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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2015 - * 036
Amendment No. (req. for Amendments *) 1

Filing by Financial Industry Regulatory Authority

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial *	Amendment *	Withdrawal	Section 19(b)(2) *	Section 19(b)(3)(A) *	Section 19(b)(3)(B) *
☐	☑	☐	☑	☐	☐

Rule

☐ 19b-4(f)(1) ☐ 19b-4(f)(4)
☐ 19b-4(f)(2) ☐ 19b-4(f)(5)
☐ 19b-4(f)(3) ☐ 19b-4(f)(6)

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐

Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document ☐

Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Adam Last Name * Arkel
Title * Associate General Counsel
E-mail * adam.arkel@finra.org
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Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 01/13/2016
By Patrice Gliniecki
(Name *)

(Title *)
Senior Vice President and Deputy General Counsel

Patrice Gliniecki,

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information * Add Remove View	The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.
Exhibit 1 - Notice of Proposed Rule Change * Add Remove View	The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)
Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies * Add Remove View	The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)
Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications Add Remove View Exhibit Sent As Paper Document ☐	Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.
Exhibit 3 - Form, Report, or Questionnaire Add Remove View Exhibit Sent As Paper Document ☐	Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.
Exhibit 4 - Marked Copies Add Remove View	The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.
Exhibit 5 - Proposed Rule Text Add Remove View	The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.
Partial Amendment Add Remove View	If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

On October 6, 2015, Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission (the "Commission" or "SEC") proposed rule change SR-FINRA-2015-036 (the "original filing," "proposal," or "proposed rule change"), pursuant to which FINRA proposed to amend FINRA Rule 4210 (Margin Requirements) to establish margin requirements for (1) To Be Announced ("TBA") transactions, inclusive of adjustable rate mortgage ("ARM") transactions; (2) Specified Pool Transactions; and (3) transactions in Collateralized Mortgage Obligations ("CMOs"), issued in conformity with a program of an agency or Government-Sponsored Enterprise ("GSE"), with forward settlement dates, as defined more fully in the original filing (collectively, "Covered Agency Transactions," also referred to, for purposes of the original filing and this Partial Amendment No. 1, as the "TBA market").

The Commission published the proposed rule change for public comment in the Federal Register on October 20, 2015.[1] The Commission received 109 comment letters in response to the proposed rule change, including 54 form letter comments and 55 individual letter comments.[2] FINRA is filing this Partial Amendment No. 1 to respond to the comments the Commission received on the Federal Register publication and to add to the proposed rule language, in response to comments, proposed paragraph (e)(2)(H)(ii)a.2, which provides that a member may elect not to apply the margin requirements of paragraph (e)(2)(H) to multifamily and project loan securities, subject to specified conditions. Further, FINRA proposes in this Partial Amendment No. 1 that the risk limit determination requirements as set forth in paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H) of Rule 4210 and proposed Supplementary Material .05 become effective six months from the date the proposed rule change is approved by the Commission. FINRA proposes that the remainder of the proposed rule change become effective 18 months from the date the proposed rule change is approved by the Commission.

With this Partial Amendment No. 1, FINRA is including (1) Exhibit 2 (see below); (2) Exhibit 4 (see below), which reflects changes to the text of the proposed rule change pursuant to this Partial Amendment No. 1, marked to show additions to the text as proposed in the original filing; and (3) Exhibit 5 (see below), which reflects the changes to the current rule text that are proposed in the proposed rule change, as amended by this Partial Amendment No. 1.

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1 Securities Exchange Act Release No. 76148 (October 14, 2015), 80 FR 63603 (October 20, 2015) (Notice of Filing of Proposed Rule Change; File No. SR-FINRA-2015-036).

2 A list of written comments is attached with this Partial Amendment No. 1 as Exhibit 2. Unless noted otherwise, all references to commenters in this Partial Amendment No. 1 are to the commenters as listed in Exhibit 2.

A. Multifamily and Project Loan Securities

As set forth more fully in the original filing, the margin requirements set forth in the proposed rule change would apply to "Covered Agency Transactions." To recap, "Covered Agency Transactions" means:

- TBA transactions, as defined in FINRA Rule 6710(u),[3] inclusive of ARM transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;[4]

- Specified Pool Transactions, as defined in FINRA Rule 6710(x),[5] for which the difference between the trade date and contractual settlement date is greater than one business day;[6] and

- CMOs, as defined in FINRA Rule 6710(dd),[7] issued in conformity with a

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3 FINRA Rule 6710(u) defines "TBA" to mean a transaction in an Agency Pass-Through Mortgage-Backed Security ("MBS") or a Small Business Administration ("SBA")-Backed Asset-Backed Security ("ABS") where the parties agree that the seller will deliver to the buyer a pool or pools of a specified face amount and meeting certain other criteria but the specific pool or pools to be delivered at settlement is not specified at the Time of Execution, and includes TBA transactions for good delivery and TBA transactions not for good delivery. Agency Pass-Through MBS and SBA-Backed ABS are defined under FINRA Rule 6710(v) and FINRA Rule 6710(bb), respectively. The term "Time of Execution" is defined under FINRA Rule 6710(d).

4 See proposed FINRA Rule 4210(e)(2)(H)(i)c.1. in Exhibit 5 in this Partial Amendment No. 1.

5 FINRA Rule 6710(x) defines Specified Pool Transaction to mean a transaction in an Agency Pass-Through MBS or an SBA-Backed ABS requiring the delivery at settlement of a pool or pools that is identified by a unique pool identification number at the Time of Execution.

6 See proposed FINRA Rule 4210(e)(2)(H)(i)c.2. in Exhibit 5 in this Partial Amendment No. 1.

7 FINRA Rule 6710(dd) defines CMO to mean a type of Securitized Product backed by Agency Pass-Through MBS, mortgage loans, certificates backed by project loans or construction loans, other types of MBS or assets derivative of MBS, structured in multiple classes or tranches with each class or tranche entitled to receive distributions of principal or interest according to the requirements adopted for the specific class or tranche, and includes a real estate mortgage investment conduit ("REMIC").

program of an agency, as defined in FINRA Rule 6710(k),[8] or a GSE, as defined in FINRA Rule 6710(n),[9] for which the difference between the trade date and contractual settlement date is greater than three business days.[10]

FINRA noted that the scope of "Covered Agency Transactions" is intended to be congruent with the scope of products addressed by the Treasury Market Practices Group ("TMPG") best practices and related TMPG updates, and that the term would include within its scope multifamily housing and project loan program securities such as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, and Ginnie Mae Construction Loan or Project Loan Certificates (collectively, for purposes of this Partial Amendment No. 1, "multifamily and project loan securities").[11]

Commenters expressed concerns that FINRA should not include multifamily and project loan securities within the scope of the proposed margin requirements.[12] These

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8 FINRA Rule 6710(k) defines "agency" to mean a United States executive agency as defined in 5 U.S.C. 105 that is authorized to issue debt directly or through a related entity, such as a government corporation, or to guarantee the repayment of principal or interest of a debt security issued by another entity. The term excludes the U.S. Department of the Treasury in the exercise of its authority to issue U.S. Treasury Securities as defined under FINRA Rule 6710(p). Under 5 U.S.C. 105, the term "executive agency" is defined to mean an "Executive department, a Government corporation, and an independent establishment."

9 FINRA Rule 6710(n) defines GSE to have the meaning set forth in 2 U.S.C. 622(8). Under 2 U.S.C. 622(8), a GSE is defined, in part, to mean a corporate entity created by a law of the United States that has a Federal charter authorized by law, is privately owned, is under the direction of a board of directors, a majority of which is elected by private owners, and, among other things, is a financial institution with power to make loans or loan guarantees for limited purposes such as to provide credit for specific borrowers or one sector and raise funds by borrowing (which does not carry the full faith and credit of the Federal Government) or to guarantee the debt of others in unlimited amounts.

10 See proposed FINRA Rule 4210(e)(2)(H)(i)c.3. in Exhibit 5 in this Partial Amendment No. 1.

11 See 80 FR 63603, 63605.

12 See Letter Type A, Letter Type B, AGM, AJM, BDA, Bellwether, CBRE, Centennial, Century, CHF, Churchill, Columbia, Crain, Davis-Penn 1, Davis-Penn 2, Draper, DUS, Dwight, First Housing, Forest City 1, Forest City 2, Gershman 1, Gershman 2, Great Lakes, Highland 1, Highland 2, Lancaster, Love Funding, M&T Realty, MBA, MBA & Others 1, MBA & Others 2, MBA Supplemental Comments, NMHC/NAA, NorthMarq, Perez, Prairie Mortgage, Prudential Mortgage, Red Mortgage, Richmac, Sims Mortgage, W&D, and Ziegler.

commenters said that the proposed rule change would impose undue burdens on participants in the multifamily and project loan securities market, that the multifamily and project loan securities market is of small size relative to the overall TBA market, that the regulatory benefits gained from any reduction of systemic risk and counterparty exposure would be outweighed by the harms caused to the market, that there are safeguards in the market, including the provision of good faith deposits by the borrower to the lender, and requirements imposed by the issuing agencies and GSEs, and, related to that point, that the manner in which multifamily and project loan securities are originated and traded does not give rise to the type of credit exposure that may exist in the TBA market overall. Commenters said that about $40 to $50 billion per year in multifamily and project loan securities are issued versus about $1 trillion for the TBA market overall,[13] that a typical multifamily or project loan security is based on a single loan for a single project the identity of which is known at the time the lender and borrower agree to the terms of the loan and the security is underwritten, thereby helping to reduce settlement risk, and that, by contrast, securities in the overall TBA market are based on pools of loans that often have not been originated at the time the Covered Agency Transaction takes place.[14] Commenters said that multifamily and project loan securities are not widely traded and often cannot be marked to the market for purposes of complying with the proposed margin requirements.[15]

In response, FINRA has reconsidered and does not propose at this time to require that members apply the proposed margin requirements[16] to multifamily and project loan securities, subject to specified conditions. Specifically, FINRA proposes in this Partial Amendment No. 1 to add to FINRA Rule 4210 new paragraph (e)(2)(H)(ii)a.2. to provide that a member may elect not to apply the margin requirements of paragraph (e)(2)(H) of the rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided that: (i) such securities are issued in conformity with a program of an agency, as defined in FINRA Rule 6710(k),[17] or a GSE, as defined in FINRA Rule 6710(n),[18] and are documented as Freddie Mac K

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13 See CBRE, CHF, Forest City 1, Forest City 2, Letter Type A, MBA, and NMHC/NAA.

14 See Century, MBA, MBA Supplemental Comments, and NorthMarq.

15 See Century, MBA, NorthMarq, and W&D.

16 In the interest of clarity, FINRA notes that the "proposed margin requirements" refers to the margin requirements as to Covered Agency Transactions as set forth in the original filing, as amended by this Partial Amendment No. 1. Products or transactions that are outside the scope of Covered Agency Transactions are otherwise subject to the requirements of FINRA Rule 4210, as applicable.

17 See note 8 supra.

18 See note 9 supra.

Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade; and (ii) the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b. of Rule 4210.[19] FINRA believes that the proposed exception for multifamily and project loan securities is appropriate at this time. Based on FINRA's analysis of transactional data, multifamily and project loan securities constitute a small portion of the Covered Agency Transactions market overall,[20] which suggests multifamily and project loan securities are less likely to pose issues of systemic risk. However, in this regard, FINRA notes that systemic risk is only one facet of FINRA's concern. As a matter of investor protection and market integrity, FINRA believes that it is appropriate to require that members make and enforce written risk limit determinations for their counterparties in multifamily and housing securities. FINRA believes that imposing the requirement on members to make and enforce risk limits as to counterparties in multifamily and project loan securities is appropriately tailored, as discussed in the original filing with respect to the risk limit requirement generally,[21] to help ensure that the member is properly monitoring its risk. The requirement would serve to help prevent over-concentration in these products. In light of ongoing analysis in this area, FINRA may consider additional rulemaking if necessary.[22]

FINRA is aware that the proposed exception for multifamily and project loan securities may potentially impact the estimates of expected mark to market margin requirements presented in the Statement on Burden on Competition section of the original filing.[23] Specifically, the original analysis was based on the net exposure to any single

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19 See Exhibit 4 and Exhibit 5 in this Partial Amendment No. 1. Proposed Rule 4210(e)(2)(H)(ii)b. sets forth the proposed rule's requirements as to written risk limits.

20 In a sample of open transactions provided by a major clearing broker-dealer, transactions in multifamily securities sum up to approximately $5 billion and constitute approximately 8% of the total open transactions in TBA market securities across 1,142 accounts.

21 See 80 FR 63603, 63606.

22 For example, the federal banking agencies (the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency) recently stated that with respect to commercial real estate lending they have observed certain risk management practices at some financial institutions that cause them concern. See Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation and Office of the Comptroller of the Currency Joint Release, "Statement on Prudent Risk Management for Commercial Real Estate Lending" (December 18, 2015), available at: <https://www.fdic.gov/news/news/press/2015/pr15100.html>.

23 See 80 FR 63603, 63609 through 63615.

counterparty in any TBA market transaction, and therefore may have included situations where the exposure on an open position in a single family TBA market transaction could be offset by an opposite exposure on an open position in a multifamily TBA market transaction with the same counterparty.

As such, the proposed exception for multifamily and project loan securities may alter the net margin calculation for members. Members that transact strictly in multifamily TBA market securities would find that their margin obligations would be lower under this formulation, and thus have lower burdens imposed, if the member elects not to apply the margin requirements specified in paragraph (e)(2)(H) of the rule as permitted by proposed paragraph (e)(2)(H)(ii)a.2. But members who transact in both single and multifamily TBA market securities with a given counterparty might find that their margin obligations could be higher or lower in the presence of the exception. In addition, these members would likely incur additional costs to monitor single and multifamily TBA market transactions separately.

While the amendment proposed in this Partial Amendment No. 1 may impact the margin requirements for some members, FINRA has reason to expect that these impacts would be small based on a review of TBA market transactions. First, the size of the multifamily and project loan securities market is estimated to be relatively small compared to the single family segment of the market. According to the Financial Accounts of the United States published by the Federal Reserve Board, as of the third quarter of 2015, there were approximately $189.9 billion of multifamily residential agency and GSE-backed mortgage pools outstanding, compared to approximately $1.5 trillion for single family mortgage pools.[24] Second, FINRA staff also analyzed the TBA transactions in 2014 from TRACE and found that less than 1% of TBA transactions occurred in Delegated Underwriting and Servicing ("DUS") pools securities sponsored by Fannie Mae.

To estimate the impact of the exception on broker-dealers and mortgage banks, FINRA staff also analyzed transactional data provided by a major clearing broker-dealer. This dataset contains 27,350 open transactions as of January 7, 2016 in 1,142 accounts at 49 brokers. 261 of these accounts, at four brokers, had exposure to multifamily and project loan securities. The size of the open transactions in the single family securities ranged between $7,000 and approximately $14 billion per account in the whole sample, with an average (median) of approximately $64 million ($6.9 million). For comparison purposes, the size of open transactions in the multifamily securities ranged between $25,000 and approximately $2 billion per account, with an average (median) of approximately $20 million ($640,000).[25]

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[24] See Table L.125 in Board of Governors of the Federal Reserve System Statistical Release (December 10, 2015), available at: <http://www.federalreserve.gov /releases/z1/current/z1.pdf>.

[25] The difference between the average size of open transactions for single family and multifamily securities is statistically significant at the 5% level.

Of the 261 accounts that had exposure to multifamily and project loan securities, only nine also had open transactions in single family securities. While the size of the open transactions for multifamily securities in these nine accounts is larger than that for single family securities in these same nine accounts that had exposure to both types of securities, the difference is not statistically significant due to the small sample size and high variance.

The average number of days until settlement is also larger, being approximately 79 days for the open transactions in multifamily securities versus 50 days for the transactions in single-family securities.[26]

The evidence presented here suggests that some brokers may have sizable positions in multifamily securities. However, as evidenced by the data, these positions are likely to be maintained by a small number of brokers and the size of the multifamily TBA market is currently a small portion of the overall TBA market that does not potentially represent any systemic risk. Further, in the sample examined, only nine brokers with transactions in multifamily TBA market securities also had open transactions in single family TBA market securities, suggesting there is limited correlation in counterparty risk across the two segments of the market.

B. Impact and Scope of the Proposal (Other Than With Respect to Multifamily and Project Loan Securities)

Some commenters supported the proposed rule change's goal of addressing counterparty risk in the TBA market and reducing systemic risk.[27] SIFMA acknowledged the need for overall consistency between the proposal and the best practices recommendations of the TMPG.[28] However, commenters expressed concerns that the proposal's scope is overly broad and its requirements too complex to be operationally feasible, and that the proposal would increase costs on various participants in the mortgage market, including small, medium or regional participants, with the effect of driving some participants from the market.[29] Brean Capital said that all but the largest firms would be driven out of the market. ACLI questioned the need for the rulemaking on grounds that the TBA market remained stable prior to and throughout the 2008 financial crisis. ACLI expressed concern that the eligible pool of collateral for margin purposes is limited and that the opportunity cost of posting collateral would force institutions to forgo participating in the market or would force them to pass costs on to consumers. ICI suggested the rule should only reach TBA transactions and Specified Pool Transactions. Robert Baird suggested the proposal should not reach Specified Pool

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26 The difference between the average settlement days for single family and multifamily securities is statistically significant at the 5% level.

27 See ACLI, AII, Brean Capital 1, SIFMA, and SIFMA AMG.

28 As set forth more fully in the original filing, FINRA noted that the proposal is informed by the TMPG best practices. See 80 FR 63603, 63605.

29 See ACLI, BDA, Brean Capital 1, Coastal, and SIFMA.

Transactions. Coastal suggested that both Specified Pool Transactions and CMOs should be taken out of the proposal's scope and questioned FINRA's authority to impose the requirements. Several commenters suggested that the proposed settlement cycles set forth in the definition of Covered Agency Transactions – that is, greater than one business day between the trade date and the contractual settlement date for TBA transactions and Specified Pool Transactions, and greater than three business days for CMOs – are too short[30] and proffered alternatives such as a specified settlement cycle for TBA transactions of three days or greater, on grounds that transactions settling within three days present minimal risk,[31] or a specified cycle based on the SIFMA monthly settlement dates,[32] or, for Specified Pool Transactions, a specified cycle of three or more business days.[33]

In response, other than with respect to multifamily and project loan securities, as discussed above, FINRA does not propose to modify the proposed rule's application to Covered Agency Transactions as set forth in the original filing. Further, FINRA does not propose to modify the specified settlement periods as set forth in the Covered Agency Transactions definition. With respect to FINRA's authority, in the original filing FINRA noted that the rule change is consistent with the provisions of Section 15A(b)(6) of the Securities Exchange Act.[34] FINRA noted, as set forth more fully in the original filing, that the proposed margin requirements will likely impose direct and indirect costs, including direct costs of compliance with the requirements and indirect costs resulting from changed market behavior of some participants, which may impact liquidity in the market.[35] Though FINRA shares commenters' concerns regarding such potential effects, the proposed requirements are needed because the unsecured credit exposures that exist in the TBA market today can lead to financial losses by members. In this regard, FINRA noted that the TBA market has potential for a significant amount of volatility,[36] and that

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30 See ACLI, BDA, ICI, Matrix, Robert Baird, and SIFMA.

31 See ICI.

32 See ACLI.

33 See Robert Baird.

34 See 80 FR 63603, 63609. Section 15A(b)(6) 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.

35 See 80 FR 63603, 63611.

36 See 80 FR 63603, 63616. ACLI suggested that FINRA had conceded in the original filing that the TBA market seems to respond only slightly to the volatility in the U.S. interest rate environment. In response, this only partially states the tenor of FINRA's analysis, which, again, noted that price movements in the TBA

permitting counterparties to participate in the TBA market, in the absence of the proposed requirements, can facilitate increased leverage by customers, thereby posing risk to the member extending credit and to the marketplace and potentially imposing, in economic terms, negative externalities on the financial system in the event of failure.[37] As such, to assert that there has been no or limited degradation in the TBA market does not of itself demonstrate that there is no credit risk in this market.[38]

In the original filing, FINRA discussed how it had considered, among other things, various options for narrowing the scope of Covered Agency Transactions or extending the specified settlement cycles.[39] As FINRA noted, the Federal Reserve Bank of New York ("FRBNY") staff advised FINRA that such modifications to the proposal would result in a mismatch between FINRA standards and the TMPG best practices, thereby resulting in perverse incentives in favor of non-margined products and leading to distortions of trading behavior, including clustering of trades around the specified settlement cycles in an effort to avoid margin expenses.[40] Further, in response to comments on the proposal as it had been published for comment in Regulatory Notice 14-02,[41] FINRA engaged in extensive discussions with industry participants and other regulators, including staff of the SEC and the FRBNY, and engaged in analysis of the potential economic impact of the proposal.[42] FINRA made revisions to the proposal to ameliorate its impact on business activity and to address the concerns of smaller customers that do not pose material risk to the market as a whole, in particular those engaging in non-margined, cash account business. These revisions included, among other things, the establishment of the exception from the proposed margin requirements for any counterparty with gross open positions amounting to $2.5 million or less, subject to specified conditions, as well as specified exceptions to the maintenance margin requirement and modifications to the proposal's de minimis transfer provisions.[43] As

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market over the past five years suggest the market has potential for significant volatility.

37 See 80 FR 63603, 63615 through 63616.

38 See 80 FR 63603, 63613.

39 See 80 FR 63606, 63615.

40 See 80 FR 63606, 63614 through 63615.

41 Regulatory Notice 14-02 (January 2014) (Margin Requirements: FINRA Requests Comment on Proposed Amendments to FINRA Rule 4210 for Transactions in the TBA Market).

42 See 80 FR 63603, 63605.

43 See 80 FR 63603, 63605. Commenters expressed concerns regarding these exceptions as set forth in the original filing. Commenters' concerns, and FINRA's response, are addressed more fully below.

such, FINRA reiterates its view that narrowing the scope of Covered Agency Transactions or modifying the proposed settlement cycles in the fashion suggested by commenters would undermine the rule's fundamental purpose of improving counterparty risk management and, further, that the revisions made to the proposal, as described in the original filing, will ameliorate its impact.

C. Maintenance Margin

As set forth more fully in the original filing, non-exempt accounts[44] would be required to post two percent maintenance margin plus any net mark to market loss on their Covered Agency Transactions.[45] Commenters opposed the maintenance margin requirement and expressed concerns about the proposed requirement's impact and efficacy.[46] SIFMA AMG said that the requirement would disproportionately affect small to medium-sized participants and would exacerbate risks by not requiring that the margin be segregated and held at a non-affiliated custodian. BDA similarly expressed concern that the requirement would disadvantage small dealers. SIFMA said that the requirement would have the effect of requiring maintenance margin from medium-sized firms, rather than small or large firms, and that the requirement would create complexity for members

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44 The term "exempt account" is defined under FINRA Rule 4210(a)(13). Broadly, an exempt account means a FINRA member, non-FINRA member registered broker-dealer, account that is a "designated account" under FINRA Rule 4210(a)(4) (specifically, a bank as defined under SEA Section 3(a)(6), a savings association as defined under Section 3(b) of the Federal Deposit Insurance Act, the deposits of which are insured by the Federal Deposit Insurance Corporation, an insurance company as defined under Section 2(a)(17) of the Investment Company Act, an investment company registered with the Commission under the Investment Company Act, a state or political subdivision thereof, or a pension plan or profit sharing plan subject to the Employee Retirement Income Security Act or of an agency of the United States or of a state or political subdivision thereof), and any person that has a net worth of at least $45 million and financial assets of at least $40 million for purposes of paragraphs (e)(2)(F) and (e)(2)(G) of the rule, as set forth under paragraph (a)(13)(B)(i) of Rule 4210, and meets specified conditions as set forth under paragraph (a)(13)(B)(ii). As set forth more fully in the original filing, FINRA is proposing a conforming revision to paragraph (a)(13)(B)(i) so that the phrase "for purposes of paragraphs (e)(2)(F) and (e)(2)(G)" would read "for purposes of paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H)." See 80 FR 63603, 63606; see also proposed FINRA Rule 4210(a)(13)(B)(i) in Exhibit 5.

45 See 80 FR 63603, 63607 through 63608.

46 See AII, Robert Baird, BDA, Matrix, SIFMA, and SIFMA AMG. Some commenters expressed concern as to the operational feasibility of the rule's proposed exception to the maintenance margin requirement. These comments, and FINRA's response, are addressed more fully below.

by requiring that maintenance margin be calculated on a transaction by transaction basis. Matrix also expressed the concern that the requirement would impact medium-sized firms and suggested that FINRA should consider a tiered maintenance margin requirement for trades under a defined gross dollar amount. Robert Baird said that the requirement should be eliminated. AII suggested that the TMPG best practices do not have a maintenance margin requirement, which would create opportunity for regulatory arbitrage. AII said that the accounts that would be subject to the requirement are too small to create systemic risk.

In response, FINRA does not propose to modify the maintenance margin requirement. Maintenance margin is a mainstay of margin regimes in the securities industry, and as such the need to appropriately track transactions should be well understood to market participants. FINRA is sensitive to commenters' concerns as to the potential impact of the requirement on members and their non-exempt customer accounts. For this reason, as set forth more fully in the original filing and as discussed further below, FINRA revised the proposal to include an exception tailored to customers engaging in non-margined, cash account business. FINRA noted that the requirement is designed to be aligned to the potential risk in this area and that the two percent amount approximates rates charged for corresponding products in other contexts.[47]

D. "Cash Account" Exceptions

As set forth more fully in the original filing, the proposed margin requirements would not apply to any counterparty that has gross open positions[48] in Covered Agency Transactions with the member amounting to $2.5 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a Delivery Versus Payment ("DVP") basis or for cash. Similarly, a non-exempt account would be excepted from the rule's proposed two percent maintenance margin requirement if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and the customer regularly settles its Covered Agency Transactions on a DVP basis or for cash. The rule uses parallel language with respect to both of these exceptions to provide that they are not available to a counterparty that, in its transactions with the member,

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47 See 80 FR 63603, 63616.

48 Paragraph (e)(2)(H)(i)e. of the rule defines "gross open position" to mean, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty's contracts with the member and which the counterparty intends to deliver. See Exhibit 5 in this Partial Amendment No. 1.

engages in dollar rolls, as defined in FINRA Rule 6710(z),[49] or "round robin"[50] trades, or that uses other financing techniques for its Covered Agency Transactions. FINRA noted that these exceptions are intended to address the concerns of smaller customers engaging in non-margined, cash account business.[51]

Commenters expressed concern that the cash account exceptions are difficult to implement operationally and are in need of further guidance.[52] These commenters suggested that the term "regularly settles" is ambiguous and vague, that members may find it too difficult to comply with the requirement and may therefore choose not to make the cash account exceptions available to their customers, that the references to dollar rolls, round robin trades and other financing techniques should be removed to make the cash account exceptions more accessible, or that the rule should permit members to rely on representations counterparties make where activity away from the member firm is involved. SIFMA sought guidance as to whether it would suffice if the member has a reasonable expectation of the customer's behavior based on the customer's prior history of physical settlement. SIFMA AMG sought guidance as to the scope of the term "other financing techniques" and whether, for instance, a customer's engaging in a single dollar roll or round robin trade would make the cash account exceptions unavailable.

In response, FINRA does not propose to modify the cash account exceptions as proposed in the original filing. Given that the purpose of the exceptions is to help ameliorate the proposal's impact on smaller customers, it is not FINRA's intention that the exceptions should be onerous to implement. FINRA believes that, as worded, the term "regularly settles" is sufficient to convey that the rule's intent is to provide scope for flexibility on members' part as to how they implement the exceptions. FINRA expects that members are in a position to make reasonable judgments as to the observed pattern and course of dealing in their customers' behavior by virtue of their interactions with their customers. In this regard, FINRA believes the import of the term "other financing techniques" should be clear as a matter of plain language, that is, transactions other than

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[49] FINRA Rule 6710(z) defines "dollar roll" to mean a simultaneous sale and purchase of an Agency Pass-Through MBS for different settlement dates, where the initial seller agrees to take delivery, upon settlement of the re-purchase transaction, of the same or substantially similar securities.

[50] Paragraph (e)(2)(H)(i)i. defines "round robin" trade to mean any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer. See Exhibit 5 in this Partial Amendment No. 1.

[51] See 80 FR 63603, 63605. For convenience, the $2.5 million and maintenance margin exceptions are referred to as the "cash account" exceptions for purposes of this Partial Amendment No. 1.

[52] See Robert Baird, BDA, Credit Suisse, Matrix, SIFMA, and SIFMA AMG.

on a DVP basis or for cash suggest the use of financing. FINRA does not expect that a customer that engages in a single dollar roll or round robin trade would be denied access to the exceptions provided the member can reasonably demonstrate a regular pattern by that customer of settling its Covered Agency Transactions on a DVP basis or for cash. In so doing, a member may use the customer's history of transactions with the member, as well as any other relevant information of which the member is aware. Further, FINRA believes that members should be able to rely on the reasonable representations of their customers where necessary for purposes of this requirement. FINRA welcomes further discussion with industry participants on this issue, and will consider issuing further guidance as needed.

E. Two-Way (Bilateral) Margin

Several commenters suggested that the proposed rule should require the posting of two-way or bilateral margin in Covered Agency Transactions, so that members and their counterparties in such transactions would both post and receive margin.[53] These commenters suggested that two-way margin is necessary to reduce risk effectively given the exposure of the parties and that two-way margin is standard in other contexts. SIFMA suggested that the TMPG encourages firms to engage in two-way margining and that FINRA should express support for firms that do so.

In response, in the original filing FINRA noted its support for the use of two-way margining as a means of managing risk.[54] However, FINRA does not propose to address such a requirement at this time as part of the proposed rule change. FINRA welcomes further dialogue with industry participants on this issue.

F. $2.5 Million Gross Open Position Amount and the $250,000 De Minimis Transfer Amount

As discussed above, the proposed rule sets forth an exception from the proposed margin requirements for counterparties whose gross open positions in Covered Agency Transactions with the member amount to $2.5 million or less in aggregate, as specified by the rule. As set forth more fully in the original filing, the proposed rule also sets forth, for a single counterparty, a $250,000 de minimis transfer amount up to which margin need not be collected or charged to net capital, as specified by the rule.[55] SIFMA AMG suggested that the $2.5 million amount is too low and that FINRA should provide guidance as to treatment of accounts that fluctuate in the approximate range of that amount. SIFMA and BDA suggested a $10 million exception for gross open positions. As to the $250,000 de minimis transfer amount, ACLI, ICI and SIFMA suggested increasing the amount to $500,000. SIFMA expressed concern that members would end

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[53] See ACLI, AII, CoBank, Crain, ICI, SIFMA AMG, and Sutherland.

[54] See 80 FR 63603, 63619 through 63620.

[55] See 80 FR 63603, 63608.

up needing to monitor the $250,000 amount even though it would benefit few if any customers. SIFMA further suggested that the rule should grandfather existing agreements that already provide for $500,000 de minimis transfer amounts. ICI suggested $500,000 is appropriate because that amount is used in other regulatory contexts. BDA suggested raising the de minimis transfer amount to $1 million. CoBank, SIFMA AMG and Sutherland suggested that the rule should permit parties to negotiate higher thresholds. Crain suggested the $250,000 de minimis transfer amount would not be sufficient for participants in the multifamily market.

In response, FINRA does not propose to alter the $2.5 million amount for gross open positions and does not propose to alter the $250,000 de minimis transfer amount. As discussed in the original filing, FINRA believes that these amounts are appropriately tailored to smaller accounts that are less likely to pose systemic risk.[56] FINRA believes that increasing the thresholds would undermine the rule's purpose. In that regard, permitting parties to negotiate higher thresholds by separate agreement, whether entered into before the rule takes effect or afterwards, would only serve to cut against the rule's objectives. FINRA does not propose to alter the de minimis transfer amount on account of multifamily securities transactions given that, as discussed above, FINRA is amending the rule so that members may elect not to apply the proposed margin requirements to multifamily and project loan securities, subject to specified conditions.

G. Timing of Margin Collection and Position Liquidation

As set forth more fully in the original filing, the proposed rule provides that, with respect to exempt accounts, if a mark to market loss, or, with respect to non-exempt accounts, a deficiency, is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member must deduct the amount of the mark to market loss or deficiency from net capital as provided in SEA Rule 15c3-1. Further, unless FINRA has specifically granted the member additional time, the member is required to liquidate positions if, with respect to exempt accounts, a mark to market loss is not satisfied within five business days, or, with respect to non-exempt accounts, a deficiency is not satisfied within such period.[57] Commenters expressed concerns that the proposed rule's time frame for collection of the mark to market loss or deficiency (that is, margin collection) and the time frame for liquidation are too onerous, that longer periods should be permitted as the five-day liquidation period is not sufficient to resolve various issues that may arise, that parties should be permitted to set the applicable time frames in a Master Securities Forward Transaction Agreement ("MSFTA") or other agreement, and that the time frames do not align with the 15 days permitted under FINRA Rule 4210(f)(6) or other market conventions.[58] SIFMA and SIFMA AMG suggested that the "T+1" margin call would

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[56] See 80 FR 63603, 63616 through 63617.

[57] See 80 FR 63603, 63607 through 63608.

[58] See ACLI, AII, BDA, SIFMA, and SIFMA AMG.

raise operational issues. BDA suggested that the capital charge should apply five days after the initial margin call. ICI suggested FINRA should allow firms to take a capital charge in lieu of collecting margin. AII suggested that allowing dealers to take a capital charge is a suitable practice to address margin delivery fails and that the forced liquidation requirement should be eliminated.

In response, FINRA does not propose to modify the timing for margin collection and position liquidation as set forth in the proposed rule change. With respect to position liquidation, while it is true that longstanding language under FINRA Rule 4210(f)(6) sets forth a 15-day period, more recent requirements adopted under the portfolio margin rules, which have been in widespread use among members, set forth a three-day time frame.[59] FINRA believes that, with respect to Covered Agency Transactions, the five-day period should provide sufficient time for members to resolve issues. Further, as FINRA noted in the original filing, FINRA believes the five-day period is appropriate in view of the potential counterparty risk in the TBA market.[60] Consistent with longstanding practice under FINRA Rule 4210(f)(6), the proposed rule allows FINRA to specifically grant the member additional time. FINRA maintains, and regularly updates, the Regulatory Extension System for this purpose. FINRA welcomes further discussion with industry participants on this issue. With respect to the timing of margin collection, FINRA notes that the proposed language "by the close of business on the next business day after the business day" on which the market to market loss or deficiency arises is consistent, again, with language under the portfolio margin rules, which are well understood by members.[61] FINRA does not believe it is appropriate to revise the proposed rule to permit members to take a capital charge in lieu of collecting margin. FINRA notes that taking a capital charge, of itself, does not suffice to address counterparty risk, which is a key purpose of the proposed rule change. Further, FINRA believes that only requiring capital charges would render the rule without effect. FINRA does not believe it is appropriate to eliminate the liquidation requirement given that the requirement is intended to mitigate risk.

H. Concentration Limits

As set forth more fully in the original filing, under current (pre-revision) paragraph (e)(2)(H) of the rule, a member must provide written notification to FINRA and is prohibited from entering into any new transactions that could increase credit exposure if net capital deductions, over a five day period, exceed: (1) for a single account or group of commonly controlled accounts, five percent of the member's tentative net capital; or (2) for all accounts combined, 25 percent of the member's tentative net

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59 See FINRA Rule 4210(g)(9) and FINRA Rule 4210(g)(10).

60 See 80 FR 63603, 63619.

61 See FINRA Rule 4210(g)(10)(B).

capital.[62] BDA and SIFMA suggested that the five percent threshold should be raised to 10 percent so as to take account of the impact of the proposal. In response, FINRA does not propose to revise the five percent threshold. FINRA noted in the original filing that both the five percent and the 25 percent thresholds are currently in use and are designed to address aggregate risk in this area. FINRA noted that if the thresholds are easily reached in volatile markets, then that would suggest the thresholds serve an important purpose in monitoring risk.

I. Mortgage Bankers

As set forth more fully in the original filing, the proposed rule provides that members may treat mortgage bankers that use Covered Agency Transactions to hedge their pipeline of commitments as exempt accounts for purposes of paragraph (e)(2)(H) of the rule.[63] Proposed Supplementary Material .02 of the rule provides that members must adopt written procedures to monitor the mortgage banker's pipeline of mortgage loan commitments to assess whether the Covered Agency Transactions are being used for hedging purposes.[64] MBA suggested that, in addition to excepting mortgage bankers from treatment as non-exempt accounts if they hedge their pipeline of commitments, and thereby excepting them from the maintenance margin requirements that would otherwise apply, FINRA should also except mortgage bankers from the mark to market (also referred to as variation) margin requirements that would apply to exempt accounts. MBA suggested that mortgage bankers function as "end users" that should not be unduly burdened by mandatory transaction rules, that requiring variation margin would distort the mortgage finance markets, and that hedging transactions by mortgage brokers do not represent a systemic risk. MBA said that FINRA had not done sufficient economic analysis as to the rule's impact on mortgage bankers. BDA, Matrix, SIFMA, and Sandler O'Neill said that FINRA should clarify what level of diligence members need to apply to determine whether a mortgage banker is hedging its pipeline of commitments and thereby eligible to be treated as an exempt account. Commenters sought guidance as to whether for example members may comply by obtaining representations or certifications from the mortgage bankers.

In response, as FINRA noted in the original filing, the type of monitoring set forth in the proposed rule is not a wholly new requirement. The current Interpretations under Rule 4210 already contemplate that members evaluate the loan servicing portfolios of specified counterparties that are being treated as exempt accounts.[65] FINRA believes it is

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62 See 80 FR 63603, 63618. Under the proposed rule change, current paragraph (e)(2)(H) would be redesignated as paragraph (e)(2)(I).

63 See 80 FR 63603, 63607.

64 See proposed FINRA Rule 4210.02 in Exhibit 5 of this Partial Amendment No. 1.

65 See Interpretation /02 of FINRA Rule 4210(e)(2)(F); see also 80 FR 63603, 63607. The Interpretation cites, in part, such factors as loan balance, servicing fee,

sound practice that members have written procedures to monitor the portfolios of mortgage bankers that are being treated as exempt accounts. As discussed earlier with respect to the cash account exceptions, FINRA believes that members should be able to rely on the reasonable representations of their mortgage banker customers where necessary for purposes of this requirement. FINRA welcomes further discussion with industry participants on this issue, and will consider issuing further guidance as needed. FINRA does not propose to modify the proposal to except mortgage bankers from the mark to market requirements, such as by creating an "end user" or other similar type of exception, as doing so would undermine the rule's purpose by excepting a major category of participant in the market. FINRA believes that such an exception would create incentives that would distort trading behavior, which could increase the risk of member firms and their customers. As discussed in Section B above, and as further discussed below, FINRA has noted that the proposed rule change will likely impose direct and indirect costs, which may lead to decreased liquidity in the market.[66] However, FINRA has noted the need for the rule change given the potential for risk in this market.[67]

In response to MBA's suggestion that FINRA did not do sufficient economic analysis as to the rule's impact on mortgage bankers, FINRA notes the following. First, MBA stated that FINRA's analysis consisted of a cursory examination of the TBA market over a short period of time using data from one broker-dealer across 35 days leading up to and including May 30, 2014. In response, FINRA notes that this interpretation of the data used in the analysis is not accurate; the sample period is not 35 days and the data do not contain the open positions of a single broker-dealer. To estimate the potential burden on mortgage bankers, FINRA analyzed data provided by a major clearing broker. This dataset contained 5,201 open transactions as of May 30, 2014 in 375 customer (including mortgage banker) accounts at 10 broker-dealers. These open transactions were created between October 18, 2013 and May 30, 2014, with approximately 60% created in May 2014. Based on FINRA's discussions with the clearing broker, FINRA believes that the sample is a good representation of typical exposures. These open positions would require posting margin on 35 days throughout the sample, corresponding to less than 0.01% of the 14,001 account-day combinations.

Second, MBA suggested that FINRA's analysis did not control the results of its study against typical market volatility, against the expected withdrawal of the Federal Reserve as an active buyer of TBA-eligible MBS or even to follow its sample data through other periods throughout 2014. However, as discussed in the original filing, FINRA analyzed the relation between interest rate volatility and the volatility in the TBA market by comparing the volatility of Deutsche Bank's TBA index in two different

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remaining life of the loan, probability of loan survival, delinquency rate, geographic relationships, cost of foreclosure and servicing costs.

66 See 80 FR 63606, 63611.

67 See note 36 supra.

interest rate regimes based on 10-year U.S. Treasury yields and found no significant change across the two periods.[68] FINRA acknowledged that the Federal Reserve (specifically, the FRBNY) is a major market participant in the TBA market.[69] The withdrawal of FRBNY as an active buyer would have a significant impact on the market, unless other market participants increase their activities or new participants choose to enter the market. FINRA discussed this potential impact in the original filing.[70]

Third, MBA suggested that FINRA's analysis did not appear to evaluate the financial and other costs the proposed rule change would impose on mortgage bankers and borrowers and that FINRA did not evaluate the impact to consumers and other borrowers resulting from an increase in mortgage rates and reduction in competition that would arise due to the proposed rule change. MBA suggested that the proposed rule change will harm borrowers by limiting their access to credit, and that requiring mortgage bankers to divert their liquidity from origination for margin calls imposes an acute liquidity risk on mortgage bankers. In response, as discussed earlier, FINRA acknowledged in the original filing the potential impact of the proposed rule change on market behavior of participants and noted that "[s]ome parties who currently transact in the TBA market may choose to withdraw from or limit their participation in the TBA market. Reduced participation may lead to decreased liquidity in the market for certain issues or settlement periods, potentially restricting access to end users and increasing costs in the mortgage market."[71] However, FINRA noted that the impact on access to credit would be limited if new participants choose to enter the market to offset the impact of participants that exit the market. Further, in light of the importance of the role of mortgage bankers in the mortgage finance market, FINRA noted in the original filing that the proposed rule change has accommodated the business of mortgage bankers by including provision for members to treat mortgage bankers as exempt accounts with respect to their hedging, subject to specified conditions.[72]

Fourth, MBA suggested that FINRA neglected to analyze the impact of mortgage bankers being forced to switch from mandatory to best efforts delivery commitments in the process forsaking significant amounts of their gain on sale or limiting their competitiveness in various products. In response, FINRA has no basis to believe that the margin requirement would force mortgage bankers to switch from mandatory execution basis to best efforts execution. FINRA expects that the majority of the mortgage bankers' positions would be excepted from the proposed margin requirements, and market competition would maintain the origination of loans to the borrowers.

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[68] See 80 FR 63603, 63614.

[69] See note 73 at 80 FR 63603, 63610.

[70] See 80 FR 63603, 63614.

[71] See 80 FR 63603, 63611.

[72] See 80 FR 63603, 63612.

J. Risk Limit Determinations

SIFMA sought clarification as to whether paragraphs (e)(2)(F), (e)(2)(H) and (e)(2)(G) of the rule require a member to write a separate risk limit determination for the types of products addressed by each of those paragraphs for each counterparty. In response, FINRA notes that one written risk limit determination, for each counterparty, should suffice, provided it addresses the products. As set forth more fully in the original filing, FINRA notes that the proposed risk limit language in paragraphs (e)(2)(F) and (e)(2)(G) is drawn from language that appears under current, pre-revision paragraph (e)(2)(H) and which currently, by its terms, already applies to both paragraphs (e)(2)(F) and (e)(2)(G).

K. Advisory Clients of Registered Investment Advisers

As set forth more fully in the original filing, proposed Supplementary Material .05 requires in part that, for purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G), or (e)(2)(H) of Rule 4210, if a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level, except with respect to any account or group of commonly controlled accounts whose assets managed by that investment adviser constitute more than 10 percent of the investment adviser's regulatory assets under management as reported on the investment adviser's most recent Form ADV.[73] Credit Suisse sought clarification as to whether the 10 percent threshold may be calculated as of the time of the credit review under the member's written risk analysis policy and procedures. SIFMA suggested that the 10 percent threshold is not necessary and FINRA should clarify whether the 10 percent goes to the commonly controlled accounts at the member firm. Sandler O'Neill requested guidance as to whether it would be permissible for the member to collect aggregated margin in a single account, given that the investment adviser may be contractually prohibited from disclosing details about customers in the sub-accounts.

In response, FINRA believes it is consistent with the rule's intent that the 10 percent threshold may be calculated as of the time of the member's credit review pursuant to its written risk policies and procedures.[74] FINRA expects that the 10 percent

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73 See 80 FR 63603, 63606, 63617 through 63618; see also proposed FINRA Rule 4210.05 in Exhibit 5 of this Partial Amendment No. 1.

74 The proposed rule is not intended to prescribe specific intervals at which a member would need to review risk limit determinations. However, FINRA notes that, with respect to risk limit determinations pursuant to the proposed rule, proposed Rule 4210.05(a)(4) provides that a member shall consider whether the margin required pursuant to the rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements. FINRA believes members should be mindful, in the conduct of their business, of the need to revisit risk limit determinations as

would be as to accounts of which the member is aware by virtue of the member's relationship with the investment adviser. As noted in the original filing, FINRA believes the 10 percent threshold is appropriate given that accounts above that threshold pose a higher magnitude of risk.[75] FINRA believes that the rule does not prevent a member from aggregating margin, provided the member observes all applicable requirements under SEC and FINRA rules.

L. Sovereign Entities

As set forth more fully in the original filing, the proposed rule provides that, with respect to Covered Agency Transactions with any counterparty that is a federal banking agency, as defined in 12 U.S.C. 1813(z),[76] central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of the proposed rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.[77] SIFMA and SIFMA AMG said that sovereign wealth funds should be included among the entities with respect to which a member may elect not to apply the proposed margin requirements. SIFMA said that FINRA should consider the credit profile of sovereign wealth funds rather than whether they are commercial participants. In response, FINRA does not propose to make the suggested modification. The proposed exception is designed specifically for selected sovereign entities performing the functions of governments. As commercial participants in the market, sovereign wealth funds are subject to risk. As noted in the original filing, FINRA believes that to include sovereign wealth funds within the parameters of the proposed exception would create perverse incentives for regulatory arbitrage.[78]

M. Federal Home Loan Banks and Farm Credit Banks

Sutherland, on behalf of the Federal Home Loan Banks ("FHLB"), and CoBank, on behalf of the Farm Credit Banks ("FCB"), requested that FINRA amend the rule so that members would have discretion to except FHLB and FCB from the proposed margin requirements. FHLB requested that, in the alternative, a member should be permitted

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appropriate. See proposed Rule 4210.05(a)(4) in Exhibit 5 in this Partial Amendment No. 1.

[75] See 80 FR 63603, 63617 through 63618.

[76] 12 U.S.C. 1813(z) defines federal banking agency to mean the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, or the Federal Deposit Insurance Corporation.

[77] See 80 FR 63603, 63606.

[78] See 80 FR 63603, 63619.

discretion to except FHLB from the proposed margin requirements when the Covered Agency Transactions are entered into for the purpose of hedging risk. The commenters suggested further that the rule should provide for a member's counterparty to have the right to segregate any margin posted with a FINRA member with an independent third-party custodian. In response, FINRA does not propose to make the requested modifications to the proposed rule. The requested exceptions would undermine the rule's purpose of reducing risk. With respect to third-party custodial arrangements, FINRA believes these are best addressed in separate rulemaking or guidance, as appropriate. FINRA welcomes further discussion of these issues.

N. Other Comments

Several commenters expressed concerns, as set forth below, that FINRA believes raise issues that are outside the scope of the proposed rule change. As such, in response, FINRA does not propose any revisions to the proposed rule change. However, FINRA welcomes further discussion of these issues.

- BDA, Sandler O'Neill and SIFMA said that the proposed rule change should address the responsibilities of introducing and clearing firms, including such issues as assignment of responsibility for capital charges to one party versus the other for purposes of FINRA Rule 4311 when engaging in Covered Agency Transactions. FINRA notes that the proposed rule change is not intended to address issues under Rule 4311.

- SIFMA AMG said FINRA should work with international regulators to harmonize the proposed requirements with other regulatory regimes. As noted above, FINRA believes this is outside the scope of the proposed rule change.

- Matrix and BDA said that smaller and medium firms may find it difficult to develop in-house systems to comply with the proposed rule change. Matrix requested that FINRA clarify that members may utilize third-party providers to assist with their compliance. Broadly, FINRA believes third-party service providers should be permissible provided the member complies with all applicable rules and guidance, including, among other things, the member's obligations under FINRA Rule 3110 and as described in Notice to Members 05-48 (July 2005) (Outsourcing).

- Brean Capital said that FINRA should coordinate the rule change with the former Mortgage-Backed Securities Clearing Corporation, now part of the Fixed Income Clearing Corporation.[79] As noted above, FINRA believes this is outside the scope of the proposed rule change.

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[79] See Brean Capital 2.

- SIFMA and SIFMA AMG said that FINRA should provide guidance that would permit collective investment trusts, common trust funds or collective trust funds to be treated as exempt accounts. SIFMA AMG further said that foreign institutions should be recognized as exempt accounts. Credit Suisse suggested FINRA should confirm that an omnibus account maintained by an investment adviser may be classified as an exempt account based on the assets under management in the account and a risk analysis conducted at the investment adviser level. FINRA notes that, other than for purposes of one conforming revision, as set forth in the original filing,[80] the proposed rule change is not intended to revisit the definition of exempt accounts for the broader purposes of Rule 4210.

O. Implementation Period

Commenters said that considerable operational and systems work will be needed to comply with the proposed rule change, including changes to or renegotiation of MSFTA documentation and other agreements.[81] These commenters suggested that firms should be permitted 18 months to two years to prepare for implementation of the proposed rule change.

In response, FINRA believes that a phased implementation should be appropriate. FINRA proposes that the risk limit determination requirements as set forth in paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H) of Rule 4210 and proposed Supplementary Material .05 of the rule become effective six months from the date the proposed rule change is approved by the Commission. FINRA proposes that the remainder of the proposed rule change become effective 18 months from the date the proposed rule change is approved by the Commission.

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[80] See 80 FR 63603, 63606.

[81] See ACLI, AII, BDA, Credit Suisse, ICI, Robert Baird, Sandler O'Neill, SIFMA, and SIFMA AMG.

EXHIBIT 2

Alphabetical List of Written Comments

Form Letter Comments: The Commission received 50 comments using Letter Type A and 4 comments using Letter Type B.

Individual Comments:

1. Margaret Allen, AGM Financial ("AGM") (November 10, 2015)

2. Paul J. Barrese, Sandler O'Neill & Partners, L.P. ("Sandler O'Neill") (November 10, 2015)

3. Doug Bibby and Doug Culkin, National Multifamily Housing Council and National Apartment Association ("NMHC"/"NAA") (November 10, 2015)

4. David W. Blass, Investment Company Institute ("ICI") (November 9, 2015)

5. Robert Cahn, Prudential Mortgage Capital Company, LLC ("Prudential Mortgage") (November 10, 2015)

6. James M. Cain, Sutherland Asbill & Brennan LLP ("Sutherland") (November 10, 2015") (on behalf of the Federal Home Loan Banks)

7. Timothy W. Cameron, Esq. and Laura Martin, Securities Industry and Financial Markets Association, Asset Management Group ("SIFMA AMG") (November 10, 2015)

8. Jonathan S. Camps, Love Funding ("Love Funding") (November 9, 2015)

9. Richard A. Carlson, Davis-Penn Mortgage Co. ("Davis-Penn 1") (November 9, 2015)

10. Michael S. Cordes, Columbia-National Real Estate Finance, LLC ("Columbia") (November 9, 2015)

11. Carl E. Corrado, Great Lakes Financial Group, LP ("Great Lakes") (January 4, 2016)

12. Daniel R. Crain, Crain Mortgage Group LLC ("Crain") (November 6, 2015)

13. James F. Croft, Red Mortgage Capital, LLC ("Red Mortgage") (November 10, 2015)

14. Dan Darilek, Davis-Penn Mortgage Co. ("Davis-Penn 2") (November 9, 2015)

15. Jayson F. Donaldson, NorthMarq Capital Finance, L.L.C ("NorthMarq") (November 10, 2015)

16. Robert B. Engel, CoBank, ACB (“CoBank”) (November 10, 2015) (on behalf of the Farm Credit Banks)

17. Robert M. Fine, Brean Capital, LLC (“Brean Capital 1”) (November 10, 2015)

18. Tari Flannery, M&T Realty Capital Corporation (“M&T Realty”) (November 9, 2015)

19. Bernard P. Gawley, The Ziegler Financing Corporation (“Ziegler”) (November 10, 2015)

20. John R. Gidman, Association of Institutional INVESTORS (“AII”) (November 10, 2015)

21. Keith J. Gloeckl, Churchill Mortgage Investment LLC (“Churchill”) (November 6, 2015)

22. Eileen Grey, Mortgage Bankers Association & Others (“MBA & Others 1”) (October 29, 2015)

23. Eileen Grey, Mortgage Bankers Association & Others (“MBA & Others 2”) (November 10, 2015)

24. Tyler Griffin, Dwight Capital (“Dwight”) (November 10, 2015)

25. Pete Hodo, III, Highland Commercial Mortgage (“Highland 1”) (November 5, 2015)

26. Robert H. Huntington, Credit Suisse Securities (USA) LLC (“Credit Suisse”) (November 10, 2015)

27. Matthew Kane, Centennial Mortgage, Inc. (“Centennial”) (November 9, 2015)

28. Christopher B. Killian, Securities Industry and Financial Markets Association (“SIFMA”) (November 10, 2015)

29. Robert T. Kirkwood, Lancaster Pollard Holdings, LLC (“Lancaster”) (November 10, 2015)

30. Tony Love, Forest City Capital Corporation (“Forest City 1”) (November 5, 2015)

31. Tony Love, Forest City Capital Corporation (“Forest City 2”) (November 10, 2015)

32. Anthony Luzzi, Sims Mortgage Funding, Inc. (“Sims Mortgage”) (November 9, 2015)

33. Diane N. Marshall, Prairie Mortgage Company (“Prairie Mortgage”) (November 10, 2015)

34. Matrix Applications, LLC (“Matrix”) (November 10, 2015)

35. Douglas I. McCree, CMB, First Housing ("First Housing") (November 10, 2015)

36. Michael McRoberts, DUS Peer Group ("DUS") (November 2, 2015)

37. Chris Melton, Coastal Securities ("Coastal") (November 9, 2015)

38. John O. Moore Jr., Highland Commercial Mortgage ("Highland 2") (November 6, 2015)

39. Dennis G. Morton, AJM First Capital, LLC ("AJM") (November 10, 2015)

40. Michael Nicholas, Bond Dealers of America ("BDA") (November 10, 2015)

41. Lee Oller, Draper and Kramer, Incorporated ("Draper") (November 10, 2015)

42. Roderick D. Owens, Committee on Healthcare Financing ("CHF") (November 6, 2015)

43. Jose A. Perez ("Perez") (November 9, 2015)

44. David F. Perry, Century Health Capital, Inc. ("Century") (November 9, 2015)

45. Deborah Rogan, Bellwether Enterprise Real Estate Capital, LLC ("Bellwether") (November 10, 2015)

46. Bruce Sandweiss, Gershman Mortgage ("Gershman 1") (November 18, 2015)

47. Craig Singer and James Hussey, RICHMAC Funding LLC ("Richmac") (November 9, 2015)

48. David H. Stevens, Mortgage Bankers Association ("MBA") (November 10, 2015)

49. David H. Stevens, Mortgage Bankers Association ("MBA Supplemental Comments") (January 11, 2016)

50. Stephen P. Theobald, Walker & Dunlop, LLC ("W&D") (November 10, 2015)

51. Robert Tirschwell, Brean Capital, LLC ("Brean Capital 2") (November 10, 2015)

52. Mark C. Unangst, Gershman Mortgage ("Gershman 2") (November 23, 2015)

53. Charles M. Weber, Robert W. Baird & Co. Incorporated ("Robert Baird") (November 10, 2015")

54. Steve Wendel, CBRE, Inc. ("CBRE") (November 10, 2015)

55. Carl B. Wilkerson, American Council of Life Insurers ("ACLI") (November 10, 2015)

EXHIBIT 4

Exhibit 4 shows the changes proposed in this Partial Amendment No. 1, with the proposed changes in the original filing shown as if adopted. Proposed new language in this Partial Amendment No. 1 is underlined; proposed deletions in this Partial Amendment No. 1 are in brackets.

* * * * *

4000. FINANCIAL AND OPERATIONAL RULES

* * * * *

4210. Margin Requirements

(a) through (d) No Change.

(e) Exceptions to Rule

The foregoing requirements of this Rule are subject to the following exceptions:

(1) No Change.

(2) Exempted Securities, Non-equity Securities and Baskets

(A) through (G) No Change.

(H) Covered Agency Transactions

(i) No Change.

(ii) Margin Requirements for Covered Agency Transactions

a. All Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, shall be subject to the provisions of paragraph (e)(2)(H) of this Rule, except:

1. with respect to Covered Agency Transactions with any counterparty that is a Federal

banking agency, as defined in 12 U.S.C. 1813(z), central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b[.]; and

2. a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided:

A. such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project

Loan Certificates, as commonly known to the trade; and

B. the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.

b. through g. No Change.

(I) No Change.

* * * * *

(f) through (h) No Change.

• • • Supplementary Material: ---------------

.01 through .05 No Change.

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EXHIBIT 5

Exhibit 5 shows the text of the proposed rule change, as amended by this Partial Amendment No. 1. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

4000. FINANCIAL AND OPERATIONAL RULES

* * * * *

4210. Margin Requirements

(a) Definitions

For purposes of this Rule, the following terms shall have the meanings specified below:

(1) through (12) No Change.

(13) The term "exempt account" means:

(A) No Change.

(B) any person that:

(i) has a net worth of at least $45 million and financial assets of at least $40 million for purposes of paragraphs (e)(2)(F), [and] (e)(2)(G)[,] and (e)(2)(H), and

(ii) No Change.

(14) through (16) No Change.

(b) through (d) No Change.

(e) Exceptions to Rule

The foregoing requirements of this Rule are subject to the following exceptions:

(1) No Change.

(2) Exempted Securities, Non-equity Securities and Baskets

(A) through (E) No Change.

(F) Transactions with Exempt Accounts Involving Certain "Good Faith" Securities

Other than for Covered Agency Transactions as defined in paragraph (e)(2)(H) of this Rule, [O]on any "long" or "short" position resulting from a transaction involving exempted securities, mortgage related securities, or major foreign sovereign debt securities made for or with an "exempt account," no margin need be required and any marked to the market loss on such position need not be collected. However, the amount of any uncollected marked to the market loss shall be deducted in computing the member's net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)([H]I) [below] of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

(G) Transactions With Exempt Accounts Involving Highly Rated Foreign Sovereign Debt Securities and Investment Grade Debt Securities

On any "long" or "short" position resulting from a transaction made for or with an "exempt account" (other than a position subject to paragraph (e)(2)(F) <u>or (e)(2)(H) of this Rule</u>), the margin to be maintained on highly rated foreign sovereign debt and investment grade debt securities shall be, in lieu of any greater requirements imposed under this Rule, (i) 0.5 percent of current market value in the case of highly rated foreign sovereign debt securities, and (ii) 3 percent of current market value in the case of all other investment grade debt securities. The member need not collect any such margin, provided the amount equal to the margin required shall be deducted in computing the member's net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)([H]<u>I</u>) [below] <u>of this Rule</u>.

<u>Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(G) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.</u>

<u>**(H) Covered Agency Transactions**</u>

<u>**(i) Definitions**</u>

For purposes of paragraph (e)(2)(H) of this Rule:

a. The term "bilateral transaction" means a Covered Agency Transaction that is not cleared through a registered clearing agency as defined in paragraph (f)(2)(A)(xxviii) of this Rule.

b. The term "counterparty" means any person that enters into a Covered Agency Transaction with a member and includes a "customer" as defined in paragraph (a)(3) of this Rule.

c. The term "Covered Agency Transaction" means:

1. To Be Announced ("TBA") transactions, as defined in Rule 6710(u), inclusive of adjustable rate mortgage ("ARM") transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;

2. Specified Pool Transactions, as defined in Rule 6710(x), for which the difference between the trade date and contractual settlement date is greater than one business day; and

3. Transactions in Collateralized Mortgage Obligations ("CMOs"), as defined in Rule 6710(dd), issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-

Sponsored Enterprise, as defined in Rule 6710(n), for which the difference between the trade date and contractual settlement date is greater than three business days.

d. The term "deficiency" means the amount of any required but uncollected maintenance margin and any required but uncollected mark to market loss.

e. The term "gross open position" means, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty's contracts with the member and which the counterparty intends to deliver.

f. The term "maintenance margin" means margin equal to 2 percent of the contract value of the net "long" or net "short" position, by CUSIP, with the counterparty.

g. The term "mark to market loss" means the counterparty's loss resulting from marking a Covered Agency Transaction to the market.

h. The term "mortgage banker" means an entity, however organized, that engages in the business of

providing real estate financing collateralized by liens on such real estate.

i. The term “round robin” trade means any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer.

j. The term “standby” means contracts that are put options that trade OTC, as defined in paragraph (f)(2)(A)(xxvii) of this Rule, with initial and final confirmation procedures similar to those on forward transactions.

(ii) Margin Requirements for Covered Agency Transactions

a. All Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, shall be subject to the provisions of paragraph (e)(2)(H) of this Rule, except:

1. with respect to Covered Agency Transactions with any counterparty that is a Federal banking agency, as defined in 12 U.S.C. 1813(z), central bank, multinational central bank, foreign sovereign, multilateral development bank, or the

Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b; and

2. a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided:

A. such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade; and

B. the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.

b. A member that engages in Covered Agency Transactions with any counterparty shall make a determination in writing of a risk limit for each such counterparty that the member shall enforce. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

c. The margin requirements specified in paragraph (e)(2)(H) of this Rule shall not apply to:

1. Covered Agency Transactions that are cleared through a registered clearing agency, as defined in paragraph (f)(2)(A)(xxviii) of this Rule, and are subject to the margin requirements of that clearing agency; and

2. any counterparty that has gross open positions in Covered Agency Transactions with the member amounting to $2.5 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade

date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a Delivery Versus Payment ("DVP") basis or for "cash"; provided, however, that such exception from the margin requirements shall not apply to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in Rule 6710(z), or "round robin" trades, or that uses other financing techniques for its Covered Agency Transactions.

d. Transactions with Exempt Accounts: On any net "long" or net "short" position, by CUSIP, resulting from bilateral transactions with a counterparty that is an "exempt account" no maintenance margin shall be required. However, such transactions shall be marked to the market daily and the member shall collect any net mark to market loss, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of this Rule. If the mark to market loss is not satisfied by the close of business on the next business day after the business day on which the mark to market loss arises, the member shall be required to deduct the amount of the mark to market loss from net capital as provided in

SEA Rule 15c3-1 until such time the mark to market loss is satisfied. If such mark to market loss is not satisfied within five business days from the date the loss was created, the member shall promptly liquidate positions to satisfy the mark to market loss, unless FINRA has specifically granted the member additional time. Members may treat mortgage bankers that use Covered Agency Transactions to hedge their pipeline of mortgage commitments as exempt accounts for purposes of paragraph (e)(2)(H) of this Rule.

e. Transactions with Non-Exempt Accounts: On any net "long" or net "short" position, by CUSIP, resulting from bilateral transactions with a counterparty that is not an "exempt account," maintenance margin, plus any net mark to market loss on such transactions, shall be required margin, and the member shall collect the deficiency, as defined in paragraph (e)(2)(H)(i)d. of this Rule, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of this Rule. If the deficiency is not satisfied by the close of business on the next business day after the business day on which the deficiency arises, the member shall be required to deduct the amount of the deficiency from net capital as provided in SEA Rule 15c3-1 until such time the deficiency is satisfied. If such deficiency is not satisfied within five

business days from the date the deficiency was created, the member shall promptly liquidate positions to satisfy the deficiency, unless FINRA has specifically granted the member additional time. No maintenance margin is required if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and the customer regularly settles its Covered Agency Transactions on a DVP basis or for "cash"; provided, however, that such exception from the required maintenance margin shall not apply to a non-exempt account that, in its transactions with the member, engages in dollar rolls, as defined in Rule 6710(z), or "round robin" trades, or that uses other financing techniques for its Covered Agency Transactions.

f. Any aforementioned deficiency, as set forth in paragraph (e)(2)(H)(ii)e. of this Rule, or mark to market losses, as set forth in paragraph (e)(2)(H)(ii)d. of this Rule, with a single counterparty shall not give rise to any margin requirement, and as such need not be collected or charged to net capital, if the aggregate of such amounts with such counterparty does not exceed $250,000 ("the de minimis transfer amount"). The full amount of the sum of the

required maintenance margin and any mark to market loss must be collected when such sum exceeds the de minimis transfer amount.

g. Unrealized profits in one Covered Agency Transaction position may offset losses from other Covered Agency Transaction positions in the same counterparty's account and the amount of net unrealized profits may be used to reduce margin requirements. With respect to standbys, only profits (in-the-money amounts), if any, on "long" standbys shall be recognized.

([H]I) Limits on Net Capital Deductions [for Exempt Accounts]

[(i) Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) and (e)(2)(G) which shall be made available to FINRA upon request.]

([ii]i) In the event that the net capital deductions taken by a member as a result of deficiencies or marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) of this Rule (exclusive of the percentage requirements established thereunder), plus any mark to market loss as set forth under paragraph (e)(2)(H)(ii)d. of this Rule and any deficiency as set forth under paragraph (e)(2)(H)(ii)e. of this Rule, and inclusive of all amounts excepted from margin requirements as set forth under paragraph

(e)(2)(H)(ii)c.2. of this Rule or any de minimis transfer amount as set forth under paragraph (e)(2)(H)(ii)f. of this Rule, exceed:

a. [on] for any one account or group of commonly controlled accounts, 5 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), or

b. [on] for all accounts combined, 25 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), and,

c. such excess as calculated in paragraphs (e)(2)(I)(i)a. or b. of this Rule continues to exist[s] on the fifth business day after it was incurred,

the member shall give prompt written notice to FINRA and shall not enter into any new transaction(s) subject to the provisions of paragraphs (e)(2)(F), [or] (e)(2)(G) or (e)(2)(H) of this Rule that would result in an increase in the amount of such excess under, as applicable, [subparagraph (ii)] paragraph (e)(2)(I)(i) of this Rule.

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(f) Other Provisions

(1) through (5) No Change.

(6) Time Within Which Margin or "Mark to Market" Must Be Obtained

The amount of margin or "mark to market" required by any provision of this Rule, other than that required under paragraph (e)(2)(H) of this Rule, shall be

obtained as promptly as possible and in any event within 15 business days from the date such deficiency occurred, unless FINRA has specifically granted the member additional time.

(7) through (10) No Change.

(g) through (h) No Change.

• • • Supplementary Material: ---------------

.01 No Change.

.02 Monitoring Procedures. For purposes of paragraph (e)(2)(H)(ii)d. of this Rule, members shall adopt written procedures to monitor the mortgage banker's pipeline of mortgage loan commitments to assess whether the Covered Agency Transactions are being used for hedging purposes.

.03 Mark to Market Loss/Deficiency. For purposes of paragraph (e)(2)(H) of this Rule, to the extent a mark to market loss or deficiency is cured by subsequent market movements prior to the time the margin call must be met, the margin call need not be met and the position need not be liquidated; provided, however, if the mark to market loss or deficiency is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member shall be required to deduct the amount of the mark to market loss or deficiency from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss or deficiency is satisfied.

.04 Determination of Exempt Account. For purposes of paragraph (e)(2)(H) of this Rule, the determination of whether an account qualifies as an exempt account shall be made based upon the beneficial ownership of the account. Sub-accounts managed by an

investment adviser, where the beneficial owner is other than the investment adviser, shall be margined individually.

.05 Risk Limit Determination.

(a) For purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of this Rule:

(1) If a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level, except with respect to any account or group of commonly controlled accounts whose assets managed by that investment adviser constitute more than 10 percent of the investment adviser's regulatory assets under management as reported on the investment adviser's most recent Form ADV;

(2) Members of limited size and resources that do not have a credit risk officer or credit risk committee may designate an appropriately registered principal to make the risk limit determinations;

(3) The member may base the risk limit determination on consideration of all products involved in the member's business with the counterparty, provided the member makes a daily record of the counterparty's risk limit usage; and

(4) A member shall consider whether the margin required pursuant to this Rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements.

* * * * *