

REMINDER—TRACE REPORTING OF AGENCY DEBT SECURITIES AND PRIMARY MARKET TRANSACTIONS EFFECTIVE MARCH 1, 2010

In September 2009 the Financial Industry Regulatory Industry (“FINRA”) issued Regulatory Notice 09-57 (the “Notice”) to notify members that the Securities and Exchange Commission (the “SEC”) approved major amendments to the Trade Reporting and Compliance Engine (“TRACE”) Rules (FINRA Rule 6700 Series) and FINRA Rule 7730 relating to TRACE fees that will increase the number and type of securities and transactions that will be reported to TRACE. On March 1, 2010, the amended TRACE Rules and amended FINRA Rule 7730 will be effective. FINRA members must then report transactions in Agency Debt Securities and primary market transactions and comply with all other requirements in these amended rules.

The full text of the Notice is located at <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p120043.pdf>.

Amendment Overview

Effective March 1, 2010, amended FINRA Rule 6700 Series and FINRA Rule 7730 include all Agency Debt Securities as TRACE-Eligible Securities and require that all FINRA member firms must report primary market transactions in any TRACE-Eligible Security to TRACE. “Agency Debt Securities” include debt securities issued or guaranteed by an Agency or Government-Sponsored Enterprise. As defined in 5 U.S.C. § 105, “Agency” includes a U.S. “executive agency” but excludes the U.S. Department of the Treasury (the “Treasury”) in the exercise of its authority to issue Treasury securities. In FINRA Rule 6710(n), “Government-Sponsored Enterprise” has the same meaning as defined in 2 U.S.C. § 622(8). The amendments:

- expand and restate the definition of TRACE-Eligible Security in FINRA Rule 6710(a) to include Agency Debt Securities as “TRACE-Eligible Securities” and delete the criteria that a security be investment grade or non-investment grade and depository eligible;
- alter FINRA Rule 6710 to include the following newly defined terms: “Agency,” “Agency Debt Security,” “Asset-Backed Security,” “Government-Sponsored Enterprise,” “Money Market Instrument,” and “U.S. Treasury Security”;
- expand TRACE to include primary market transactions as “Reportable TRACE Transactions,” as defined in FINRA Rule 6710(c);
- require member firms to report transactions in Agency Debt Securities and primary market transactions under FINRA Rule 6730 and incorporate certain modified trade reporting requirements applicable to “List or Fixed Offering Price Transactions” and “Takedown Transactions” (as defined in FINRA Rule 6710) in FINRA Rule 6730(a)(5) and FINRA Rule 6730(d)(4)(D);
- provide for the dissemination of information on transactions in Agency Debt Securities and primary market transactions under FINRA Rule 6750, except List or Fixed Offering Price Transactions and Takedown Transactions, as provided in FINRA Rule 6750(b)(3);

- regarding notification requirements in Rule 6760, establish an alternative notification requirement when a new TRACE-Eligible Security is not assigned a CUSIP, require notification of the time when a new issue is priced and, if different, the time when the first transaction in the distribution or offering is executed, and extend the period for a firm to timely provide all information required in the member firm's notice to FINRA regarding a new TRACE-Eligible Security when the new issue is priced and commences on the same business day between 9:30 a.m. Eastern Time (ET) and 4:00 p.m. ET;
- grant FINRA emergency authority to suspend the reporting and/or dissemination of certain transactions in TRACE-Eligible Securities, or the reporting of certain data elements otherwise required to be reported and/or the dissemination of certain data elements, as market conditions warrant and in consultation with the SEC in new FINRA Rule 6770; and
- apply the fee rates currently in effect in FINRA Rule 7730 to transactions in Agency Debt Securities and primary market transactions, and do not require firms to pay a reporting fee when reporting List or Fixed Offering Price Transactions and Takedown Transactions as provided in FINRA Rule 7730(b)(1), distinguish TRACE market data relating to corporate debt from market data relating to Agency Debt Securities (the "Agency Data Set"), and establish fees for the new Agency Data Set in Rule 7730 generally, including fees that are incorporated in FINRA Rule 7730(a)(1) for "Web Browser Access."

Agency Debt Securities

FINRA Rule 6710(a) currently precludes any security issued by an agency of the U.S. from being a TRACE-Eligible Security. Certain types of securities, including a security issued by a Government-Sponsored Entity ("GSE"), are specifically excluded. To reflect industry convention, amended FINRA Rule 6710(l) expands TRACE-Eligible Security to include a debt security that is (i) issued or guaranteed by an Agency as defined in paragraph (k); or (ii) issued or guaranteed by a GSE as defined in paragraph (n). The definition explicitly excludes U.S. Treasury Securities. Asset-Backed Securities, as broadly defined in FINRA Rule 6710(m), will not be included in the definition of TRACE-Eligible Security, as amended.

With the foregoing parameters included, a TRACE-Eligible Security will be defined in amended FINRA Rule 6710(a) as:

a debt security that is United States 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 Securities Act Rule 144A; or is a debt security that is U.S. dollar-denominated and issued or guaranteed by an Agency as defined in paragraph (k) or a Government-Sponsored Enterprise as defined in paragraph (n). "TRACE-Eligible Security" does not include a debt security that is:

- (1) issued by a foreign sovereign or is a U.S. Treasury Security as defined in paragraph (p);
- (2) a Money Market Instrument as defined in paragraph (o); or
- (3) an Asset-Backed Security as defined in paragraph (m).

Primary Market Transactions

FINRA Rule 6710(c) currently defines “Reportable TRACE Transaction” as any secondary market transaction in a TRACE-Eligible Security except transactions that are not reported as specified in FINRA Rule 6730(e). As amended, FINRA Rule 6710(c) is not limited to secondary market transactions, and firms will be required to report primary market transactions in any TRACE-Eligible Security. Two types of primary market transactions, List or Fixed Offering Price Transactions and Takedown Transactions, will be subject to more liberal trade reporting requirements and two other significant modifications to the current TRACE requirements due to the nature of the transactions and the assumption that such transactions (in a single security) will be executed at a single price. A List or Fixed Offering Price Transaction will be defined in FINRA Rule 6710(q) as:

a primary market sale transaction sold on the first day of trading of a new issue:
(i) by a sole underwriter, syndicate manager, syndicate member or selling group member at the published or stated list or fixed offering price, or (ii) in the case of a primary market sale transaction effected pursuant to Securities Act Rule 144A, by an initial purchaser, syndicate manager, syndicate member or selling group member at the published or stated fixed offering price.

A Takedown Transaction will be defined similarly in Rule 6710(r).

The current TRACE requirements that will be modified for List or Fixed Offering Price Transactions and Takedown Transactions are:

- List or Fixed Offering Price Transactions and Takedown Transactions will not be subject to 15-minute reporting. Instead, member firms will be permitted to report a List or Fixed Offering Price Transaction or a Takedown Transaction that is executed on a business day at or after 12:00 a.m. ET through 11:59:59 p.m. ET, not later than T+1 during TRACE system hours under Rule 6730(a)(5);
- List or Fixed Offering Price Transactions and Takedown Transactions will not be disseminated as provided in FINRA Rule 6750(b)(3); and
- a member firm that timely reports a List or Fixed Offering Price Transaction or a Takedown Transaction will not be required to pay the standard transaction reporting fee set forth in FINRA Rule 7730(b)(1). However, firms that report such transactions incorrectly or late will incur “Cancel/correct” and “As/of Trade Late” fees.

Emergency Authority

Under new Rule 6770, FINRA will possess emergency authority regarding TRACE. FINRA may suspend the reporting and/or dissemination of certain transactions in TRACE-Eligible Securities, or the reporting of certain data elements that are otherwise required to be reported under FINRA Rule 6730, and/or the dissemination of certain data elements, as market conditions warrant and in consultation with the SEC.

If you would like to discuss any of the issues discussed in this Client Alert, please contact any attorney in our Corporate and Securities Group or visit us online at chapman.com.

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