

Secretary
Securities and Exchange Commission
100 F Street NE
Washington DC 20549
(Transmitted electronically)

May 17, 2024

Comments on Release No. 34-100006 and Release No. 34-100003

Dear Madam Secretary,

The Bond Dealers of America is happy to provide comments on two related SEC releases. The first is Release No. 34-100006 (File No. SR-FINRA-2024-004), "Order Instituting Proceedings To Determine Whether To Approve or Disapprove a Proposed Rule Change To Amend FINRA Rule 6730 (Transaction Reporting) To Reduce the 15-Minute TRACE Reporting Timeframe to One Minute." The second is Release No. 34-100003 (File No. SR-MSRB-2024-01), "Order Instituting Proceedings To Determine Whether To Approve or Disapprove a Proposed Rule Change Consisting of Proposed Rule Change To Amend MSRB Rule G-14 To Shorten the Timeframe for Reporting Trades in Municipal Securities to the MSRB" (together, the "Orders").

The Orders relate to two companion proposals from FINRA and the MSRB to shorten the time dealers have to report relevant fixed income trades to FINRA's Trade Reporting and Compliance Engine (TRACE) and the MSRB's Real-time Trade Reporting System (RTRS) from the current 15 minutes to one minute with significant exceptions (the "Proposals"). BDA supports approval of both Proposals as filed by FINRA and the MSRB.

We stand by our letter of February 15, 2024,¹ filed in response to FINRA and the MSRB transmitting their Proposals. In that letter we said "BDA supports reasonable regulation to ensure fixed income market transparency. We generally agree with the proposal to have those trades which can reasonably be reported within one minute be required by rulemaking to be reported within such time. However, BDA strongly believes that a significant number of trades cannot operationally be reported within one minute or potentially even shorter reporting timeframes than the current 15-minute requirement under current market practice and available operational technologies. Further, we question the benefit of an across-the-board shortening of reporting times and have concerns about the costs and risks associated with implementation."

As we pointed out in our February 15 letter, there are many categories of bond trades which, due to operational limitations, cannot be reported within one minute. These include, among numerous others, when a firm has never traded a particular bond. Before a trade in that CUSIP can be reported to the RTRS or TRACE, the dealer must enter or import a descriptive security record into its trade order management system, a step not necessary if a firm has traded the bond before and which necessarily

¹ Letter from BDA on SEC Release No. 34-99404 and Release No. 34-99402, February 15, 2024.

extends the time to report the trade. They also include broker-dealers who are dually registered as a Registered Investment Advisors (RIA) and must follow additional reporting steps for trades with the affiliated RIA for single trades that are allocated among numerous RIA accounts. The dealer must report both the single trade with the RIA and the allocations to the RIA's customer accounts, which can number in the thousands and can obviously extend the time to complete all trade reports.

Still another example includes certain municipal securities trades executed through brokers' brokers, or interdealer brokers who specialize in municipal securities. Providing or accessing liquidity through brokers' brokers can be complex and involve dozens of actual transactions with multiple counterparties for a single "trade," making it impossible to report all transactions within one minute. Also, dealer hedging trades can also be complex and involve multiple actual transactions with several different counterparties all simultaneously. Depending on the details, it could be impossible to report all related transactions within one minute.

The two major exceptions in the Proposals to the one-minute requirement—for dealers with limited trading activity and for transactions with a manual component—are essential to make FINRA's and the MSRB's trade reporting rules workable. Without those exceptions, either trade reporting violations would increase as dealers struggled to comply with an unworkable rule or a significant number of trades would not be executed at all because trade details could not be reported within one minute as would be required under FINRA and MSRB rules.

The Commission received three comment letters on the Proposals that objected to the exceptions.² Their arguments, however, fail to recognize the operational realities of the fixed income markets. The bond markets are significantly different from the equity market in fundamental ways. The bond markets are hundreds of times bigger than the equity market in terms of number of CUSIPs outstanding, for example. There is no system of constant two-way quotations for every issue. Also, while electronic trading has made significant inroads in the bond markets, fixed income is not nearly as homogenous or electronified as equities. In large part due to the lack of fungibility in the fixed income markets, a majority volume of bonds still trades by telephone or by electronic messaging service, especially in the institutional market. Dealers conduct bond trading by phone or messaging service because that is the execution method often preferred by institutional investor customers. Institutional investors often negotiate bond prices with dealer counterparties through a back-and-forth exchange, and that is often best facilitated through phone or messaging communication.

Both Proposals include an exception to one-minute reporting for "trades with a manual component." These include trades conducted by telephone or messaging system, trades that require special post-trade processing, or any trade which requires human intervention to execute or clear. The referenced commenters argued the Proposals do not justify the need for an exemption for trades with a manual component, with one stating "Investors and other market participants are subjected to greater risk for having incomplete, untimely information each time a 'manual' exception is relied upon. Yet, the Proposal makes no reference to why they should be subjected to these greater risks, or what the impacts upon them may be as a result of this new exemption."³ The reason is clear to anybody active in

² See letters from Citadel Securities ("Citadel letter"), Dimensional Fund Advisors LP ("DFA letter"), and Healthy Markets Association ("HMA letter").

³ HMA letter, page 11.

the fixed income markets.⁴ The market is not entirely electronic. As we described in detail in our February letter, there are trading and trade settlement processes which necessarily delay reporting past one minute. Any proposal to shorten the trade reporting time which does not reflect the operational realities of the fixed income markets is doomed to fail.

One commenter argued that maintaining next-day reporting for after-hours TRACE trades is a deficiency. “We worry that the new distinction may distort the markets by leading to more ‘off’ hours trading. We also worry about new opportunities for firms to engage in potentially manipulative trading strategies across different, related markets and products,” the commenter states.⁵ This perspective reflects a fundamental misunderstanding of the fixed income markets. Very few bond trades take place after hours because there is virtually no market liquidity after hours. There is no evidence that the provision under current rules that permits after-hours trades to be reported the next day has been abused or exploited or that dealers wait until after the TRACE system closes to execute transactions. The commenter’s perspective does not reflect reality.

Moreover, critics of the two exceptions in the Proposal generally suggest that dealers could or would use the exceptions to skirt trade reporting requirements. First, under both Proposals, dealers would be required to report trades “as soon as practicable” but in no case in longer than one minute after execution or 15 minutes if the trade qualifies for one of the exemptions. That means any action purposefully intended to extend the trade reporting time would be a violation. Both FINRA and the MSRB have been explicit about this. Second, there is no evidence that dealers “sit” on trades under current rules waiting for the 15-minute deadline. To be sure, dealers occasionally report trades late due to unanticipated hiccups in the trade or settlement process, and regulators sanction dealers for trade reporting violations. But there is no incentive or benefit for a dealer to purposely delay a trade report. And there is nothing in the Proposals that would incentivize dealers to start that behavior.

The exemption in both Proposals for trades with a manual component includes a requirement that manual trades would be subject to 15-minute reporting in the first year the rule changes are in effect, 10-minute reporting in the second year, and 5-minute reporting in the third year and thereafter. This stepdown would occur “automatically” as it is written into the Proposals. As we said in our February letter, we are concerned about committing to a stepdown in the reporting time for manual trades absent any experience with implementing the Proposals. We cannot be sure that manual trades can be reported within 10 or five minutes as the Proposals would require in years two and three. In that respect, we ask FINRA and the MSRB to commit to seeking public comment before allowing the stepdown in trade reporting times for manual trades to take effect.

⁴ The manual trade exception is justified even if the SEC were to wholly accept the commenter’s questionable assertion that investors would be “subjected to greater risk” as a result. As noted below, the BDA notes that dealers would still be required to report trades as soon as practicable under the manual trade exception, and so BDA believes the SROs have appropriately anticipated and mitigated any such potential investor harm through the proposed amendments. The BDA nevertheless questions whether the manual trade exception would, in fact, create greater risks for investors as the commentor suggests. More specifically, the commenter fails to address the challenges and costs associated with one-minute reporting, nor acknowledge that a significant portion of the investors who participate in the fixed income markets buy and hold to maturity and so arguably receive little to no benefit from intraday trading information (let alone materially benefit from accessing such trade information fourteen minutes faster).

⁵ HMA letter, page 8.

Commenters also criticized the exception for dealers with limited trading activity.⁶ The Proposals include exceptions which specify that any dealer who had fewer than 4000 TRACE-reportable trades or 1800 RTRS-reportable trades in either of the preceding two years would be subject to 15-minute reporting for the next year.

There was an average of over 11,000 TRACE-reportable corporate bond trades each day in 2023.⁷ That means approximately 2.25 million corporate trades were reported in the year. A dealer who executed fewer than 4000 trades in either of the previous two years reflects an insignificantly tiny portion of the market. Receiving and disseminating that dealer's trades in 15 minutes instead of one minute would not materially affect market transparency. Moreover, dealers eligible for the limited trading exemption would still be subject to the "as soon as practicable" requirement, so it is likely that many of their trade reports would come in before the 15-minute deadline. Smaller dealers need this exception because many conduct the trade reporting process entirely manually. There is no justification for requiring small broker-dealers who conduct a limited number of relevant trades to incur the cost of building expensive automated compliance systems when reducing their reporting time would have no material effect on transparency.

Another commenter suggested that "FINRA could phase out the exception for members with 'limited trading activity' by lowering the transaction threshold each year, which would give members both the time and incentive to modernize their systems so that they can report more quickly."⁸ Unfortunately, the cost to many firms to "modernize their systems" would drive some small firms out of the fixed income business entirely.

The fixed income markets and fixed income issuers and investors benefit from having a diversity of underwriters and dealers in the industry. Smaller broker-dealers play a vital role in servicing issuer and investor customers who may be overlooked by larger firms. Especially in the municipal securities market, characterized by a large number of relatively small issuers, issuers and investors would suffer if trade reporting rules drove smaller dealers out of the business. Regulating small broker-dealers out of business would signal a failed rulemaking. Losing dealer participation in the markets would also negatively affect liquidity.

Another commenter argued that the FINRA proposal does not meet the requirements of the Securities Exchange Act of 1934 because FINRA did not "estimate the number of transactions that are expected to qualify for the manual trade exception."⁹ This comment fails to give adequate weight to the information and statistics that FINRA provided throughout the rulemaking process. We are convinced that both FINRA and the MSRB have demonstrated that the Proposals are consistent with the Exchange Act.

Although the industry did not request a rulemaking to shorten the TRACE and RTRS trade reporting times, we have constructively engaged with regulators to help ensure that the Proposals enhance market transparency without creating insurmountable operational hurdles. The industry has worked hard over the last 20 years to continuously improve transparency. As the MSRB pointed out in its 2022 concept release, the share of RTRS trades reported within one minute increased from 69.5 percent in

⁶ Citadel letter, page 2, DFA letter, page 2, HMA letter, page 9

⁷ FINRA, "2023 TRACE Fact Book," Table P1.

⁸ DFA letter, page 2.

⁹ Citadel letter, page 2.

2005 to 80.2 percent in 2019.¹⁰ That is not the product of rulemaking but of consistent investments the industry has made to improve trading and clearing processes.

The BDA believes that accelerated trade reporting is best achieved through the dynamics of healthy market competition, rather than top-down regulatory intervention. The SROs' own data support the conclusion that competition among firms is already incentivizing the fixed income industry to report trades faster, as individual firms compete to offer customers more and more options like fully electronic trading.

As a matter of policy, BDA does not believe regulators should disrupt this healthy competition among firms to force a one-minute trade reporting deadline—an arbitrary policy objective that is certain to impose prohibitive costs and offers dubious transparency benefits at best. However, if the SEC, MSRB and FINRA believe that one-minute trade reporting must be achieved at this time through a regulatory mandate, then the BDA believes that any such rule must account for the unique characteristics of the fixed income markets. In this limited regard, the BDA supports the SEC's approval of the SROs' proposed rule changes because our membership believes that the exceptions for limited trading activity and for transactions with a manual component will limit the harms and unintended consequences of a one-minute trade reporting obligation. If those exceptions were eliminated, the BDA could not support the proposed rule changes.

Relatedly, once in effect, we remain concerned about how the proposed rule changes will affect the fixed income markets. We request that FINRA and the MSRB commit to seek public comment prior to each future step-down in the trade reporting deadline for transactions with a manual component. Public comment would ensure that any unintended harms caused by this one-minute policy objective can be timely avoided.

For a shortened trade reporting regime to work effectively, dealers must be able to comply with trade reporting rules. Without the two significant exceptions for firms with limited trading activity and for trades with a manual component, the Proposals cannot be fully complied with. Either late trade reports would rise as dealers struggle to comply, liquidity would diminish as dealers avoid trades where they may not meet the one-minute deadline, or most likely both. The exceptions to the Proposals are reasonably and narrowly targeted to comport with the realities of the fixed income markets and are essential to the workability of the trade reporting regulations. We support approval of the Proposals as filed.

Sincerely,



Michael Decker
Senior Vice President

¹⁰ MSRB, Notice 2022-07, Chart 1, page 12.