactions could change in the future. While FINRA believes that firms may want to consider such an eventuality when deciding how to design their systems, FINRA is not imposing it as a regulatory obligation at this time. FINRA also disagrees with Virtu's assertion that end-of-day reporting will negatively affect the surveillance of trading in U.S. Treasury Securities.

The Proposal generally applies the existing TRACE reporting requirements to transactions in U.S. Treasury Securities; however, the Proposal includes several new requirements that reflect particular aspects of the Treasury cash market. Specifically, the Proposal requires that firms use a new trade indicator for "when-issued" transactions and also that firms append new trade modifiers, if applicable, to certain transactions that are undertaken as a part of a series of transactions.[32] Finally, the Proposal requires that executions in U.S. Treasury Securities that are electronic be reported to TRACE in the finest increment of time captured by the member's systems (e.g., millisecond, microsecond) but, in any event, at least to the second.[33]

Four commenters suggested that FINRA remove, revise, or delay the proposed requirements regarding the use of trade modifiers until further discussions with the

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29 Citadel at 4.

30 KCG at 4.

31 Virtu at 2.

32 See Proposal, supra note 1, at 48468.

33 Id.

industry were conducted.[34] Credit Suisse, for example, stated its belief that "it may take significant system changes both internally and at the various brokers and venues in order to comply with [the proposed modifiers]" and that "it may be challenging for FINRA members to identify trades within their systems that are part of a series of transactions when executing one specific trade," which "may require building new processes and systems to link trades across trading platforms and possibly desks or even division lines."[35] FIF echoed this view, noting that the proposed modifiers would require firms "to establish linkages across trading platforms and systems that do not exist today" and noted that it would be "helpful to better understand what FINRA hopes to achieve in defining these modifiers, as there may be more straightforward solutions."[36] Similarly, Thomson Reuters and SIFMA suggested further discussion on the proposed modifiers prior to adoption,[37] and SIFMA requested that "the final rule contain a clear and comprehensive list" of the types of transactions and strategies to which the ".S" modifier applies. Conversely, Citadel was supportive of the proposed supplemental modifiers and noted the importance of the ability of the official sector to identify accurately various types of package transactions involving U.S. Treasury Securities.[38] Further, Citadel suggested expanding the information required on transaction reports to capture additional information regarding the number of legs in a series of transactions as well as the types of instruments involved.[39]

As SIFMA noted in its letter, "[t]here are various wholly legitimate trading combinations or strategies that potentially could be executed at prices away from the current market."[40] For this reason, as noted in the Proposal, FINRA proposed two modifiers to "allow FINRA to better understand and evaluate execution prices for specific transactions in U.S. Treasury Securities that may otherwise appear aberrant because they are significantly outside of the price range for that security at that

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34 See Credit Suisse at 5; FIF at 2; SIFMA at 6-8; Thomson Reuters at 2.

35 Credit Suisse at 5.

36 FIF at 2.

37 See SIFMA at 8; Thomson Reuters at 2.

38 Citadel at 2-3.

39 Citadel also recommended requiring firms to report the trading venue (if any) where the transaction was executed and whether the transaction was cleared. See Citadel at 2. As noted in the Proposal, "FINRA believes that, initially, the new fields and modifiers it is proposing are sufficient for surveillance and review of transaction activity; however, FINRA will monitor the information once reporting beings to determine whether additional transaction information may be needed to enhance the audit trail and its surveillance program." Proposal, supra note 1, at 48474.

40 SIFMA at 7.

time."[41] In essence, FINRA is proposing these two modifiers—with an extended implementation timeline—to permit it to more easily identify legitimate transactions that, standing alone, may appear to raise regulatory concerns. FINRA believes these proposed modifiers are necessary for effective and efficient implementation of the Proposal, even if they may result in additional implementation burdens or costs on firms.

While FINRA appreciates the implementation concerns of the commenters, FINRA believes there is sufficient information available for firms regarding how to report certain trades as ".B" or ".S" trades. FINRA believes ".B" trades are well defined in that they relate specifically to a series of trades involving both U.S. Treasury Securities and a futures contract. FINRA intends the ".S" modifier to apply more broadly to a trade report if the transaction being reported is part of a series of transactions that could result in the reported transaction being executed away from the current market.[42] FINRA also agrees with SIFMA regarding the use of the ".S" modifier in that the modifier should apply to a transaction in a particular strategy that meets the ".S" criteria regardless of whether one or more of the transactions in the series is, in fact, off market.[43] Consequently, FINRA is submitting a Partial Amendment No. 1 contemporaneously with this response to clarify that the ".S" modifier can be used under these circumstances. FINRA believes this amendment should reduce some of the compliance burdens for firms in that firms will no longer need to assess whether a particular transaction was, in fact, priced outside of the market at the time of execution.[44] FINRA also believes that permitting end-of-day, rather than requiring more prompt reporting, will ease the compliance burden on firms in implementing the modifiers. In addition, FINRA will work with member firms to better understand their questions and post any necessary trade reporting guidance on the FINRA website (as has been done in connection with other new trade reporting implementations) if the Proposal is approved. However, FINRA does not intend to publish a list of specific transactions and strategies for which the ".S" modifier is required as such a list could never be comprehensive or account for variations that may be appropriate. FINRA believes that the firms themselves are in a superior position to evaluate whether the modifier is applicable to any particular transaction in a series.

Three commenters objected to the proposed Supplementary Material requiring that electronic executions be reported to the level of granularity captured by the

41 Proposal, supra note 1, at 48468.

42 See id.

43 See SIFMA at 7.

44 See SIFMA at 7.

member's system.[45] FIF expressed concern that the requirement would introduce disparate timing in trade reports, result in different requirements for different firms, and "would produce misleading results, and give a false impression of precision and accuracy."[46] Similarly, SIFMA suggested that the proposed requirement "may provide for inconsistent market application, a false sense of precision and may result in unwarranted regulatory inquiries based on imprecise sequencing of events."[47]

As noted in the Proposal, a significant portion of trading activity in the Treasury cash market occurs on electronic platforms that currently capture timestamps in sub-second time increments.[48] FINRA believes that more granular timestamps on execution data can enhance its ability to surveil trading activity, and for this reason, FINRA recently required firms that capture time in milliseconds to report time to the millisecond level when reporting trades in equity securities to a FINRA Trade Reporting Facility or reporting order information to the Order Audit Trail System (OATS).[49] Notably, when adopting these requirements for equity securities, FINRA did not require firms to update their existing systems; it simply required firms to report time at the same level that they captured it. FINRA believes a similar approach is appropriate for transactions in U.S. Treasury Securities that are executed electronically: firms should be able to easily report an execution time in increments finer than a second when they already capture the time to that same level of granularity. Because finer time increments can also enhance FINRA's ability to

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45 Credit Suisse at 5; FIF at 2-3; SIFMA at 9. Although Credit Suisse requested that the time requirement be removed from the proposed rule change, it stated that, if it is not removed, FINRA should "not mandate its members undergo system enhancements to require more granular reporting times." Credit Suisse at 5. FINRA notes that, as stated in the Proposal, the Supplementary Material does not require members to enhance their systems; it merely requires that a member report the time to the same level of granularity its systems currently capture. See Proposal, supra note 1, at 48468. Similarly, FINRA notes that it is not requiring members who have multiple systems, some of which may capture timestamps in finer increments than one second, to update other systems to comply with the finer time increment required under the proposed Supplementary Material. See SIFMA at 9 ("SIFMA therefore requests confirmation that FINRA is not requiring members to update their systems to comply with a finer time increment (i.e., less than one second) in those circumstances.").

46 FIF at 3. See also Credit Suisse at 5 (suggesting that the time requirement "may result in mismatches in trade reporting timing").

47 SIFMA at 9.

48 See Proposal, supra note 1, at 48468.

49 See Regulatory Notice 14-21 (May 2014).

recreate the proper time sequencing of trades and conduct automated surveillance of trading activity, FINRA believes that the requirement is appropriate in this context for the same reasons it adopted the requirement for equity security reporting.

FIF requested confirmation regarding several specific data elements in connection with the Proposal.[50] First, FIF noted that the field for ATS MPID is not included in the list of data elements in the Proposal and that FIF members "prefer to keep the fields aligned with existing requirements." FIF also noted that it assumed the "No Remuneration" flag will be considered a modifier to be consistent with Rule 6730 reporting of other modifiers.[51] Both the ATS MPID field (to be used when an ATS has received a trade reporting exemption pursuant to Rule 6732) and the "No Remuneration" flag apply to all transactions reported to TRACE, as applicable. Consequently, both will apply as applicable to transactions in U.S. Treasury Securities that must be reported to TRACE under the Proposal.

Finally, Credit Suisse requested guidance on the treatment of mark-ups and mark-downs as well as the requirement that firms report commissions as a total dollar amount since, according to the commenter, there is inconsistency across the industry.[52] Credit Suisse also requested clarification regarding the treatment of interdealer broker fees for principal trading as well as platform fees that may be applied to certain client transactions.

Since TRACE implementation in 2002, FINRA has provided guidance, as well as specific rulemaking, in the area of remuneration reporting. For example, interdealer brokers that charge per transaction remuneration are generally required to calculate and include such remuneration when reporting the transaction to TRACE; however, commissions, mark-ups, or mark-downs charged on a monthly or other basis that cannot be assessed on a per transaction basis are not required to be reported.[53] Regarding platforms such as ATSs, FINRA recognizes that multiple fee structures exist; however, firms generally should not include such fees in TRACE reports and should report only bona fide commissions in the commission field.[54] FINRA believes that current remuneration guidance will be helpful for U.S. Treasury Security reporting, and FINRA will continue to provide timely guidance as needed. Although

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50 See FIF at 2.

51 Both the ATS MPID field and the No Remuneration flag became effective on July 18, 2016, the same day FINRA filed the Proposal.

52 Credit Suisse at 4-5.

53 See Regulatory Notice 15-47 (November 2015).

54 See Letter from Sharon K. Zackula, FINRA, to Mustafa Fazel, National Financial Services, LLC, dated July 11, 2003, available at https://www.finra.org/industry/interpretive-letters/july-11-2003-1200am.

FINRA is sensitive to member firm implementation concerns, FINRA believes that remaining consistent with well-established TRACE trade reporting precedent with respect to reporting commissions and mark-ups and mark-downs is appropriate.

Implementation

Several commenters raised questions regarding the implementation of the Proposal if it is approved.

SIFMA and FIF asked whether FINRA would populate TRACE with the appropriate CUSIPs rather than have them registered by market participants.[55] FINRA intends to register the CUSIPs for outstanding U.S. Treasury Securities with TRACE so firms will not be required to do so, and CUSIPs for these securities will be included on FINRA's daily list of reportable securities. On a going-forward basis, FINRA will register CUSIPs for TRACE reporting purposes coincident with the announcement of an auction.

SIFMA and FIF also requested that FINRA clarify whether re-reporting or amending of transaction reports before the end-of-day cut-off would count toward a firm's error statistics or be subject to fees for corrections.[56] As in other FINRA trade reporting system contexts, member firm re-reporting and amending of trades are captured in a firm's error statistics published on the TRACE Report Cards even if the transactions are not considered late. However, as no transaction reporting fees are being charged for U.S. Treasury Security reporting at this time, there will be no fees charged for re-reports or amendments.

As noted in the Proposal, FINRA is not proposing to charge TRACE transaction-level fees on reports for U.S. Treasury Securities, and FINRA has proposed to exempt these transactions from the Trading Activity Fee; however, FINRA notes that it may reassess this exclusion from fees in the future.[57] BDA and Thomson Reuters supported the exclusion of U.S. Treasury Security transactions from applicable fee provisions; however, both commenters expressed concern with FINRA's reserving the right to revisit the issue in the future.[58] As noted in the

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55 FIF at 2; SIFMA at 9.

56 FIF at 2; SIFMA at 9. FINRA is also confirming that there is no prohibition against real-time or earlier submission of transaction reports by firms; the Proposal establishes outside time limits but does not impose limitations on how soon a firm may submit a transaction report. See FIF at 2.

57 Proposal, supra note 1, at 48468-69.

58 BDA at 2; Thomson Reuters at 2. Thomson Reuters suggested that "FINRA should not assess any additional fees with respect to the expansion into Treasuries for a minimum of five years."

Proposal, FINRA will incur costs to expand the TRACE system and to enhance its existing examination and surveillance efforts to monitor U.S. Treasury Security transactions if the Proposal is approved by the SEC. Consequently, FINRA is unable to commit to continuing to exclude these transactions from the applicable fee provisions for a specified time period; however, any fees on these transactions would be subject to a separate proposed rule change filed with the SEC.

Thomson Reuters noted that allowing TRACE reporting for U.S. Treasury Securities via an existing line – either the CA (corporate/agency) or SP (securitized product) line should be used.[59] Thomson Reuters suggested that permitting this connectivity would eliminate both initial and ongoing costs while requiring new network connectivity would be a significantly larger build.

TRACE generally allows a firm reporting through FIX or CTCI to use the same connection line to submit transactions to the system. Some firms currently use the same line to report transactions in both TRACE products currently available: CA (Corporate/Agency) and SP (Securitized Product). Due to the protocol itself, firms using the FIX protocol to report transactions may use the same connection line but are required to obtain separate ports for each TRACE product. Because reporting in U.S. Treasury Securities will be implemented as a new product, firms reporting via FIX will have to obtain a new port; however, this is not the case for firms reporting using the CTCI protocol. FINRA notes that a firm's need to obtain and operate separate lines is dependent on the firm's activity in each product and the firm's desired balance between costs and latency/performance.

Finally, several commenters provided their views on the time and effort necessary to implement transaction reporting for U.S. Treasury Securities.[60] In general, the commenters believed that one year would be an appropriate time to complete the processes necessary to begin reporting U.S. Treasury Security transactions, noting in particular that these securities tend to be traded across multiple areas of many firms, not all of which currently report to TRACE.[61] Some commenters noted that the implementation could be more difficult and costly for those firms that are not currently reporting to TRACE or that would have to expand existing TRACE reporting systems to other business segments or trading desks.[62] Commenters also supported a staggered implementation period for reporting and for the requirement to

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[59] See Thomson Reuters at 2.

[60] See Credit Suisse at 6; FIF at 3; SIFMA at 10; Thomson Reuters at 1-2; Tradeweb at 3.

[61] See Credit Suisse at 6; SIFMA at 10.

[62] Credit Suisse at 6; FIF at 4.

include trade modifiers,[63] and several commenters stressed the important role played by technical specifications in ensuring successful implementation.[64]

As a general matter, FINRA understands the implementation challenges firms may face if the Proposal is adopted and will, as always, consider these challenges when establishing an appropriate implementation date. FINRA also recognizes the importance of timely and detailed technical specifications in ensuring firms are able to effectively implement new reporting requirements. As noted in the Proposal, FINRA will announce the implementation date in a Regulatory Notice if the Proposal is approved by the SEC and is preparing to publish technical specifications concurrent with the Commission's approval of the proposed rule change.

In order to provide cost-effective alternatives to reporting firms, FINRA offers several methods for firms to meet their reporting obligations appropriate to the firms' trading activity and existing infrastructure. For firms with relatively low trading activity, FINRA has built an infrastructure to permit secure web-browser for manual reporting. For firms with higher levels of trading activity, where manual reporting may be challenging and not cost-effective, FINRA offers direct connectivity (via either CTCI or FIX protocols). In addition, FINRA's experience with TRACE reporting demonstrates that many firms rely upon clearing firms that generally offer transaction reporting as a service to their correspondents, and several service bureaus offer TRACE reporting as a service to subscribers to their trade order management systems. FINRA understands that many firms currently active in trading U.S. Treasury Securities currently rely on clearing firms or subscription trade order management systems and would be able to use those service providers to meet the proposed reporting obligation.

As noted in the Proposal, a majority of FINRA members that are also government securities dealers or government securities brokers currently are registered for, and report to, TRACE.[65] The FINRA members that are also government securities dealers or government securities brokers but currently are not registered for TRACE, or are registered for TRACE but have not reported a trade between June 2015 and May 2016, are predominantly small firms, with 80% having fewer than 25 registered representatives. In FINRA's general experience, firms with limited trading volumes would generally use the web browser to report, limiting the cost of

63 See Credit Suisse at 6; FIF at 2; SIFMA at 10. FINRA notes that, in response to a question by SIFMA, firms will not be required to amend previously submitted transactions to include modifiers after the implementation date. See SIFMA at 11.

64 FIF at 3; SIFMA at 10; Thomson Reuters at 1-2.

65 See Proposal, supra note 1, at 48471.

reporting.[66] Firms with higher trading volumes generally have a greater degree of automation and utilization of trade order management systems, many of which offer TRACE reporting as a service to their subscribers.

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FINRA believes that the foregoing responds to the material issues raised by the commenters to the Proposal. If you have any questions, please contact the undersigned at (202) 728-6927 or brant.brown@finra.org.

Sincerely,

Brant Brown

Brant Brown

66 The cost of the secure web browser for reporting purposes is $20 per month. See Rule 7730(a)(1).