MEMO# 11624

February 11, 2000

INSTITUTE COMMENT LETTER ON NASD'S PROPOSAL TO CREATE A CORPORATE BOND TRADE REPORTING AND TRANSACTION DISSEMINATION FACILITY

1 See Memorandum to Fixed Income Advisory Committee No. 9-99, dated December 16, 1999. The NASD's proposal would require NASD members to report to Nasdaq's Trade Reporting and Comparison Entry Service ("TRACE") all secondary transactions in specified U.S. corporate bonds within one hour of trade execution. After an initial six-month period, the one-hour timeframe would be reduced to fifteen minutes, and Nasdaq thereafter will begin disseminating trade reports to the public through market data vendors. [11624] February 11, 2000 TO: FIXED-INCOME ADVISORY COMMITTEE No. 3-00 RE: INSTITUTE COMMENT LETTER ON NASD'S PROPOSAL TO CREATE A CORPORATE BOND TRADE REPORTING AND TRANSACTION DISSEMINATION FACILITY ____ As we previously informed you, in December, the Securities and Exchange Commission requested comment on a proposal by the National Association of Securities Dealers, Inc. ("NASD") to establish a corporate bond trade reporting and transaction dissemination facility.1 The Institute filed the attached comment letter in support of the NASD proposal, which is summarized below. The TRACE Service The Institute's letter agrees that TRACE should be the central repository for the collection and dissemination of trade report information on secondary corporate bond transactions, but notes that TRACE should not be the only vehicle through which such information is disseminated. The letter supports the development of private initiatives to capture and distribute trade data and explains that such a competitive process would greatly benefit market participants. The letter also notes that much like the proposed phase in of the trade reporting process, it may be advisable to phase in the transaction dissemination process as well, which would enable the NASD and market participants to evaluate the success of the facility, including the sufficiency of the information being disseminated. The Institute's letter also addresses members' concern about the possibility of the NASD's charging excessive fees for the data it will collect and sell back to the market as a result of the market dominance TRACE will likely enjoy, at least until other methods to facilitate the flow of trade data are developed. The letter urges the Commission therefore to follow some type of cost-based standard in evaluating and approving the fees for TRACE data. Elements of the Trade Report The Institute's letter agrees with the type and nature of trade data proposed to be required in the trade reports submitted to TRACE, including the fact that much of this information would be disseminated to the public. The letter also supports the requirement that each report contain the time the trade is executed, noting that this information is critical to determining the relative value of

a bond as 2well as continued reliability of the prices. Moreover, the letter supports the NASD's decision not to disseminate information regarding the identity of the trading firm involved in the transaction, adding that to do otherwise could adversely affect the prices the firm is able to receive, thereby harming fund shareholders. The Institute's letter notes that the NASD plans to calculate and disseminate bond yield information, based on the price information it receives from the submitted reports, but points out that the proposing release fails to define "yield" or explain how it would be calculated. Thus, the letter recommends that given its importance, the method for calculating yield should be reflected in the final rule. Finally, the Institute's letter notes that the NASD plans to disseminate to the public trade report information regarding the actual quantity of bonds traded, except that high yield and unrated trades over a $1 million par value would be disseminated as "1MM+" and investment grade trades over a $5 million par value would be disseminated as "5MM+". The letter explains that because transactions in high yield and unrated bonds routinely exceed $5 million, and because trades below that level are generally viewed as odd-lot trades, which may not reflect the price at which larger trades may be executed, the threshold for high yield and unrated trades should be increased to $5 million, in order to provide the market with more relevant and useful information. Barry E. Simmons Assistant Counsel Attachment