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July 19, 2013

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F. Street NE
Washington, DC 20549-1090

Re: File Number SR–MSRB–2013–04
MSRB Notice of Filing of a Proposed Rule Change Relating to a New MSRB Rule G–45, on Reporting of Information on Municipal Fund Securities

Dear Ms. Murphy:

We are submitting this comment letter, which responds to the Notice of Filing of a Proposed Rule Change Relating to a New MSRB Rule G–45, on Reporting of Information on Municipal Fund Securities (the "***Release***"),[1] because of our firm's representation of a number of primary distributors of state-sponsored 529 college savings plans ("***529 Plans***"). We appreciate the Municipal Securities Rulemaking Board's (the "***MSRB***") continuing efforts to improve the regulatory scheme governing broker-dealers distributing 529 Plans and believe that the MSRB's efforts have enabled it to effectively and efficiently regulate the brokerage industry's distribution of 529 Plans. However, as discussed below, we strongly question the value of collecting the proposed data regarding 529 Plans.

I. GENERAL COMMENTS

As the Securities and Exchange Commission ("***SEC***") is aware, 529 Plans are an outgrowth of Section 529 of the Internal Revenue Code, which authorized the States, their agencies or their instrumentalities to sponsor and offer the plans. The States generally establish these tuition savings plans as state trusts, either directly through legislation or by granting authority to establish such trusts to the state agency that administers 529 Plans. Section 529 and the rules promulgated by the Internal Revenue Service establish the permissible parameters and required elements of 529 Plans, including eligibility, maximum contributions, control over investments, permissible uses of contributions and tax treatment of earnings on contributions.

[1] *Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change Relating to a New MSRB Rule G-45, on Reporting of Information on Municipal Fund Securities*, SEC Release No. 34-69835 (June 28, 2013).

The State trusts through which these plans are offered to the public are instrumentalities of the States that establish them. As a result, the securities issued by the State trusts are municipal securities. The Investment Company Act of 1940, as amended, and the Investment Advisers Act of 1940, as amended, expressly do not apply to agencies, authorities, or instrumentalities of states. The offer and sale of 529 Plan interests, as municipal securities, are also exempt from the registration requirements of the Securities Act of 1933, as amended (the "***Securities Act***"). In addition, the interests, as well as the State issuers, are not subject to the registration and reporting requirements of the Securities Exchange Act of 1934, as amended ("***Exchange Act***"), although to the extent interests are sold through broker-dealers, such firms are subject to regulation by the MSRB, the SEC and the Financial Industry Regulatory Authority ("***FINRA***").

529 Plans generally operate through statutory trusts created pursuant to statute, through which investors' contributions to a 529 Plan become assets of the 529 Plan that then invests in underlying investment vehicles ("***Underlying Investments***"). States usually offer more than one 529 Plan under the qualified tuition program through the statutory trust. In these cases, each 529 Plan is typically managed by a different private service provider, often invests in a distinct set of Underlying Investments and is offered through separate distribution channels. Each 529 Plan permits investors to invest contributions in one or more of the trust portfolios[2] offered in the 529 Plan. These portfolios (or investment options) in turn purchase shares of the Underlying Investments, which typically are mutual funds, although other types of securities and investments have been increasingly available as Underlying Investments in recent years.

A. Limited Value of Requested Information

The MSRB's proposal would require brokers, dealers, and municipal securities dealers ("***broker-dealers***"),[3] acting in the capacity of underwriters ("***primary distributors***") of 529 Plans, to submit to the MSRB on a semi-annual (or, in the case of performance data, annual) basis certain market information about the 529 Plans they distribute. The information includes: plan descriptive information, assets, asset allocation information (at the investment option level), contributions, withdrawals, fee and cost structure, performance data, and other information (collectively, the "***Requested Information***"). The Requested Information would be collected pursuant to new MSRB Rule G-45 via new Form G-45. The Release states that:

> The MSRB, and other regulatory authorities that are charged by statute with examining [broker-dealers] for compliance with, and enforcing, MSRB rules, including the SEC and the Financial Industry Regulatory Authority ("FINRA"),

[2] *See* Letter from William H. Donaldson, Chairman, SEC, to the Honorable Michael G. Oxley, Chairman, Committee on Financial Services, U.S. House of Representatives (Mar. 12, 2004) (containing Letter from Annette L. Nazareth, Director, Division of Market Regulation, SEC, to William H. Donaldson, Chairman, SEC (Mar. 2, 2004)) ("***SEC Letter***"). The Release and proposed Form G-45 and Rule G-45 use the term "investment option" instead of "portfolio."

[3] This comment letter does not address any potential implications arising under the proposal to municipal advisors and solely focuses on broker-dealers.

will be able to utilize this information to analyze 529 plans, monitor their growth rate, size and investment options, and compare plans based on fees and costs and performance.

The foregoing statement is one of the more specific explanations afforded in the Release as to why the MSRB believes it is necessary for it to obtain the Requested Information. Yet, it fails to provide a compelling rationale as to how such information would be useful to the MSRB, the SEC and FINRA given the nature of the Requested Information, the limited reach of the rule (as discussed below, because the rule would only cover broker-dealers, the MSRB would not receive information concerning over half of the marketplace), and the comprehensive regulatory system the MSRB has implemented for broker-dealers distributing 529 Plans. We and our clients question the value the Requested Information would provide to the MSRB, SEC and FINRA. Over the past 13 years, the MSRB has designed and implemented a comprehensive and extremely effective regulatory regime governing the offer, distribution and sale of 529 Plans by broker-dealers. And it did this without any of the information it is now seeking. Having already implemented a comprehensive system governing the offer and sale by broker-dealers of 529 Plans that has proven to be highly effective, it is difficult for our clients to understand why the MSRB now believes the Requested Information is needed in order for the MSRB to fulfill its regulatory mandate.

In the Release and preceding regulatory notices,[4] the MSRB notes that it does not collect and disseminate 529 Plan market or program-specific data as it does for the municipal bond market. In pointing to the difference in the collection and dissemination practices of market data between municipal bonds and 529 Plans, the MSRB overlooks a fundamental and crucial difference between the two markets: the prices of municipal bonds are set by the market, which means the MSRB's regulatory mission is served from increased access to market data. In contrast, the prices of 529 Plans are based, in the case of investment options that invest in mutual funds, on the net asset value of the mutual funds in which such investment options invest. In other words, the value of a 529 Plan investment option is primarily dependent upon the performance of the underlying mutual funds. For 529 Plans, there simply is no market data that is comparable to the market data that exists for municipal bonds.

None of the Requested Information can ever impact the value of mutual funds or other investments in which 529 Plan investment options invest. Thus, the Requested Information sought by the MSRB has limited value as a regulatory tool. In addition, the Requested Information that would be filed with the MSRB would be unable, by itself, to indicate anything of value. Without a substantive context in which to analyze the

[4] *Request for Comment on Plan to Collect Information on 529 College Savings Plans*, MSRB Notice 2011-33 (July 19, 2011) (the "***2011 Notice***"); *Request for Comment on Draft Proposal to Collect 529 College Savings Plan Data*, MSRB Notice 2012-40 (Aug. 6, 2012); *Second Request For Comment On Draft Rule Requiring Underwriters To Submit 529 College Savings Plan Information to the MSRB*, MSRB Notice 2012-59 (Nov. 23, 2012).

Requested Information, it would be reckless to reach conclusions merely by reviewing the Requested Information itself. Our clients therefore question the value of the Requested Information when it is divorced from the terms and characteristics of 529 Plans and merely reflects the movement of funds. Given the MSRB's ability to craft rules that only govern broker-dealers, and the comprehensive system of rules that has been instituted for broker-dealers in connection with their offer, sale and distribution of 529 Plans, our clients believe that the proposal under the Release lacks a compelling justification. As an example of how the MSRB seeks to justify the proposal, it states in the Release that:

> By collecting this information, the MSRB will enhance its understanding of the 529 plan market, the growth of plans and their investment options, and the differences among plans. Such information may inform the MSRB of the risks and impact of each plan and investment option and provide the MSRB and other regulators with additional information to monitor the market for wrongful conduct.

The Release similarly states that:

> The information will allow the MSRB to assess the impact of each plan on the market, evaluate trends and differences, and gain an understanding of the aggregate risk taken by investors by the allocation of assets in each investment option. Having this information will better position the MSRB to protect investors and the public interest.

It is not clear from the Release as to how the Requested Information will "inform the MSRB of the risks and impact of each plan and investment option" or "allow the MSRB to assess the impact of each plan on the market." In this respect, the Requested Information merely provides information regarding fund flows. It does not indicate, in any sense, the risks or impact of any plan or investment option on investors. Our clients thus take issue with the MSRB's assertions as there is a significant gap between the nature of the Requested Information and the benefits the MSRB claims will come from obtaining such information. Turning back to the quoted language above, it is not even clear how the MSRB defines "risk" in this context. Does the quoted language indicate that the MSRB believes that plans or investment options with large inflows of funds entail more risk to investors simply because they are growing? The possibility of the MSRB (and other regulators) drawing substantive conclusions concerning risks and impacts solely from data flows, without any context associated with such flows, is troubling. This concern is increased because it appears the MSRB's conclusions are based on inaccurate or unsupported assumptions regarding risk and impact.

The above quoted language also reveals a more fundamental shortcoming of the Release: the MSRB's role does not extend to regulating the 529 Plan market. Obtaining information it believes "will enhance its understanding of the 529 plan market, the growth of plans and their investment options, and the differences among plans" is not the

MSRB's responsibility. Nor is it the MSRB's role to "monitor the market." The MSRB's role is limited to regulating broker-dealers that distribute and sell municipal securities. The MSRB does not have regulatory authority over the 529 Plan market; it does not have jurisdiction over issuers or obligated persons. And the Release fails to explain how the Requested Information will help the MSRB fulfill its core responsibility of crafting rules governing broker-dealers' sale and distribution of municipal securities. Until the MSRB clarifies how obtaining the Requested Information will help it fulfill its statutory role, our clients believe the SEC should not approve the Release. In this respect, the MSRB makes no attempt to specify with particularity how its rulemaking function will be enhanced by the Requested Information. Instead, it appears that the Release is an attempt to by the MSRB to expand its jurisdiction over a market it has no statutory authority to oversee.

B. Requested Information Often Is Not Within the Possession or Control of the Primary Distributor

The MSRB continues to believe that the Requested Information is readily available to primary distributors, stating in the Release that:

> On balance, the MSRB believes that semi-annual reporting of limited information, which is readily available to underwriters, will not pose an unreasonable burden on dealers.
>
> . . .
>
> The MSRB believes that the additional burden on underwriters of submitting readily available information semi-annually will be modest . . .

The reality, however, often is very different. According to our clients, primary distributors of various 529 Plans do not maintain or have access to the Requested Information. In many instances, the Requested Information is maintained by the 529 Plan recordkeeper. In our experience, the largest factor determining whether the Requested Information is maintained or accessible by the primary distributor is the nature of the contractual arrangements and role(s) played by the primary distributor vis-à-vis the State issuers of 529 Plans. While the primary distributors of a fair number of 529 Plans also serve as the program managers of 529 Plans (and thus have broader access to the type of information desired by the MSRB), the fact remains that in many 529 Plans the primary distributors do not serve as the program managers and do not possess or have access to the Requested Information. When the primary distributor does not also serve as the program manager, the recordkeeper or program manager (after obtaining the data from the recordkeeper) typically reports some or all of the Requested Information to the State issuer of the 529 Plan (but usually not to the primary distributor).

It also is important to recognize that most of the Requested Information is divorced from the sales process and the activities of a primary distributor (unless it also

engages in sales to retail customers). For instance, total aggregate assets held in 529 Plans is impacted by performance and "add-on" contributions, and withdrawals often are processed through the recordkeeper and/or selling broker-dealer, and not through the primary distributor. The same is true with respect to information about total assets held in each 529 Plan and the total assets invested in each investment option. Thus, primary distributors that do not also serve as retail selling firms will have far less information to report since such firms do not interact with investors; significantly, even in cases where a primary distributor does retail 529 Plans, much of the information is processed directly by the recordkeeper and would not be visible to the primary distributor. Thus, much of the Requested Information is not available to many primary distributors. The MSRB should not be surprised, then, to obtain reports from primary distributors that provide information covering only a limited subset of the Requested Information.

Many primary distributors do not have possession of or access to the Requested Information and have no authority to obtain such information from the 529 Plan recordkeeper (particularly, but not exclusively, in cases where the primary distributor is not the Program Manager). In a given situation, the recordkeeper is under no obligation to provide the Requested Information to the primary distributor, and in fact, may well violate contractual provisions if they were to provide such information to the primary distributor. Accordingly, our clients seek confirmation that in such situations the Requested Information is deemed to be outside the possession or control of the primary distributor (and not subject to the reporting obligation under Rule G-45). We also note that the primary distributor may be contractually prohibited from sharing the type of information sought to be filed with the MSRB without the prior written consent of the State. Our clients therefore also request confirmation that in such situations the Requested Information is deemed to be outside the possession or control of the primary distributor (and not subject to the reporting obligation under Rule G-45). In both of these situations, Rule G-45 should clearly note that the primary distributor does not have a reporting obligation.

As discussed, the above quoted language from the Release reflects the reality of certain primary distributors but not others. Such language fails to recognize that whether primary distributors have possession or control of information or the legal right to obtain it is a facts and circumstances analysis that is largely driven by their role and contractual relationship vis-à-vis the State instrumentality issuing the 529 Plan and/or the recordkeeper. Unfortunately, it appears from the rulemaking history preceding the Release that the MSRB has reached conclusions based on discussions with primary distributors who have a particular type of arrangement and are thus able to provide the Requested Information relatively easily. However, the MSRB is seeking information that various primary distributors will not be able to provide. The MSRB, FINRA and the SEC should not be surprised that various primary distributors will not be able to provide the Requested Information, thus reducing the value of such information. Our clients therefore question the public policy rationale for the Release when the ability to provide the Requested Information hinges so greatly on the specific contractual arrangements and structures underlining 529 Plans.

We also note the Release states that "[t]he proposed rule change will only require underwriters to produce information that they possess or have a legal right to obtain, such as information in the possession of an underwriter's subcontractor" (emphasis added). While the concept of possession is fairly straightforward, our clients note that the notion of "legal right to obtain" is far less clear. We believe that unless the primary distributor has a specific, enforceable legal right, such as one existing under law (such as a right created by a statutory provision) or arising from a specific contractual provision, to obtain specified information maintained by a third party, the primary distributor does not have a legal right to obtain the information for purposes of the proposal. In this respect, our clients note that a mere contractual relationship between parties does not, by itself, indicate whether one party has a legal right to obtain records created by the other party. Analysis of the contractual provisions and the rights created thereunder would be required in each and every case, which would involve a fact-specific inquiry. Our clients therefore take issue with the MSRB's assertion that "[t]he proposed rule change will only require underwriters to produce information that they possess or have a legal right to such as information in the possession of an underwriter's subcontractor"; this quoted language presumes, incorrectly, that a primary distributor necessarily has a legal right to obtain information from a subcontractor merely because they have a contractual relationship.[5] And as noted above, very often (if not typically) the Requested Information is held by a party, such as a recordkeeper, that is not in privity with the primary distributor to begin with; in such cases, the Requested Information cannot fairly be said to be within the primary distributor's possession or control.

Our clients also wish to emphasize that in those cases where a primary distributor is able to obtain Requested Information from a third party, the primary distributor typically will not be in a position to verify the accuracy or completeness of the Requested Information and therefore cannot fairly be responsible for such information. Accordingly, our clients strongly believe that Rule G-45 should clearly note that primary distributors are not responsible for ensuring that Requested Information received from third parties and filed on Form G-45 is accurate or complete.

Finally, we reiterate a point made during the rulemaking process that the rationale for the Release is largely undercut by the reality that much of the Requested Information is readily available today in the public domain.

C. The MSRB's Proposal Will Result in Incomplete Data

Even if the MSRB's proposal is implemented, the value of the Requested Information received will be of limited value for another important reason. Unlike the municipal bond market, many 529 Plans are not offered and sold through broker-dealers, and therefore are not subject to the indirect jurisdiction of the MSRB. This difference is

[5] The MSRB makes other assumptions in the context of omnibus accounts that are, in our clients' view, equally unsupportable. For instance, according to our clients the mere creation of DTCC/NSCC aggregation files does not mean that a given primary distributor has a legal right to obtain such information.

very important in the context of the Requested Information since such information will not include data on "direct-sold" 529 Plans. By definition, such 529 Plans do not involve a broker-dealer offering or selling the securities. Rule G-45 would define "direct-sold" as the sale of 529 Plans "through a website, or toll-free telephone number or other direct means."[6] This is in contrast to the proposed definition of "advisor-sold," which would be defined as the sale of 529 Plans "through a broker, dealer or municipal securities dealer that has a selling agreement with an underwriter."

Accordingly, the Requested Information sought by the MSRB under proposed Rule G-45 will be substantially incomplete. In fact, less than half of 529 Plan assets are held in broker-sold 529 Plan accounts, according to Morningstar.[7] Accordingly, the information obtained by the MSRB would represent less than half of the assets in the 529 Plan industry. The Release acknowledges the limited extent of the proposal by noting repeatedly that the Requested Information would only be provided in connection with broker-sold 529 Plans:

> The proposed rule change will, for the first time, provide the MSRB with more comprehensive information regarding 529 College Savings Plans ("529 plans" or "plans") underwritten by brokers, dealers or municipal securities dealers ("dealers") by gathering data directly from such dealers.
> . . .
>
> MSRB rules govern the activities of dealers who transact business in municipal fund securities, and it is important that the MSRB have accurate, reliable and complete information about 529 plans underwritten by dealers in order to carry out its rulemaking responsibilities.
> . . .
>
> The proposed rule change will require dealers acting in the capacity of underwriters to submit to the MSRB . . . certain information.
> . . .
>
> In short, the voluntary collection of limited 529 plan information by private organizations is not a substitute for actual data submitted by regulated dealers.
> . . .
>
> The proposed rule change will assist the MSRB and other regulators that, pursuant to Section 15B of the Act, perform examinations and other oversight

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[6] *See* SEC Letter (describing direct-sold plans as those "in which investors acquire interests in the state trust directly from the state trust or a state agency on behalf of the trust, and do not involve a sales intermediary").

[7] Joe Morris, *Direct Plans Fuel Strong 529 Growth*, Ignites, April 23, 2013, *available at* http://www.ignites.com/c/508491/56711/direct_plans_fuel_strong_growth (citing to http://corporate.morningstar.com/us/documents/529Reports/529Landscape2013.pdf).

> activities of dealers and municipal advisors, by providing them with important information regarding 529 plans underwritten by dealers.
>
> . . .
>
> Under the proposed rule, brokers, dealers or municipal securities dealers that are underwriters under Rule 15c2-12(f)(8) will be required to submit the required information to the MSRB.
>
> . . .
>
> [The proposed rule change] would apply equally to all dealers that serve as underwriters of 529 plans. (Emphasis added.)

Our clients question the wisdom of approving the MSRB's proposal when the information to be obtained from the initiative will be so incomplete. We also note that some of the data already available in the public domain covers both broker-sold 529 Plans and direct-sold 529 Plans, which means this data is, in many ways, more comprehensive than the information that the MSRB seeks. These considerations suggest that the collection of the Requested Information will provide only marginal benefits to the MSRB.

Our clients therefore disagree with the MSRB's assertion in the Release that "the information will enable the MSRB or other regulators to, on a comprehensive basis, compare the asset allocation, fees and costs, and performance of similar investment options across plans and identify trends or changes" (emphasis added). This simply is not the case since data for direct-sold 529 Plan data, representing more than half of the 529 Plan market, will not be captured under proposed Rule G-45.

D. Costs vs. Benefits

Subject to the anti-fraud provisions of the federal securities laws, the requirements for official statements generally are determined at the State level. Accordingly, each 529 Plan treats its investment option level data differently. The Release acknowledges that systems modifications would be required to provide the Requested Information in the specified manner. Unfortunately, the MSRB determined not to collect or provide any data supportive of the notion that the benefits of the proposal will outweigh the costs that will be incurred by primary distributors of 529 Plans. Instead, the Release merely states as follows:

> Moreover, the MSRB believes that such underwriters collect and retain the information required by the proposed rule change and utilize it for a variety of purposes, including reporting to issuers and other market participants. . . . As described above, the MSRB will realize substantial benefits in obtaining reliable, accurate information about 529 plans, promoting greater regulatory oversight and investor protection. In addition, the proposed rule change will not impose any burden on dealers that sell interests in 529 plans, as the obligation to submit

> information semi-annually to the MSRB will only be imposed on underwriters. On balance, the MSRB believes that the benefits of the proposed rule change greatly exceed any potential increased burden it imposes on dealers.

The MSRB concludes the benefits of its proposal will outweigh the costs without ever seeking to quantify either the benefits or the costs. Accordingly, its statement that it "believes" that the benefits of the proposed rule change greatly exceed any potential increased burden it imposes on dealers rings rather hollow. It appears that a significant component of the justification for the proposal rests on the MSRB's assertion of the benefits that will flow to securities regulators from obtaining the Requested Information. However, it is not clear what use of such information will be made by securities regulators. The justification language in the Release is far too vague to be able to assess the benefits that would flow from collection of the Requested Information:

> The MSRB, and other regulatory authorities that are charged by statute with examining dealers for compliance with, and enforcing, MSRB rules, including the SEC and the Financial Industry Regulatory Authority ("FINRA"), will be able to utilize this information to analyze 529 plans, monitor their growth rate, size and investment options, and compare plans based on fees and costs and performance. By collecting this information, the MSRB will enhance its understanding of the 529 plan market, the growth of plans and their investment options, and the differences among plans. Such information may inform the MSRB of the risks and impact of each plan and investment option and provide the MSRB and other regulators with additional information to monitor the market for wrongful conduct.

The Release contains no explanation as to how the Requested Information, which consists of fund flow information covering less than half of the market place, will aid securities regulators. For instance, there is no explanation as to how the Requested Information will improve the MSRB's rulemaking function or improve FINRA's examination program. It is hard to see how the proposal would achieve these objectives; as noted above, there is a significant disconnect between the nature of the Requested Information, which provides information on 529 Plan and investment option fund flows, and the regulatory roles played by the MSRB and FINRA in regulating broker-dealers. It is not clear why information regarding money flows for securities products is critical to regulators who are charged with regulating broker-dealers (and not the securities products or the market). While the collection of the Requested Information might allow the MSRB, FINRA and the SEC to learn additional, if very limited, information about certain 529 Plans, such information will not help these regulators to carry out their broker-dealer oversight responsibilities in any meaningful way. There is a large gap between the nature of the Requested Information and the broker-dealer oversight responsibilities of the regulators, as the Requested Information would only provide information on fund flows

of certain 529 Plans.[8] Until such time as the MSRB clearly explains how obtaining information about certain 529 Plan fund flows will help securities regulators to regulate broker-dealers, the proposal under the Release should not be approved.

E. Direct-Sold and Broker-Sold 529 Plans

In responding to a commenter's comments on a prior iteration of the proposal the MSRB writes as follows:

> FRC suggests that the MSRB only has authority over "advisor-sold" plans and should only collect information regarding these plans. The distinction between "advisor-sold" plans and "direct-sold" plans is a marketing distinction that has no bearing on the jurisdiction of the MSRB. The MSRB's jurisdiction extends to dealers or municipal advisors with respect to all their municipal fund securities and municipal advisory activities. Consequently, underwriters of "direct-sold" and "advisor-sold" plans must submit information required by the proposed rule change to the MSRB.

The above quoted language is internally inconsistent and unsupportable. First, the MSRB's assertion that the distinction between "direct-sold" and "advisor-sold" plans is a "marketing distinction" is belied by its own definitions of these terms. As noted above, proposed Rule G-45 would define "advisor-sold" as the sale of 529 Plans "through a broker, dealer or municipal securities dealer that has a selling agreement with an underwriter" and would define "direct-sold" as the sale of 529 Plans "through a website, or toll-free telephone number or other direct means." Far from being a marketing distinction, the distinction is critical in assessing the MSRB's jurisdiction as it delineates between those 529 Plans that are sold through broker-dealers and those that are not. As the quoted paragraph notes (as do multiple other statements in the Release), the proposed rule and form, like all MSRB rules, only apply to broker-dealers. And the MSRB's proposed definition of "direct-sold" 529 Plans clearly denotes 529 Plans that are sold without the involvement of broker-dealers. How is it then that the MSRB can claim that the distinction "has no bearing on the jurisdiction of the MSRB" when the very next sentence of the quoted language states that "[t]he MSRB's jurisdiction extends to dealers"? The last sentence of the above paragraph is inaccurate as a matter of law and is inconsistent with the MSRB's own definition of "direct-sold" 529 Plans; since direct-sold 529 Plans do not involve a broker-dealer (per the MSRB's own definition of "direct-sold") and the MSRB's rules only apply to broker-dealers,[9] it is wrong to state that the proposed rule will apply to entities that are not broker-dealers (which is what the last sentence indicates by noting that "underwriters of 'direct-sold' . . . plans must submit information required by the proposed rule change to the MSRB").

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[8] As noted above, 529 Plans are largely exempt from regulation under the federal securities laws and the jurisdiction of the MSRB and FINRA are limited to regulating broker-dealers (and the SEC's jurisdiction over 529 Plans is limited to enforcing the anti-fraud provisions of the federal securities laws).

[9] *See supra* note 3.

The flaws inherent in the above-quoted paragraph appear in other places in the Release as well. Only broker-dealers would be subject to Rule G-45 and yet the MSRB states in the Release that "[t]he MSRB believes that, in most cases, the record-keeper will be an underwriter . . . ." In responding to certain comments from the Investment Company Institute, the MSRB writes:

> ICI notes that 529 plans have only one underwriter, the primary distributor, and that many other entities are involved in operating and maintaining a plan, such as the plan's program manager, record-keeper, investment manager, custodian and state sponsor. ICI suggests that none of these entities would qualify as an underwriter under the proposed rule. MSRB disagrees. Under SEC Rule 15c2-12(f)(8), an underwriter is defined broadly and may include one or more of the entities identified by ICI. Nevertheless, if a program manager, for example, is an underwriter pursuant to SEC rules, its obligation to submit information would be deemed satisfied if the primary distributor or another underwriter submitted all of the information required by proposed Rule G-45 on its behalf. (Emphasis added.)

However, under proposed MSRB G-45(d)(x)(iv), "[t]he term "underwriter" shall mean a broker, dealer or municipal securities dealer that is an underwriter, as defined in Securities Exchange Act Rule 15c2-12(f)(8), of municipal fund securities that are not local government investment pools" (emphasis added). Thus, under the MSRB's very own definition the term underwriter can only include "a broker, dealer or municipal security dealer" and therefore does not include any other entity (such as a program manager, to use the example in the quoted paragraph above, unless it is also a broker-dealer). Accordingly, the MSRB's statement is contrary to the MSRB's own definition of "underwriter" in proposed Rule G-45.[10]

[10] We also note that the definition of underwriter in Rule 15c2-12 was based on, and is substantially similar to the definition of "underwriter" in Section 2(a)(11) of the Securities Act, which was designed to connote the notion of a "statutory underwriter" for purposes of the anti-fraud provisions of the Securities Act. The definition of "underwriter," as carried through to Rule 15c2-12, is thus broader than what the term "primary distributor"connotes, in that the term "underwriter" covers entities that do not serve as and/or do not need to regiser as broker-dealers. In addition, not every firm that meets the definition of underwriter in Rule 15c2-12 (or proposed Rule G-45 for that matter) is, in reality, serving as the primary distributor of a 529 Plan. In other words, falling within the definition of underwriter does not mean an entity is serving as the primary distributor, as this term is used in the Release (and has been defined in prior iterations of the proposal). In addition, notwithstanding the broad scope of the term underwriter in Rule 15c2-12, the MSRB's suggestion in the Release that parties such as recordkeepers, investment managers and custodians, are statutory underwriters is inconsistent with the historical interpretation of such term (and the corresponding Securities Act definition) by the courts. We recognize that the Release states that such entities "may include one or more of the[se] entities." This is true only because any person may potentially be an underwriter for purposes of Rule15c2-12 (unlike the definiiton of underwriter under proposed Rule G-45, as discussed above). However, the MSRB practically assumes that these entities often will be underwriters under Rule15c2-12. For instance, the Release states "[t]he MSRB believes that, in most cases, the record-keeper will be an underwriter or a subcontractor of an underwriter," and this simply is not the case. It would take rather extraordinary circumstances for a recordkeeper, investment manager or custodian, for instance, to be an underwriter for purposes of Rule15c2-12.

II. COMMENTS ON SPECIFIC PROVISIONS

A. Requested Information on Asset Class and Asset Allocation

Proposed Form G-45 would seek, among other things, information on "asset classes in the investment option" and "Asset Class Allocation Percentage." It is not clear what the phrase "asset classes in the investment option" means as investment options do not have or invest in asset classes. Rather, according to our clients the predominant Underlying Investments in 529 Plans are diversified mutual funds. Thus, most 529 Plan investment options invest in securities that, in turn, have exposure to asset classes. Accordingly, it is not clear how primary distributors are supposed to determine how to complete the Requested Information in Form G-45. If anything, it is the underlying mutual funds into which investment options invest (and not the investment options themselves) that can arguably be said to invest in or have exposure to "asset classes." Thus, in our view it is unclear how the "Asset Class" and "Asset Class Allocation Percentages" are to be completed on proposed Form G-45. Take, for instance, age-based investment options that invest in multiple mutual funds; how are such investment options supposed to provide the Requested Information?

We also note that the term "asset class" is proposed to be defined as "domestic equities, international equities, fixed income products, commodities, insurance products, bank products, cash or cash equivalents or other product types." As noted, however, 529 Plans primarily invest in mutual funds. There is therefore a significant gap between what 529 Plan investment options invest in and the proposed definition of "asset class." We submit that the two items in the proposal relating to asset class should be eliminated because the Requested Information is not applicable and cannot be provided.

B. Requested Information on Underlying Investments

The proposal under the Release requests information on "the name of each underlying investment in each investment option . . . ." (emphasis added). This description is inaccurate as a matter of law and is simply not accurate. 529 Plan account owner funds solely invest in the 529 Plan. They are not invested in anything else. The 529 Plan trust is the sole legal and beneficial owner of the Underlying Investments. We note, in particular, the following from the SEC Letter:

> Investors in 529 tuition savings plans, however, hold interests in a municipal issuer – the state trust fund – that is exempt from the bulk of the federal securities laws. Thus, many of the substantive aspects of the Investment Company Act and the other federal securities laws do not operate to the direct benefit of 529 plan investors.... Because 529 plan investors are not considered to be beneficial owners of the investment companies that serve as the underlying investments in their 529 plan accounts, the federal securities laws do not require delivery of disclosure documents such as annual reports, semi-annual reports, and proxy statements. These documents must generally be delivered directly to beneficial

> owners of investment company shares. Similarly, 529 plan investors do not have voting rights in the registered investment companies held in their accounts.
>
> Thus, it is legally and factually incorrect to describe the Underlying Investments as being "in" the investment option; they are not part of the 529 Plan security.[11]

The proposal under the Release requests information on the name of each underlying investment, the corresponding "allocation percentage" and the "Estimated Underlying Fund Expenses." It is inappropriate to request information about the Underlying Investments. As the SEC explained in the SEC Letter, the Underlying Investments are not part of what investors purchase and are not municipal securities. The MSRB itself acknowledged this in the process of adopting MSRB Rule G-21(e)(ii)(F), which is entitled "applicability with respect to underlying assets" and which states, in relevant part, that "subsection (e)(ii) shall apply solely to the calculation of performance relating to municipal fund securities and does not apply to . . . the calculation of performance for any security held as an underlying asset of the municipal fund securities." In proposing this provision, the MSRB stated as follows:

> **Underlying Registered Securities.** New paragraph (vi) requires that, if an advertisement for a municipal fund security provides specific details of a security held as an underlying asset of the municipal fund security, the details included in the advertisement relating to such underlying security be presented in a manner that would be in compliance with any SEC or NASD advertising rules that would be applicable if the advertisement related solely to such underlying security. Details of the underlying security included in the advertisement must be accompanied by any further statements necessary to ensure that the inclusion of such details does not cause the advertisement to be false or misleading with respect to the municipal fund securities advertised. This provision does not limit the applicability of any rule of the SEC, NASD or any other regulatory body relating to advertisements of securities other than municipal fund securities, including advertisements that contain information about such other securities together with information about municipal fund securities.[12]

Similarly, the MSRB has stated that "the draft language confirms that these provisions of Rule G-21 would apply solely to the calculation of performance relating to municipal

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[11] *See supra* note 2. In describing 529 Plans, the SEC Letter notes that investors' contributions, "which are held in separate accounts in the state trust fund, are generally invested by the trust fund in state-managed portfolios that, in turn, usually invest their assets in several mutual funds or other pooled investment vehicles." Similarly, the 2004 SEC Letter discusses "discrepancies between the returns on underlying investments and the reported returns of plan portfolios" and notes that "[i]n the case of direct-sold 529 plans, plan documents typically offer prospective investors a choice of several managed portfolios that invest in investment companies or other pooled investment vehicles, and provide generalized disclosure about the underlying investments."

[12] *Notice of Filing of Amendments Relating to Advertisements of Municipal Fund Securities*, MSRB Notice 2004-42 (Dec. 16, 2004).

fund securities and not to the calculation of performance for any security (such as a mutual fund) held as an underlying asset of the municipal fund securities."[13]

We note that the Release itself distinguishes between investment options and the Underlying Investments in noting that "the investment options are unique to 529 plans and are not regulated as registered investment companies by the SEC." The MSRB thus expressly contrasts 529 Plan investment options, about which the MSRB asserts information is important to obtain, and the Underlying Investment mutual funds, which it implicitly acknowledges already are subject to SEC regulation.

The MSRB and SEC have recognized that securities in which the 529 Plan investment options invest, such as mutual funds, are not subject to MSRB regulation because they are not part of the municipal fund securities. Given the statutory provisions of Section 15B of the Exchange Act, our clients question the legal authority of the MSRB to mandate the filing of information regarding mutual funds and other securities and financial instruments that are not municipal securities. They believe, and we concur, that the SEC is obligated to reject the MSRB's proposed rule request to the extent it seeks the filing of information concerning Underlying Investments, which are beyond its jurisdiction as provided in the Exchange Act.[14]

C. Requested Information on Marketing Channel

Proposed Form G-45 would require disclosure of the "marketing channel," which is proposed to be defined as "the manner by which municipal fund securities . . . .are sold to the public, such as through a broker, dealer or municipal securities dealer that has a selling agreement with an underwriter (commonly known as 'advisor-sold') or through a website or toll-free telephone number or other direct means (commonly known as 'direct-sold')." Our clients see no value in asking for information on the marketing channel since under the proposal *only* broker-dealers could be required to provide this information. As discussed above, by definition, "direct-sold" plans do not involve a broker-dealer offering the securities.[15] A form designed for broker-dealers should not require disclosure of information in situations where no broker-dealer is involved (*i.e.*, the form should not contemplate and ask for information that would be relevant only in the case of voluntary filings by non-broker-dealers).

With respect to this latter point, our clients believe there is a significant chance of investor confusion if voluntary filings are permitted under the proposal. Our clients likewise believe the ability of issuers to make voluntary filings of Official Statements and

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[13] *Request for Comments on Draft Amendments Relating to Advertisements of Municipal Fund Securities and Draft Interpretive Guidance on Disclosures in Connection with Out-of-State Sales of College Savings Plan Shares*, MSRB Notice 2004-16 (June 10, 2004).

[14] Ironically, the Release states "in order to ease the burden on dealers, the proposed rule change 'eliminate[d] the requirement to submit information on underlying investments' . . . ."

[15] *See also* the SEC Letter (describing direct-sold plans as those "in which investors acquire interests in the state trust directly from the state trust or a state agency on behalf of the trust, and do not involve a sales intermediary").

other documents on the MSRB's Electronic Municipal Market Access system ("***EMMA***") has the potential for investor confusion. Without clear and prominent disclosure on EMMA that MSRB and FINRA oversight is not available and that MSRB rules do not apply with respect to direct-sold offerings, investors that happen to see filed Forms G-45 and Official Statements for offerings would naturally (but incorrectly) believe that such oversight and rules apply and that a registered broker-dealer is involved in the offering.

D. Requested Information on Program Managers

A number of items in the proposed Form G-45 relate to the Program Manager. Our clients believe that it is outside the jurisdiction of the MSRB to seek information about an entity hired by 529 Plan trustees to provide services to the plan when neither the issuer nor the entity are regulated by the MSRB. The MSRB provides no justification for seeking this information. Such information has no relevance to the MSRB's role as a securities regulator of broker-dealers distributing municipal securities. It is not clear why an MSRB filing should contain information on service providers hired by municipal issuers to provide various services. Our clients therefore believe that all such information requests should be struck from Form G-45.

E. Requested Information on Fees and Expenses

A number of items in the proposed Form G-45 request information regarding 529 Plan fees and expenses, such as State fees, audit fees, asset-based fees, annual account maintenance fees, and bank administration fees. The MSRB's jurisdiction does not extend to the regulation of 529 Plans; it only has regulatory authority over broker-dealers. Our clients therefore believe that it is inappropriate for the MSRB to require primary distributors to file data concerning securities product fees that are unrelated to the primary distributor. Such information is simply too far removed from the MSRB's charge to regulate broker-dealers and the Release contains no clear explanation as to how receiving data on these fees will help it to regulate broker-dealers distributing 529 Plans. Our clients thus ask the SEC to reject the proposal in the Release to the extent it seeks securities product fee data that is not tied to the primary distributor.

IV. CONCLUSION

Although we appreciate the MSRB's desire to learn more about the 529 Plan marketplace, there is an unsubstantiated assumption in the Release that possessing the Requested Information would improve the MSRB's regulatory efforts. We believe that the MSRB should, before requiring the filing of any data, first support the notion that the Requested Information will in fact aid it in regulating primary distributors of 529 Plans, particularly since the Requested Information will provide such a limited, and perhaps skewed, snapshot of the industry. Until the MSRB satisfies this burden, we believe it would be premature for it to impose a substantial burden on the industry to obtain, review, and report the Requested Information.

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I would be pleased to provide additional information or discuss these comments at your convenience.

Very truly yours,

Michael Koffler

Michael Koffler