

organization consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2009-067 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2009-067. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of the filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-

2009-067 and should be submitted on or before November 18, 2009.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>11</sup>

**Elizabeth M. Murphy,**  
*Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-60860; File No. SR-FINRA-2009-065]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change To Define Asset-Backed Securities, Mortgage-Backed Securities, and Other Similar Securities as TRACE-Eligible Securities and Require the Reporting of Transactions in Such Securities to TRACE

October 21, 2009.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 1, 2009, the Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend the FINRA Rule 6700 Series (except for Rule 6740) and FINRA Rule 7730 to designate asset-backed securities, mortgage-backed securities and other similar securities (collectively defined hereinafter as "Asset-Backed Securities") as Trade Reporting and Compliance Engine ("TRACE") TRACE-Eligible Securities, and establish reporting, fee and other requirements relating to such securities as follows:

(1) In Rule 6710, to amend the defined term: (A) "TRACE-Eligible Security" to include Asset-Backed Securities; and make certain technical changes in Rule 6710(a); (B) "Reportable TRACE Transaction" to include specific requirements regarding certain Asset-

Backed Securities in Rule 6710(c); (C) "Agency Debt Security" to incorporate proposed defined terms in Rule 6710(l); and (D) "TRACE System Hours" to transfer the defined term from Rule 6730(a) to Rule 6710(bb);

(2) In Rule 6710, to add the defined terms, "Sponsor," "Issuing Entity," "TBA," "Agency Pass-Through Mortgage-Backed Security," "Factor," "Specified Pool Transaction," "Stipulation Transaction," "Dollar Roll," and "Remaining Principal Balance," as, respectively, new paragraphs (s) through (aa);

(3) In Rule 6730, to provide for reporting of Asset-Backed Securities transactions;

(4) In Rule 6750, to provide that information on a transaction in a TRACE-Eligible Security that is an Asset-Backed Security will not be disseminated;

(5) In Rule 6760, to require a member that is a Sponsor or an Issuing Entity of an Asset-Backed Security to provide notice as required under the Rule, and to modify the notification requirements to accept a mortgage pool number in certain circumstances;

(6) In Rule 7730, to establish transaction reporting fees for Asset-Backed Securities that are TRACE-Eligible Securities at the same rates in effect for corporate bonds; for certain Asset-Backed Securities, to identify size (volume) for determining a trade reporting fee, and to provide that for purposes of Rule 7730(b), a transaction in an Agency Pass-Through Mortgage-Backed Security is not a List or Fixed Offering Price Transaction or a Takedown Transaction; and

(7) In the Rule 6700 Series, except for Rule 6740, and Rule 7730 to incorporate certain technical, administrative and clarifying changes.

The text of the proposed rule change is available on FINRA's Web site at <http://www.finra.org>, at the principal office of FINRA and at the Commission's Public Reference Room.

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of, and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

<sup>11</sup> 17 CFR 200.30-3(a)(12).

<sup>15</sup> U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

*A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change*

1. Purpose

Introduction

(A) Background

FINRA proposes to expand TRACE to include Asset-Backed Securities, as defined in Rule 6710(m), as TRACE-Eligible Securities, requiring members to report transactions in such securities to TRACE. For purposes of this proposed rule change, the term "Asset-Backed Security" is broadly defined, and the reporting of such securities to TRACE will permit FINRA to obtain additional transaction information and observe patterns of trading, facilitating the oversight and regulation of the Asset-Backed Securities market. FINRA will study the reported data to determine the volume and trading in various types of Asset-Backed Securities.

Generally, FINRA's policy favors transparency in the debt securities markets, and for most TRACE-Eligible Securities, real-time dissemination of transaction information is provided for under Rule 6750(a). Although at this time FINRA does not propose that transaction information on Asset-Backed Securities be disseminated, FINRA believes that the transparency in corporate bonds provided by TRACE today has contributed to better pricing, more precise valuations and reduced investor costs. After FINRA has had an opportunity to review data over a period of time, FINRA may determine that dissemination of some transaction information for Asset-Backed Securities is warranted.<sup>3</sup>

(B) Summary of Proposed Amendments

To incorporate Asset-Backed Securities in TRACE, FINRA proposes significant amendments to Rule 6710, Rule 6730 and Rule 6750 and lesser amendments to Rule 6720, Rule 6760 and Rule 7730. In Rule 6710, FINRA proposes to revise the defined terms, "TRACE-Eligible Security" and "Reportable TRACE Transaction,"<sup>4</sup> and to add nine defined terms, most of which relate to the trading of Agency

Pass-Through Mortgage-Backed Securities<sup>5</sup> and other types of Asset-Backed Securities that are collateralized by mortgages or other assets that are self-amortizing. In Rule 6730, FINRA proposes more liberal trade reporting requirements for transactions in Asset-Backed Securities than those in effect for corporate bonds, modifications to the reporting requirements relating to particular structural aspects or other features of certain Asset-Backed Securities, and, in Rule 6750(b), not to disseminate transaction information on Asset-Backed Securities. The proposed amendments to Rule 6760 characterize a member that is a Sponsor or an Issuing Entity<sup>6</sup> of an Asset-Backed Security as a managing underwriter, requiring such persons to provide notice as required under the rule. FINRA proposes amendments to Rule 7730 to apply the fees currently in effect under the rule at the same rates to transactions in Asset-Backed Securities; to provide that a transaction in an Agency Pass-Through Mortgage-Backed Security will not be treated as a List or Fixed Offering Price Transaction or a Takedown Transaction for purposes of trade reporting fees; and to define size (volume) for purposes of the reporting fees payable for transactions in certain Asset-Backed Securities. Finally, several minor, technical or clarifying amendments are proposed to the Rule 6700 Series (except for Rule 6740) and Rule 7730.

Discussion

(A) "TRACE-Eligible Security"; Other Defined Terms

*TRACE-Eligible Security and Asset-Backed Security.* Under Rule 6710(a), a TRACE-Eligible Security is a debt security that is U.S. dollar denominated and issued by a U.S. or foreign private issuer, and if a "restricted security" as defined in Securities Act Rule 144(a)(3), sold pursuant to Rule 144A; or is a U.S. dollar denominated security that is issued or guaranteed by an Agency or a Government-Sponsored Enterprise ("GSE").<sup>7</sup> Securities excluded from "TRACE-Eligible Security" include U.S. Treasury Securities, foreign sovereign securities and other securities not issued by a private issuer, Money

Market Instruments and Asset-Backed Securities.<sup>8</sup>

In Rule 6710(m), "Asset-Backed Security" is defined broadly to include a security that is defined as such under Securities Act Regulation AB,<sup>9</sup> a

<sup>8</sup> "U.S. Treasury Security" is defined in Rule 6710(p); "Money Market Instrument" is defined in Rule 6710(o); and "Asset-Backed Security" is defined in Rule 6710(m).

<sup>9</sup> Securities Act Regulation AB, Section 1101(c) defines "asset-backed security" as:

(1) "Asset-backed security" means a security that is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distributions of proceeds to the security holders; provided that in the case of financial assets that are leases, those assets may convert to cash partially by the cash proceeds from the disposition of the physical property underlying such leases.

(2) The following additional conditions apply in order to be considered an asset-backed security:

(i) Neither the depositor nor the issuing entity is an investment company under the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*) nor will become an investment company as a result of the asset-backed securities transaction.

(ii) The activities of the issuing entity for the asset-backed securities are limited to passively owing or holding the pool of assets, issuing the asset-backed securities supported or serviced by those assets, and other activities reasonably incidental thereto.

(iii) No non-performing assets are part of the asset pool as of the measurement date.

(iv) Delinquent assets do not constitute 50% or more, as measured by dollar volume, of the asset pool as of the measurement date.

(v) With respect to securities that are backed by leases, the portion of the securitized pool balance attributable to the residual value of the physical property underlying the leases, as determined in accordance with the transaction agreements for the securities, does not constitute:

(A) For motor vehicle leases, 65% or more, as measured by dollar volume, of the securitized pool balance as of the measurement date.

(B) For all other leases, 50% or more, as measured by dollar volume, of the securitized pool balance as of the measurement date.

(3) Notwithstanding the requirement in paragraph (c)(1) of this section that the asset pool be a discrete pool of assets, the following are considered to be a discrete pool of assets for purposes of being considered an asset-backed security:

(i) *Master Trusts.* The offering related to the securities contemplates adding additional assets to the pool that backs such securities in connection with future insurances of asset-backed securities backed by such pool. The offering related to the securities also may contemplate additions to the asset pool, to the extent consistent with paragraphs (c)(3)(ii) and (c)(3)(iii) of this section, in connection with maintaining minimum pool balances in accordance with the transaction agreements for master trusts with revolving periods or receivables or other financial assets that arise under revolving accounts.

(ii) *Prefunding Periods.* The offering related to the securities contemplates a prefunding account where a portion of the proceeds of that offering is to be used for the future acquisition of additional pool assets, if the duration of the prefunding period does not extend for more than one year from the date of insurance of the securities and the portion of the proceeds for such prefunding account does not involve in excess of:

<sup>3</sup> FINRA used this approach previously when it implemented dissemination in phases for various types of corporate bonds. Similarly, any proposal to adopt dissemination protocols for Asset-Backed Securities will be subject to rulemaking under Section 19(b)(1) of the Act, 15 U.S.C. 78s(b)(1).

<sup>4</sup> FINRA also proposes technical or clarifying amendments to "Agency Debt Security," "Asset-Backed Security" and "TRACE System Hours" as defined, respectively, in Rule 6710(l), Rule 6710(m) and Rule 6710(bb).

<sup>5</sup> "Agency Pass-Through Mortgage-Backed Security" is defined in proposed Rule 6710(v) and discussed, *infra*.

<sup>6</sup> "Sponsor" and "Issuing Entity" are defined in proposed Rule 6710(s) and proposed Rule 6710(t) and discussed, *infra*.

<sup>7</sup> "Agency" is defined in Rule 6710(k) and "Government-Sponsored Enterprise" ("GSE") is defined in Rule 6710(n).

mortgage-backed security, a collateralized mortgage obligation, a synthetic asset-backed security, or any instrument involving or based on the securitization of mortgages or other credits or assets, including but not limited to a collateralized debt obligation, a collateralized bond obligation, a collateralized debt obligation of Asset-Backed Securities or a collateralized debt obligation of collateralized debt obligations. These instruments include any instrument involving or based on the securitization of mortgages or other credits or assets, such as asset-backed securities backed by a pool credit card receivables, automobile loans, student loans, or Small Business Administration loans. The term includes Asset-Backed Securities that are issued or guaranteed by an Agency or a GSE.<sup>10</sup>

FINRA proposes to amend the defined term "TRACE-Eligible Security" in Rule 6710(a) to include all Asset-Backed Securities as broadly defined in Rule 6710(m) as TRACE-Eligible Securities. The specific exclusion of Asset-Backed Securities in the definition of "TRACE-Eligible Security" will be deleted. The proposed amendment will include in TRACE a significant, high dollar volume and increasing number of debt securities.

In addition, in Rule 6710(m) FINRA proposes minor amendments to the term, "Asset-Backed Security," which will clarify but will not change the scope or meaning of the definition. As amended, the definition will provide:

"Asset-Backed Security" means a security collateralized by any type of financial asset, such as loans, leases, mortgages, or secured or unsecured receivables, and includes but is not limited to an asset-backed security as used in Securities Act Regulation AB, Section 1101(c), a mortgage-backed security, a collateralized mortgage obligation, a synthetic asset-backed security, a collateralized debt obligation, a collateralized bond obligation, a collateralized debt obligation of Asset-Backed Securities or a

(A) For master trusts, 50% of the aggregate principal balance of the total asset pool whose cash flows support the securities; and

(B) For other offerings, 50% of the proceeds of the offering.

(iii) *Revolving Periods.* The offering related to the securities contemplates a revolving period where cash flows from the pool assets may be used to acquire additional pool assets, provided, that, for securities backed by receivables or other financial assets that do not arise under revolving accounts, the revolving period does not extend for more than three years from the date of issuance of the securities and the additional pool assets are of the same general character as the original pool assets.

<sup>10</sup>The defined term "Agency Debt Security" in Rule 6710(l) does not include an Asset-Backed Security, even if such security is issued or guaranteed by an Agency or a GSE.

collateralized debt obligation of collateralized debt obligations.

#### *Reportable TRACE Transaction.*

FINRA recently amended the Rule 6700 Series to require members to report primary market transactions, which harmonized the reporting requirements regarding such transactions with the requirements of The Municipal Securities Rulemaking Board ("MSRB").<sup>11</sup> Neither FINRA, with respect to TRACE-Eligible Securities, nor the MSRB, with respect to municipal securities, require that the initial sale from an issuer to an underwriter(s) or an initial purchaser(s) be reported as a primary market transaction.

FINRA proposes to amend the term "Reportable TRACE Transaction" in Rule 6710(c) to provide that, for Agency Pass-Through Mortgage-Backed Securities, all transactions, including the initial sale of an Agency Pass-Through Mortgage-Backed Security from an Issuing Entity or a Sponsor to an underwriter or an initial purchaser, are Reportable TRACE Transactions. FINRA proposes that such initial sales in an Agency Pass-Through Mortgage-Backed Security be reported due to the particular origination process, including the manner in which such securities are sold initially. In most cases, the origination of a TRACE-Eligible Security involves an offering where an issuer sells securities to one or more underwriters or initial purchasers that then resell such securities. However, due in part to the TBA process, and their status as exempt securities, Agency Pass-Through Mortgage-Backed Securities generally are not sold in traditional private offerings (or a traditional public offering). Consequently, requiring the reporting of the initial transaction may be the only opportunity to elicit necessary information for a regulatory audit trail of Asset-Backed Securities. In addition, the proposed amendments clarify that similar primary market sale transactions from the issuer to an underwriter or initial purchaser in other TRACE-Eligible Securities will continue not to be Reportable TRACE Transactions.

FINRA also proposes to streamline the definition, "Agency Debt Security," in Rule 6710(l) by using proposed defined terms and to transfer the defined term "TRACE System Hours" from Rule

<sup>11</sup> Securities Exchange Act Release No. 60726 (September 28, 2009), 74 FR 50991 (October 2, 2009) (Order Approving SR-FINRA-2009-010) (hereinafter "SEC Order Approving TRACE Expansion—Agency Debt Securities"). The MSRB requires the reporting of primary market transactions in municipal securities under MSRB Rule G-14.

6730(a) to Rule 6710(bb), with a minor amendment to clarify that the TRACE system operates only on business days.

#### *New Defined Terms*

FINRA proposes to add to Rule 6710 the following defined terms: "Sponsor" as proposed Rule 6710(s); "Issuing Entity" as proposed Rule 6710(t); "TBA" as proposed Rule 6710(u); "Agency Pass-Through Mortgage-Backed Security" as proposed Rule 6710(v); "Factor" as proposed Rule 6710(w); "Specified Pool Transaction" as proposed Rule 6710(x), "Stipulation Transaction" as proposed Rule 6710(y); "Dollar Roll" as proposed Rule 6710(z); and "Remaining Principal Balance" as proposed Rule 6710(aa).

*Sponsor and Issuing Entity.* In Asset-Backed Securities, the Sponsor of an Asset-Backed Security is the person (*i.e.*, usually a non-natural "person" such as a corporation) that decides to issue a security and determines its structure, pool and features. FINRA proposed to incorporate the definition of "Sponsor" adopted by the Commission in Securities Act Regulation AB, Item 1101(l) as proposed Rule 6710(s). Securities Act Regulation AB, Item 1101(l) defines "Sponsor" as "the person who organizes and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuing entity."<sup>12</sup>

The Sponsor of an Asset-Backed Bond is generally not the issuer. In Asset-Backed Securities, the issuer is often a trust, or special purpose vehicle ("SPV") or special purpose entity ("SPE") that is established solely to issue the Asset-Backed Securities and hold the pool of assets that back the asset-backed security, and, in SEC Regulation AB, is referred to as the "issuing entity." For purposes of TRACE, FINRA proposes to define "Issuing Entity" as the term is defined in Securities Act Regulation AB, Item 1101(f) in proposed Rule 6710(t). Securities Act Regulation AB, Item 1101(f) defines an issuing entity as "the trust or other entity created at the direction of the sponsor or depositor that owns or holds the pool assets and in whose name the asset-backed securities supported or serviced by the pool assets are issued."<sup>13</sup> Among other things, under the TRACE provisions, members that are Sponsors or Issuing

<sup>12</sup> Securities Act Regulation AB, Item 1101(l), 17 CFR 229.1101(l).

<sup>13</sup> Securities Act Regulation AB, Item 1101(f), 17 CFR 229.1101(f).

Entities are required to provide notice to FINRA Operations under Rule 6760.

TBA. FINRA proposes to add the defined term "TBA" as proposed Rule 6710(u). "TBA" stands for "to be announced" and refers to a transaction in an Agency Pass-Through Mortgage-Backed Security, as defined in proposed Rule 6710(v) and discussed in the following paragraph, where the parties agree to specific terms (*i.e.*, face amount of the security, coupon, maturity, the Agency or GSE under which the mortgage pools will be issued or guaranteed, price and clearance and settlement in conformity with the uniform practices established as "good delivery" on a standard pre-announced settlement date for such instruments), but do not identify the specific pool(s) of mortgages that will be delivered on settlement date.<sup>14</sup>

*Agency Pass-Through Mortgage-Backed Security.* Proposed Rule 6710(v) defines Agency Pass-Through Mortgage-Backed Security to mean:

[A] mortgage-backed security issued by an Agency or a Government-Sponsored Enterprise, for which the timely payment of principal and interest is guaranteed by an Agency or a Government-Sponsored Enterprise, representing ownership interests in a pool or pools of residential mortgage loans with the security structured to "pass through" the principal and interest payments made by the mortgagees to the owners of the pool(s) on a pro rata basis.

Several of the defined terms and other amendments to the Rule 6700 Series and Rule 7730 in this proposed rule change address issues that are specific to transactions in Agency Pass-Through Mortgage-Backed Securities.

*Remaining Principal Balance and Factor.* The related terms, "Remaining Principal Balance" and "Factor" are defined, respectively, in proposed Rule 6710(aa) and proposed Rule 6710(w). Factors and Remaining Principal Balances are relevant in the pricing and valuation of mortgage-backed securities and certain other types of Asset-Backed Securities that are backed by mortgage pools or other pools containing assets that are self-amortizing. Proposed Rule

6710(aa) defines "Remaining Principal Balance" to mean:

[F]or an Asset-Backed Security backed by a pool of mortgages or other assets that are self-amortizing, the total unpaid principal balance of all such mortgages, or the equivalent remaining value of such self-amortizing assets held in the asset pool, at a specific time, such as the Time of Execution.

A "Factor" is used by dealers and other market professionals to calculate the Remaining Principal Balance of an Asset-Backed Security that is backed by a pool of mortgages or other self-amortizing assets. Specifically, proposed Rule 6710(w) defines "Factor" as:

[T]he decimal value representing the proportion of the outstanding principal value of a security to its original principal value.

For example, at issuance, the Factor for every mortgage-backed security and certain other types of Asset-Backed Securities for which a Factor is used is 1.0. Over time, the Factor for the specific security changes, reflecting the Remaining Principal Balance of the pool of assets for such security.<sup>15</sup> In a transaction in an Asset-Backed Security that is backed by mortgages or other assets that are self-amortizing, under proposed amendments to Rule 6730(d)(2), discussed *infra*, a member will be required to report a Factor, which is used to price the security. However, not all types of Asset-Backed Securities are priced using a Factor.

*Specified Pool Transaction; Stipulation Transaction; Dollar Roll.* In proposed Rule 6710(x), Rule 6710(y), and Rule 6710(z), respectively, FINRA defines three special types of transactions that occur solely in Agency Pass-Through Mortgage-Backed Securities. The term "Specified Pool Transaction" is defined in proposed Rule 6710(x). A "Specified Pool Transaction" is a transaction in an Agency Pass-Through Mortgage-Backed Security that requires the seller to deliver at settlement "one or more pools of mortgages that, at the Time of Execution, are identified by their unique pool identification numbers and original principal value." The conditions limiting the seller's delivery options affect pricing, and FINRA proposes that such transactions be reported with an indicator, as discussed *infra*.

*In proposed Rule 6710(y), the term "Stipulation Transaction" is defined to mean a transaction:*

<sup>15</sup> For example, a mortgage-backed security with an original face value of \$10 million that has a Factor of .5 on April 15, 2009 has a Remaining Principal Balance of \$5 million as of April 15, 2009 (assuming all mortgage payments and prepayments have been included in the calculation of the Factor).

[I]n an Agency Pass-Through Mortgage-Backed Security as defined in paragraph (v) where, at the Time of Execution, the parties agree that the seller will deliver to the buyer an Agency Pass-Through Mortgage-Backed Security of a specified face amount and coupon from a specified Agency or Government-Sponsored Enterprise program that represents a pool (or pools) of mortgages, at a specified price, and the parties stipulate that the pool or pools to be delivered meet certain conditions that preclude settlement of the transaction in conformity with the uniform practices established as "good delivery" for an Agency Pass-Through Mortgage-Backed Security effected TBA.

A transaction in an Agency Pass-Through Mortgage-Backed Security that is a Stipulation Transaction differs from a "Specified Pool Transaction" because good delivery, although conditioned by the special stipulations, is not limited to specific pools that the parties have identified by pool number. Again, the special conditions that limit the seller's flexibility as to delivery affect pricing, and FINRA proposes that such trades be reported with an indicator.

The term "Dollar Roll," as defined in proposed Rule 6710(z), describes simultaneous transactions that are executed pursuant to an agreement between a buyer and seller of an Agency Pass-Through Mortgage-Backed Security. At the time of the transactions, the initial buyer of the Agency Pass-Through Mortgage-Backed Security pays a specific purchase price, agrees to a settlement date, and also agrees to reverse the purchase transaction at a later occurring settlement date, at a different price, and deliver to the initial seller of such securities the same or substantially similar securities. FINRA also proposes amendments to Rule 6730 requiring a member to report any of such transactions with an indicator, as discussed, *infra*.<sup>16</sup>

#### (B) Reporting

Rule 6730(a) requires members to report transactions to TRACE within 15 minutes of the Time of Execution, with certain exceptions for trades executed during non-TRACE System Hours.<sup>17</sup> The 15 minute reporting requirement applies to all TRACE-Eligible Securities transactions, except primary market

<sup>16</sup> Specifically, proposed Rule 6710(z) provides: "Dollar Roll" means a simultaneous sale and purchase of an Agency Pass-Through Mortgage-Backed Security as defined in paragraph (v) for different settlement dates, where the initial seller agrees to take delivery, upon settlement of the repurchase transaction, of the same or substantially similar securities.

<sup>17</sup> Rules 6730(a)(1) through (4) provides exceptions to the standard 15 minute reporting requirement if a member executes a transaction after or before TRACE System Hours or less than 15 minutes before the TRACE system closes.

<sup>14</sup> Specifically, proposed Rule 6710(u) provides: "TBA" means "to be announced" and refers to a transaction in an Agency Pass-Through Mortgage-Backed Security as defined in paragraph (v) where the parties agree that the seller will deliver to the buyer an Agency Pass-Through Mortgage-Backed Security of a specified face amount and coupon from a specified Agency or Government Sponsored Enterprise program representing a pool (or pools) of mortgages (that are not specified by unique pool number), at a specified price, and the parties will clear and settle the transaction in conformity with the uniform practices established as "good delivery" for such transactions and will not impose any special conditions or stipulations.

transactions that are List or Fixed Offering Price Transactions or Takedown Transactions.<sup>18</sup> Rules 6730(a) through (d) list the information that must be reported, including certain trade reporting indicators and modifiers that are required for some transaction reports.

#### End-of-Day Reporting

FINRA proposes to liberalize the reporting period for Asset-Backed Securities transactions. Under proposed Rule 6730(a)(6), members executing Asset-Backed Securities transactions will have until the end of the business day—until the TRACE system closes—to report such transactions. If a transaction in an Asset-Backed Security is executed after 5 p.m. Eastern Time, a broker-dealer will have until the end of the next business day to report the transaction under proposed Rules 6730(a)(6)(B)(i). In addition, if a broker-dealer executes an Asset-Backed Securities transaction at any time outside of the TRACE System Hours, the broker-dealer will have until the end of the TRACE System Hours on the next business day to report such transactions under Rules 6730(a)(6)(B)(ii) and (iii).<sup>19</sup>

Generally, transactions must be reported within 15 minutes of the Time of Execution to facilitate better pricing and to enhance transparency.<sup>20</sup> The more liberal end-of-day reporting requirements proposed for Asset-Backed Securities transactions are appropriate because, although pricing and other transaction information will be reviewed for surveillance, Asset-Backed Securities transactions initially will not be disseminated publicly to market participants. Also, the end-of-day reporting provisions will provide broker-dealers operational flexibility and will ease compliance burdens, particularly during the implementation of the proposed changes. FINRA will work with broker-dealers and third party vendors to ensure effective and cost efficient implementation.

<sup>18</sup> See SEC Order Approving TRACE Expansion—Agency Debt Securities.

<sup>19</sup> In Rule 6730(a)(6)(B)(iii), the proposed reporting requirements for transactions in Asset-Backed Securities that a broker-dealer executes on a Saturday, a Sunday, or a Federal or religious holiday when the TRACE system is closed include specific information requirements and have parallels to the reporting requirements for transactions reported under Rule 6730(a)(4).

<sup>20</sup> The extended reporting period that was recently approved by the SEC for List or Fixed Offering Price Transactions and Takedown Transactions permits T + 1 reporting only of those transactions that occur at the fixed price stated in the offering materials and are executed on the first day of an offering. See SEC Order Approving TRACE Expansion—Agency Debt Securities.

#### Additional Reporting Requirements for Asset-Backed Securities

*Security Identification.* Rule 6730(c)(1) requires a member to identify a TRACE-Eligible Security by a CUSIP number or a FINRA symbol in each transaction report. However, certain Asset-Backed Securities may be traded without an assigned CUSIP. FINRA proposes to amend Rule 6730(c)(1) to permit a member, when a CUSIP number is not available at the Time of Execution (or will not be assigned), to provide a similar numeric identifier, such as a mortgage pool number or a FINRA symbol. (FINRA symbols are assigned by FINRA Operations upon request.)

*Size (Volume).* Currently, members report the size (or volume) of a transaction for TRACE-Eligible Securities by reporting the number of bonds, as provided in Rule 6730(c)(2) and Rule 6730(d)(2). The TRACE System converts the information to a dollar value for purposes of the dissemination of transaction information. The stated reporting requirement includes the assumption that one bond represents a specific par amount, typically \$1,000 par (or principal) value.<sup>21</sup>

For certain Asset-Backed Securities, such as Agency Pass-Through Mortgage-Backed Securities, the principal value—the value of the collateral of the mortgages or other assets backing the security—declines over time (e.g., the mortgagees in the pool of mortgages pay down their mortgages).<sup>22</sup> In such cases, the size (volume) of such Asset-Backed Securities is the original face value or principal amount of the security at issuance, stated in dollars, and thereafter, the Remaining Principal Balance. The Remaining Principal Balance is calculated by multiplying the original face value by a Factor. FINRA proposes to amend Rule 6730(d)(2), which provides guidance on how to report size (volume) under Rule 6730(c)(2). In a transaction in an Asset-Backed Security for which par value is not used to measure the size (volume) of a transaction, the proposed amendments to Rule 6730(d)(2) will require a member to report the original face value of such security and, in a second field, the Factor the member used at the Time of Execution. Generally, FINRA expects that the Factor a member uses to execute a

<sup>21</sup> For example, a member reports a trade of 10 bonds and the total par value of \$10,000 is displayed.

<sup>22</sup> Occasionally, the value of the collateral increases—for example, in “interest only” mortgages, the loan balances may increase.

transaction will be the Factor that was most recently published by the Sponsor or Issuing Entity of the security or other source providing such information periodically to market participants.

*Price.* Rule 6730(c)(3) and Rule 6730(d)(1) require members to report price. If a price field is not available, members are required to report the contract amount and the accrued interest. Accrued interest is not a component of the total sale price of Asset-Backed Securities. To harmonize the reporting provision in connection with the reporting of Asset-Backed Securities, proposed amended Rule 6730(d)(1) will require members to report accrued interest only if applicable.

*Settlement Modifiers.* FINRA proposes several amendments to Rule 6730(d)(4) providing for modifiers and indicators that will distinguish certain trades executed at special prices or subject to other conditions affecting price. FINRA proposes to amend Rule 6730(d)(4)(B) to clarify that many securities are conventionally settled on T + 3, by stating this specifically, instead of using the phrase “regular way.” The change is necessary because the T + 3 convention for settlement of many securities does not apply to certain Asset-Backed Securities to be included in TRACE.<sup>23</sup> In addition, FINRA proposes additional amendments to Rule 6730(d)(4)(B) to reflect settlement conventions regarding Agency Pass-Through Mortgage-Backed Securities and the settlement of other Asset-Backed Securities. Transactions in Agency Pass-Through Mortgage-Backed Securities, by industry convention, are assigned one of four *monthly* settlement dates according to the type of Agency Pass-Through Mortgage-Backed Security to be settled.<sup>24</sup> The proposed amendments to Rule 6730(d)(4)(B) will not require a member to use a settlement modifier for a transaction in an Agency Pass-Through Mortgage-Backed Security that the parties will settle in conformity with the uniform practices established as “good delivery” for such transactions on the next occurring monthly date announced for settlement of such

<sup>23</sup> In some cases, certain types of Asset-Backed Securities transactions routinely may settle a number of months after trade date.

<sup>24</sup> Industry professionals involved in transactions in Agency Pass-Through Mortgage-Backed Securities effected TBA developed a convention for “regular way” settlement of these instruments. According to the type of security, such securities are settled monthly on specified settlement dates, which are announced for each month several months in advance. In total, four monthly Settlement Dates (A through D), per month, were established and published, to establish settlement conventions for the various types of securities being originated and traded.

securities. However, if the parties will settle other than in conformity with the uniform practices established as “good delivery” for such transactions, under the amendments members will be required to report using the settlement modifier (“.sNN”), indicating the number of days until settlement (e.g., “.s55”). In addition, the proposed amendments to Rule 6730(d)(4)(B) will require members to report transactions in all other types of Asset-Backed Securities using the settlement modifier (“.sNN”) and providing the specified number of days to settlement (e.g., “.s55”).

*Indicators for Specified Pool Transactions; Stipulation Transactions; Dollar Rolls.* As discussed above, transactions in Agency Pass-Through Mortgage-Backed Securities that are Specified Pool Transactions or Stipulation Transactions contain additional terms and conditions, which affect price. Price also is impacted in a Dollar Roll, which is a third type of transaction also discussed above that occurs in Agency Pass-Through Mortgage-Backed Securities. FINRA proposes indicators that a member must use when reporting a Specified Pool Transaction, a Stipulation Transaction, a Dollar Roll, and a transaction that is both a Dollar Roll and a Stipulation Transaction in, respectively, proposed Rule 6730(d)(4)(E)(i), (ii), (iii) and (iv).

*Agency Pass-Through Mortgage-Backed Security Initial Sale.* FINRA recently amended the Rule 6700 Series to require that primary market transactions be reported to TRACE. The reporting requirements for primary market transactions that are List or Fixed Offering Price transactions and Takedown Transactions are set forth in Rule 6730(a)(5), and extend the reporting period to the close of the TRACE system on T + 1. FINRA proposes that these reporting requirements will not apply to a transaction in an Agency Pass-Through Mortgage-Backed Security, which are not sold in a traditional underwriting or placement as envisioned and incorporated in the definitions of List or Fixed Offering Price Transaction and Takedown Transaction.

#### (C) Dissemination

Generally, FINRA’s policy favors transparency in the debt securities markets, and for most TRACE-Eligible Securities, real-time dissemination of transaction information is provided for under Rule 6750(a). Dissemination of the information occurs immediately upon receipt of the transaction report. The exceptions to the policy favoring dissemination in Rule 6750(b) are

currently limited to transactions effected pursuant to Securities Act Rule 144A, transfers of certain proprietary positions effected in connection with broker-dealer mergers or other broker-dealer consolidations, and List or Fixed Offering Price Transactions and Takedown Transactions.<sup>25</sup>

However, at this time, FINRA proposes not to disseminate information on transactions in Asset-Backed Securities in proposed Rule 6750(b)(4). The reporting of Asset-Backed Securities transactions will permit FINRA to obtain additional information, observe patterns of trading and otherwise engage in more in-depth surveillance of the Asset-Backed Securities market. FINRA will study the collected data to determine the volume and trading in various types of Asset-Backed Securities. FINRA may determine that dissemination of transaction information is warranted with respect to Asset-Backed Securities after it has had an opportunity to review data over a period of time. FINRA used this approach previously when it implemented dissemination in phases for various types of corporate bonds.

#### (D) Other Amendments to Rule 6700 Series

*Rule 6760.* Currently, Rule 6760 requires members that are managing underwriters to notify FINRA that a new TRACE-Eligible Security is about to be offered and sold in a primary offering. FINRA must have this information in the TRACE system to facilitate timely transaction reporting by all members that have effected transactions in a newly issued TRACE-Eligible Security. For TRACE-Eligible Securities that are Asset-Backed Securities, for the purposes of Rule 6760, FINRA proposes to amend Rule 6760(a) to characterize a Sponsor and an Issuing Entity of an Asset-Backed Security, if members, as managing underwriters, and require them, like underwriters or initial purchasers of Asset-Backed Securities, to provide FINRA Operations notice of

<sup>25</sup> TRACE-Eligible Securities transactions that are not disseminated are set forth in Rule 6750(b). Rule 6750(b)(1) applies as to transactions in TRACE-Eligible Securities that are affected as Securities Act Rule 144A transactions. Under Rule 6750(b)(2), FINRA does not disseminate information on a transfer of proprietary securities positions between a member and another member or non-member broker-dealer where the transfer: (A) Is effected in connection with a merger of one broker-dealer with the other broker-dealer or a direct or indirect acquisition of one broker-dealer by the other broker-dealer or the other broker-dealer’s parent company, and (B) is not in furtherance of a trading or investment strategy. Under recently approved Rule 6750(b)(3), FINRA will not disseminate List or Fixed Offering Price Transactions and Takedown Transactions.

a new Asset-Backed Security and information that identifies the new security by CUSIP (or if a CUSIP number is not available, a similar numeric identifier (e.g., a mortgage pool number) or a FINRA symbol) and describes the security.

For an Asset-Backed Security, FINRA proposes to amend the notice requirements in Rule 6760(b) to require the names of the Issuing Entity and the Sponsor, in addition to the CUSIP (or an alternative identifier) and other currently required information (i.e., coupon rate; maturity; the time the new issue is priced, and, if different, the time that the first transaction in the distribution or offering is executed; a brief description of the security type; and if the security will be traded subject to Securities Act Rule 144A).

FINRA also proposes minor technical, stylistic, or conforming changes to the Rule 6700 Series, including renumbering certain provisions, incorporating the term TRACE System Hours in certain provisions, and restating certain requirements regarding settlement and settlement modifiers.

#### (E) Fees

FINRA proposes that the current trade reporting fees set forth in Rule 7730 also apply to the reporting of transactions in Asset-Backed Securities. Because Asset-Backed Securities transaction information will not be disseminated, there will not be any market data available, and thus no market data fees are proposed. For transactions in Asset-Backed Securities, such as Agency Pass-Through Mortgage-Backed Securities, for which par value is not used to determine the size (or volume) of a transaction, FINRA clarifies how transaction fees will be assessed. For purposes of trade reporting fees, proposed Rule 7730(b)(1)(B) provides that transaction size for such securities will be the lesser of the original face amount or Remaining Principal Balance.

In proposed Rule 7730(b)(1)(D), FINRA proposes that transactions in an Agency Pass-Through Mortgage-Backed Security not be considered List or Fixed Offering Price Transactions or Takedown Transactions for purposes of the reporting fees in Rule 7730(b), which will eliminate any possible application to Agency Pass-Through Mortgage-Backed Security transactions of the recently adopted provision in Rule 7730(b)(1)(C). Rule 7730(b)(1)(C) provides that a member that reports a List or Fixed Offering Price Transaction or a Takedown Transaction shall not be charged the standard trade reporting fee assessed under Rule 7730(b)(1).

Finally, FINRA proposes minor technical, stylistic, or conforming changes to Rule 7730, including changes to conform the fee chart to the changes in the rule text.

FINRA will announce the effective date of the proposed rule change in a *Regulatory Notice* to be published no later than 60 days following Commission approval. The effective date will be no later than 270 days following publication of the *Regulatory Notice* announcing Commission approval.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>26</sup> which 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 and Section 15A(b)(5) of the Act,<sup>27</sup> which requires, among other things, that FINRA rules provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system that FINRA operates or controls in that: (i) the proposed rule change will enhance FINRA's surveillance of the debt market in connection with Asset-Backed Securities transactions generally; and (ii) the proposed fee proposal provides for reporting fees that mirror the fees currently in effect for corporate bonds, and are reasonable and equitably allocated among members.

### B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants or Others

Written comments were neither solicited nor received.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such

longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self regulatory organization consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2009-065 on the subject line.

### Paper Comments

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2009-065. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of the filing will also be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make

available publicly. All submissions should refer to File No. SR-FINRA-2009-065 and should be submitted on or before November 18, 2009.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>28</sup>

**Elizabeth M. Murphy,**

*Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-60851; File No. SR-FINRA-2009-068]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change Relating to FINRA's Rules Governing Clearly Erroneous Executions

October 21, 2009.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 19, 2009, Financial Industry Regulatory Authority, Inc. ("FINRA") (f/k/a National Association of Securities Dealers, Inc. ("NASD")) filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to adopt NASD Rule 11890, IM-11890-1, and IM-11890-2 into the Consolidated FINRA Rulebook as part of a new FINRA Rule 11890 Series governing clearly erroneous transactions and to amend these rules as part of a market-wide effort designed to provide transparency and finality with respect to clearly erroneous executions.

The text of the proposed rule change is available on FINRA's Web site at <http://www.finra.org>, at the principal office of FINRA and at the Commission's Public Reference Room.

<sup>28</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>26</sup> 15 U.S.C. 78o-3(b)(6).

<sup>27</sup> 15 U.S.C. 78o-3(b)(5).