December 11, 2015

Submitted electronically

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: **FINRA Regulatory Notice 15-36,**
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2015-16,
Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-Ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith and Mr. Smith:

Fidelity Investments[1] ("Fidelity") appreciates the opportunity to respond to the Financial Industry Regulatory Authority's ("FINRA's") Regulatory Notice 15-36 and the Municipal Securities Rulemaking Board's ("MSRB's") Regulatory Notice 2015-16 (together the "Proposals").[2] The Proposals seek to enhance fixed income pricing transparency for retail customers by generally requiring brokers, dealers and municipal security dealers ("broker-dealers") to disclose, on retail customer confirmation statements, the price to the customer, the price to the broker-dealer, and the differential between those two prices for certain principal transactions in corporate, agency and municipal securities. FINRA and the MSRB obtained initial views on the Proposals in FINRA Regulatory Notice 14-52 and MSRB Regulatory Notice 2014-20[3] (the "initial Proposals") on which Fidelity provided comments.[4]

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[1]Fidelity is one of the world's largest providers of financial services. Fidelity provides investment management, retirement planning, portfolio guidance, brokerage, benefits outsourcing and many other financial products and services to more than 20 million individuals and institutions, as well as through 10,000 financial intermediary firms.

[2]*See* FINRA Regulatory Notice 15-36; Pricing Disclosure in the Fixed Income Markets (October 2015) *available at:* http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-15-36.pdf ("FINRA Proposal") *See* MSRB Regulatory Notice 2015-16; Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations (September, 2015) *available at:* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2015-16.ashx?la=en ("MSRB Proposal"). Unless otherwise defined in this letter, capitalized terms have the meanings ascribed to them in the Proposals.

[3]*See* FINRA Regulatory Notice 14-52; Pricing Disclosure in the Fixed Income Markets (November 2014) *available at:* http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p601685.pdf and *See* MSRB Regulatory Notice 2014-20; Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations (November 2014) *available at:* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-20.ashx?n=1

Fidelity submits this letter on behalf of Fidelity Brokerage Services LLC ("FBS"), a Securities and Exchange Commission ("SEC") registered introducing retail broker-dealer and FINRA member, and its affiliate, National Financial Services LLC ("NFS"), a SEC registered clearing firm and FINRA member. Both FBS and NFS are registered with the MSRB as municipal securities dealers. Fidelity's comments reflect the views of both an introducing broker-dealer and a clearing broker-dealer that will be affected by the Proposals.

As we discussed in our comments on the initial Proposals, Fidelity supports targeted, market-driven, pricing transparency efforts in the fixed income markets. Pricing transparency promotes robust competition among diverse market participants, which helps foster innovation and allows for greater customer choice.

Fidelity's pricing model for our self-directed retail brokerage customers demonstrates our commitment to transparent, simple and low cost fixed income pricing. Fidelity provides its retail brokerage customers access to a wide selection of secondary market fixed income inventory sourced directly from third-party alternative trading systems (Tradeweb Direct, KCG Bondpoint and TMC Bonds), other national broker-dealers, and from its affiliate, Fidelity Capital Markets (FCM), a division of NFS. Bonds from FCM are treated on a par with fixed income security offerings from unaffiliated third-party sources. When FCM is not the offering dealer, Fidelity's compensation is limited to a fully disclosed bond trading fee of $1 per bond online.[5] We disclose this fee prior to the trade, in our retail brokerage commission schedule, on order preview pages at the point of trade on *Fidelity.com*, and via representatives in representative-assisted trades.

We believe that a reasonably disclosed, fixed, bond transaction fee is a more transparent form of pricing for retail brokerage customers than mark-up based pricing and, in many cases, is more cost efficient. Fidelity recently commissioned Corporate Insight to study bond pricing, available online, for self-directed retail investors from five brokers that offer corporate and municipal bonds. The study found on average that three competitors that bundled their markups or fees into their online bond prices were asking an average of $13.97 more per bond than Fidelity.[6]

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[4]Fidelity comment letter available at:
http://www.finra.org/sites/default/files/notice_comment_file_ref/Fidelity_Investments_FINRA_RN14-52.pdf and http://www.msrb.org/RFC/2014-20/Fidelity.pdf

[5]Minimum concessions apply: online secondary market transactions $8; if traded with a Fidelity representative, $19.95. For U.S. Treasury auction purchases traded with a Fidelity representative, $19.95 per trade. Fixed income trading requires a Fidelity brokerage account with a minimum opening balance of $2,500. Rates are for U.S. dollar–denominated bonds; additional fees and minimums apply for non-dollar bond trades. Other conditions may apply. See Fidelity.com/commissions for details.

[6]The study compared online bond prices for over 20,000 municipal and corporate inventory matches between September 2 and October 6, 2015. It compared municipal and corporate inventories offered online in quantities of at least $10,000 face or par value. Corporate Insight determined the average cost differential by calculating the difference between the costs of matching corporate and municipal bond inventory at Fidelity vs. the markup-based firms in the study, then averaging the differences across all of the competitor firms. For further information regarding this study, see *Are Investors Getting the Biggest Bang for Their Brokerage Buck? Fidelity Investments Value Survey Reveals Comparison Shopping Can Have a Major Impact on Investor's Wallets* (November 24, 2015) *available at:* https://www.fidelity.com/about-fidelity/individual-investing/investors-getting-biggest-bang-for-buck

Fidelity appreciates regulatory efforts to improve pricing transparency in the fixed income markets. We acknowledge the deliberative approach FINRA and the MSRB have taken with respect to the Proposals and their efforts to gather thoughtful and detailed feedback through comment letters and interactive sessions with member firms. While FINRA and the MSRB have made several modifications to the initial Proposals, we continue to have significant concerns with the Proposals as currently drafted. These concerns focus on the following areas:

- *The Proposals are not harmonized.* To increase retail customer understanding and to acknowledge efficiencies in market regulation of similar products, FINRA and MSRB confirmation mark-up requirements for principal transactions must be uniform in design and operation;

- *The Proposals should apply to a broader group of principal transactions and focus on the difference between the price the customer was charged and the prevailing market price ("PMP") of the security. PMP should be defined differently in different trading scenarios.* To increase retail customer understanding of the fairness and reasonableness of fixed income pricing, mark-up disclosure requirements should 1) apply to all fixed income transactions executed on a principal basis; 2) be determined contemporaneously with trade execution; and 3) focus on the difference between the price the customer was charged and the PMP of the security. PMP should be defined differently in different trading situations; and

- *The current Proposals remain unworkable from a market participant standpoint.* Changes to the Proposals, as currently drafted, are critical because the Proposals would introduce new operational risks into the already complex confirmation statement generation process.

Each of these points in discussed in further detail below.

<u>The FINRA and MSRB Proposals Must Be Harmonized.</u>

As currently drafted, there are material and substantive differences between the Proposals. For example, the Proposals contain different disclosure requirements[7], differences in the time window for evaluating trades[8], different descriptions of transactions executed by a "functionally separate trading desk"[9], different requirements regarding how positions acquired

[7]The MSRB Proposal requires, for retail and institutional accounts, the time of trade execution accurate to the nearest minute and for retail accounts only, a hyperlink and URL address to the Securities' Details page for the customer's security on EMMA along with a brief description of the type of information available on that page while the FINRA Proposal requires for retail customer accounts only a reference, and hyperlink if the confirmation is electric, to TRACE publically available data.
[8]The MSRB Proposal contemplates a two hour look forward and look-back for applicable trades and seeks comment on its initial Proposal that required a full day look-back, while the FINRA Proposal requires a full day look-back.
[9]Under the MSRB Proposal, where multiple trading desks under a single dealer operate independently such that one trading desk may have no knowledge of the transactions executed by another trading desk, mark-up disclosure would not be required for a customer transaction if the dealer can establish that: the customer transaction was executed by a principal trading desk that is functionally separate from the principal trading desk that executed the

by an affiliate would be excluded from the proposed requirements[10] as well as different approaches to new issues[11], and material changes in the price of a security.[12] Most significantly, there are fundamental differences in the Proposals with regard to how a dealer's mark-up or mark-down would be calculated and presented to retail customers on their confirmation statement.[13]

We acknowledge FINRA and the MSRB's challenge to design rules that are consistent and address regulatory concerns across the corporate, agency and municipal securities fixed-income markets, but believe that retail investors and market participants would be well served by a coordinated regulatory approach that results in requirements that are uniform in design and operation. To this end, we anticipate that a coordinated approach to rulemaking would include not only the resolution of material and substantive differences between the FINRA Proposal and

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dealer's same-side of the market transaction; and the functionally separate principal trading desk through which such same-side of the market transaction was executed had no knowledge of the retail customer transaction. In contrast, FINRA proposes to exclude firm-side transactions from the proposed disclosure that are conducted by a department or desk that is functionally separate from the retail-side desk, *e.g.*, where the firm can demonstrate through policies and procedures that the firm-side transaction was made by an institutional desk for an institutional customer that is separate from the retail desk and the retail customer. This exception would not apply, however, where the transaction of the separate department or desk is related to the other desk, *e.g.*, if the transactions and positions of a separate department or desk are regularly used to source the retail transactions at the other desk.

[10]Under the MSRB Proposal, if a municipal securities dealer, on an exclusive basis, acquires municipal securities from [sells to] an affiliate that holds inventory in such securities and transacts with other market participants, the dealer would be required to "look through" the transaction with the affiliated dealer and substitute the affiliates trade with the third party from whom it purchased or to whom it sold the security to determine whether disclosure of the mark-up would be required. FINRA proposes to exclude trades where the member's principal trade was executed with an affiliate of the member and the affiliate's position that satisfied this trade was not acquired on the same trading day.

[11]The MSRB Proposal would not require disclosure for transactions in new issue securities affected at the list offering price by members of the underwriters group. FINRA's Proposal would not require disclosure where the member acquired the security in a fixed-price offering and sold the security to non-institutional customers at the fixed price offering price on the day the securities were acquired and the proposal would continue to apply to new issue transactions that are part of variable price offerings.

[12]FINRA proposes that in the event of a material change in the price of a security between the time of the firm principal trade and the customer trade, the reference price may be omitted from the confirm. The MSRB Proposal contains no similar exclusion, although a material change in the price of a security would presumably also affect the prevailing market price.

[13]The MSRB Proposal would require confirmation disclosure of mark-ups for certain principal transactions with retail customers when the dealer makes a corresponding trade within two hours before or after the customer's trade. The MSRB has also requested comment on proposed modifications to a November 2014 proposal that would require confirmation disclosure of same-day pricing information for specified principal transactions with retail customers. Under the MSRB' Proposal, a dealer's mark-up would be disclosed as total dollar amount and as a percentage of the principal amount of the customer transactions and the mark-up to be disclosed would be the difference between the price to the customer and the prevailing market price of the security where presumptively the prevailing market price would be established by looking at the dealer's contemporaneous costs. The FINRA Proposal would require confirmation disclosure of same-day pricing information for specified principal transactions with retail customers. Under the FINRA Proposal, the dealer would be required to disclose the price to the customer, the members Reference Price and the differential between the price the customer and the member's Reference Price where the Reference Price is defined as the price of the dealer's principal trade. The FINRA Proposal also allows for firms to use alternative methodologies to calculate the Reference Price in a complex Trade Scenario while the MSRB Proposal contains no similar provision.

MSRB Proposal but also the use of identical language where the regulatory requirements are ostensibly the same.

The use of different wording to accomplish the same regulatory goal can lead to reasonable assumptions that regulatory requirements differ. If different wording is used in the FINRA Proposal and MSRB Proposal to meet identical requirements, we are concerned that MSRB and FINRA examination and enforcement staff will interpret the different wording to mean different things, otherwise, one might reasonably ask, why wasn't the same wording used across both Proposals? Moreover, if different wording is used to accomplish the same regulatory goals, industry participants will be called upon to harmonize the FINRA and MSRB final rules in practice, which is not an appropriate or efficient use of industry resources. To the extent that FINRA and the MSRB are not able to harmonize their approach to final rulemaking on this topic, we urge the SEC to take action.

Moreover, as FINRA and the MSRB are aware, the Department of Labor is currently engaged in rulemaking that would require disclosure of dealer mark-ups, among other items, in certain fixed income transactions executed as principal in connection with the provision of investment advice to retirement accounts.[14] Fidelity has urged the Department of Labor to allow FINRA and the MSRB to take the lead in rulemaking on this topic, as FINRA and MSRB rules will apply across retirement and non-retirement accounts.[15]

It appears that the Department of Labor's final rule on disclosure of dealer mark-ups may precede any FINRA and MSRB final rulemaking. While we are hopeful that the DOL will recognize and leverage the work by FINRA and the MSRB, the potential conflict and investor confusion from potentially three different sets of mark-up disclosure requirements highlights the importance of FINRA and the MSRB adopting a uniform rule.

<u>Fixed income mark-up disclosure should 1) apply to all fixed income transactions executed on a principal basis; 2) be determined contemporaneously with trade execution; and 3) be based on the prevailing market price ("PMP") of the security, with the PMP determined by the circumstances of the trade.</u>

The Proposals seek to ensure fairness and transparency around mark-ups in fixed income transactions by requiring broker-dealers to provide mark-up disclosure on a subset of retail customer fixed income transactions executed on a principal basis. Depending on when a broker-dealer makes a corresponding principal trade to a customer's trade (i.e. within two hours, before or after, the customer's trade or on the same day as the customer's trade) the proposed mark-up disclosure may --or may not-- appear on the customer's confirmation statement. As a result,

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[14]*Definition of the Term "Fiduciary", Conflicts of Interest Rule – Retirement Investment Advice*; *Proposed Rule* 80 FR 21928 (April 20, 2015); *Proposed Class Exemption for Principal Transactions in Certain Debt Securities between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs* 80 FR 21989 (April 20, 2015)
[15]*See* Letter from Ralph Derbyshire, Senior Vice President & Deputy General Counsel, FMR LLC Legal Department, to Office of Regulations and Interpretations, Employee Benefits Security Administration, (July 21, 2015) *available at*: http://www.dol.gov/ebsa/pdf/1210-AB32-2-00658.pdf

within a single confirmation statement, mark-up disclosure may appear for some --but not other-- fixed income securities where the firm has executed the transaction on a principal basis. We believe that the limited scope of the Proposals will do little to clarify fixed income pricing for retail customers.[16] Moreover, a requirement for dealers to complete an end-of-day review of all dealer transactions that occur within a two-hour window before or after the customer transaction, or on the same day as the customer transaction, will pose risks to the process used by dealers to generate customer confirmation statements.[17]

In place of the current Proposals, FINRA and the MSRB should require *real-time* mark-up disclosure across *all* fixed income transactions executed on a principal basis, subject to the methodology we propose. A uniform disclosure requirement across all fixed income securities executed on a principal basis would:

- reduce retail customer confusion as to why this disclosure appears on some --but not all -- of their fixed income transactions where the firm acts in a principal capacity;
- avoid broker-dealers having to navigate an overly complex and at time conflicting trade matching process that invites new operational risk in the already complex confirmation statement generation process; and
- eliminate regulatory concerns with gaming by removing an artificial boundary beyond which disclosure is not required.

Additionally, we question the ultimate regulatory goal of mark-up disclosure in fixed income transactions executed on a principal basis. If the ultimate regulatory goal is to require mark-up disclosure across all fixed income transactions executed on a principal basis, an interim requirement to apply disclosure to a limited subset of trades will re-direct and reduce industry resources and confuse retail customers. Disclosure requirements that apply to all fixed income transactions executed on a principal basis would make more efficient use of limited industry and regulatory resources and promote retail investor understanding. We urge FINRA and the MSRB to consider the strategic and long term view of this approach.

Proposed Mark-Up Disclosure Methodology.

FINRA and the MSRB's mark-up disclosure requirements should focus on the difference between the price the customer was charged for a fixed income security and the PMP of the fixed income security. We acknowledge the regulatory challenge in defining PMP in the fixed income markets. Unlike the equities markets that define PMP by the National Best Bid or Offer ("NBBO"), the fixed income markets do not have a real time valuation or market wide best price

[16]Retail customers currently receive dealer compensation information for trades executed on an agency basis. Under the Proposals, retail customers would receive dealer compensation information for a subset of principal trades and would receive no dealer compensation information for other principal trades. We believe that a third scenario (no disclosure based on the time of the corresponding principal trade) will lead to customer confusion and not add to customer understanding of the fairness and reasonableness of dealer compensation.
[17]*See* discussion infra at page 9.

for each fixed income security. This issue is compounded by the fact that many fixed income securities do not have a ready market.

The Proposals seek to provide retail customers information on whether they received a fair price on their fixed income trade by comparing the price the dealer paid for the fixed income security with the price at which the dealer sold the fixed income security - that is the dealer's profit and loss on the trade - in transactions where a dealer's trade occurs on the same side of the market as the customer's trade, either on the same day or within a two hour window. For example, under the MSRB Proposal, a dealer would be required to show the difference between the price to the customer and the PMP for the security, with the PMP established by referring to the dealer's contemporaneous costs incurred or contemporaneous proceeds obtained. For the FINRA Proposal, the price to the customer would be compared to the Reference Price, defined as the price of the principal trade.

We agree that there are situations in which a dealer's actual contemporaneous costs or proceeds are a reasonable proxy for PMP. For example, we believe that this approach would work well in the case of certain "riskless principal" transactions where, after receiving an order to buy from a customer, a dealer purchases a security from another person to offset a contemporaneous sale to such customer, or, having received an order to sell from a customer, the dealer sells the security to another person to offset a contemporaneous purchase from such customer.

We also see many situations in which a dealer's costs or proceeds are not a reasonable proxy for PMP, such as where the dealer executes a trade from inventory or where there have been significant events affecting the price of the security since it was bought or sold. In these situations, the price a dealer paid for a fixed income security is a less reliable indication of fair price for retail customers based on the many different factors that can affect a dealer's profit and loss on a fixed income transaction. These factors include, but are not limited to, market events, security specific news events and length of time in inventory.

Moreover, dealer profit and loss is not how consumers typically judge fair pricing. Fair pricing is generally determined to be the price paid for a product at a given vendor versus the PMP across the industry. For example, if a consumer goes to a particular grocery store to purchase a can of soup, the price the grocery store paid their vendor for the can of soup is not relevant to the consumer's decision to purchase the can of soup at that particular store. Instead, the consumer generally determines the fairness of their purchase price by understanding the price other grocery stores charge for the can of soup and making a determination to purchase the can of soup at a particular store based off this comparison.

While a number of different alternative definitions are possible and warrant further discussion, we propose PMP be defined as the dealer's best available price for the subject security under the best available market at the time of trade execution. Because there is no single, objective standard for best available price for a particular security, regulators should consider providing detailed interpretive guidance or best practices to assist dealers in determining the PMP for a fixed income security in these situations. These industry best practices might include several different methodologies that dealers could apply when determining PMP including but not limited to, looking at a trader's mark-to-market at the end of the day, contemporaneous cost, top of book, and/or vendor solutions that offer real time valuations for certain securities.[18] Firms would employ a reasonable methodology and clearly document and consistently apply their chosen methodology. We believe that this real-time approach to mark-up disclosure, combined with existing dealer obligations of best execution and fair and reasonable compensation, will be understandable to retail investors and provide needed flexibility to market participants.

A comparison of the cost of a customer's fixed income transaction at a specific firm to the PMP, combined with a link to real-time EMMA or TRACE data regarding the specific fixed income security, would provide retail customers both dealer specific and industry information concerning their individual trade. Moreover, this combined approach sends a strong regulatory message that mark-up disclosure is an important component of a retail customers' trade across *all* fixed income transactions, not a limited subset of trades. We would anticipate that this information would be provided by introducing firms to their clearing firm during the normal trade process, minimizing disruption to the trade confirmation process. Because the disclosure would be required across all retail fixed income trades, not a subset of trades, this approach would also seek to minimize regulatory gaming concerns.

We believe that using a PMP to calculate a reference price on a fixed income security is a more tailored and more transparent approach than certain alternative proposals such as a Volume Weighted Daily Average Price ("VWAP") or a Volume Weighted Daily Average Spread ("VWAS") calculated by regulators or individual dealers. FINRA's analysis of estimated mark-ups and mark-downs on customer trades in corporate and agency debt securities during the first quarter of 2015 showed a material difference between the median mark-ups and mark-downs at the tail of the distribution, indicating that some customers paid considerably more than others in similar trades.[19] A proposed VWAP or VWAS approach does not address the issue of fairness or reasonableness of dealer compensation because it does not provide trade specific information to investors which would highlight dealer prices significantly higher than others in the industry. The approach also presents significant operational difficulties in that if regulators or dealers were to calculate a VWAP or VWAS for each security after the end of each trading day, the process a broker-dealer uses to generate confirmation statements for retail investors could be delayed.

If FINRA and the MSRB seek to improve fixed income price transparency for retail investors, we believe that 1) a comparison of the cost of a fixed income transaction at a specific firm to the PMP (under our proposed methodology) combined with 2) a link to real-time EMMA or TRACE data regarding the specific fixed income security would address this regulatory goal. Nevertheless, given the possibility that our views may not prevail, we are compelled to once

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[18]For example, MSRB Notice 2010-10 (April 21, 2010) requested comment on draft interpretive guidance on prevailing market prices and mark-up for transactions in municipal securities. We believe that this draft guidance provides a good starting point for future interpretive guidance on prevailing market price for purposes of mark-up disclosures for both the MSRB and FINRA. MSRB Notice *available at:* http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2010/2010-10.aspx
[19]FINRA Proposal at page 7.

again raise our significant concerns with the current Proposals from a market participant standpoint.

The Proposals As Currently Drafted Are Not Workable For Market Participants.

The Proposals, as currently drafted, would add significant operational challenges to the confirmation statement process by adding new layers and requirements onto already complex systems. Moreover, to the extent that the Proposals require disclosure that cannot be added to the trade record at the same time as the trade execution, the Proposals create risks to the confirmation statement process.

Notably, the Proposals would require broker-dealers to build a significant new system, at considerable cost, to match trades that meet certain time requirements transaction. By necessity, this system, at the end of the business day, will need to identify all possible matching scenarios for all principal fixed income transactions over the course of the specified time period and navigate an overly complicated – and at times conflicting – matching methodology. The application of these methodologies to situations where there is significant buying and selling activity at varying prices, varying sizes, and across varying business channels can quickly become quite complex.

The operational challenges of the Proposals are especially significant for clearing broker-dealers that would likely be required to coordinate and rely on third parties for data necessary for compliance.

Fully-disclosed clearing broker-dealers clear and settle millions of securities transactions each day for thousands of introducing broker-dealers.[20] Clearing broker-dealers do not sell securities to retail customers. Rather, a fully-disclosed clearing broker-dealer provides routine and ministerial "back office" processing services -- clearance and settlement and custody services -- to introducing broker-dealers. The relationship between the clearing broker-dealer and the introducing broker-dealer and the division of responsibilities between them is set forth in a fully disclosed clearing agreement, which is filed with and approved by FINRA before any clearing services may begin.

Among other back-office functions, clearing broker-dealers settle fixed income trades and print and mail end-customer confirmation statements for introducing broker-dealers. With considerable effort involving the review of multiple principal accounts across all of its introducing broker-dealers, a clearing broker-dealer could likely obtain access to the underlying details of when, how, or for how much the introducing broker-dealer obtained the fixed income security it ultimately sold to its end-customer. More likely, an introducing broker-dealer would need to submit information on a particular trade to its clearing broker-dealer at the end of the business day, after the introducing broker-dealer has determined this information itself.

[20]Because many introducing broker-dealers (aka "correspondents") do not have the net capital, resources, technology, personnel or expertise to clear and settle their own trades, introducing broker-dealers often contract with a third-party clearing broker-dealers to carry their proprietary accounts (if any) and its end-customer accounts and perform back office functions on a fully-disclosed basis (*i.e.*, disclosed to the introducing firm's end customers).

Requiring matched trade information with a full day “look back” conflicts with how trade confirmation statements are processed today, increasing the risk that they will not be completed within regulatory timeframes.[21] Standard industry processing of retail customer trade confirmations involves batching and pricing during the day, processing immediately after market close, overnight composing, with printing and mailing the next business day. For example, at most clearing broker-dealers:

- During the business day, trading occurs in multiple channels throughout the organization and information on these trades moves throughout the day, in real time, to a single “trade prep” location;
- At this location, among other items, calculations are performed and consolidation work is done on the underlying data used to populate the trade confirmation;
- At market close, a file is sent from the “trade prep” location to a trade confirmation engine where the data is formatted and the trade confirmation is composed. This step typically takes place in the 10pm to 2am time window; and
- After the trade confirmation is composed, next steps include, but are not limited to, monitoring, paper fulfillment, or electronic fulfillment.

If the Proposals are approved as currently drafted, at the end of each business day, introducing broker-dealers will need to sift through all of their customer fixed income transaction data for the day to identify and isolate (i) which trades, out of the larger universe of customers trades executed that day, are subject to the disclosure requirements (ii) the price to the introducing broker-dealer of the fixed income security under several different complex methodologies and (iii) mark-up information on the trade, as applicable.

The introducing broker-dealer would then need to transmit this information to its clearing broker-dealer, who would be required to (i) identify the relevant trade out of the broader universe of trades for that day; (ii) pass this information to their trade confirmation engine; and (iii) update the particular trade file in the trade confirmation engine. All of this work would need to be performed, without error or delay, before the established deadlines for passing files to the trade confirmation engine to allow the clearing broker-dealer to print and mail the statement to the end-customer within established regulatory timeframes.

We believe that the current industry practice of processing of trades throughout the business day serves important risk mitigation purposes. Straight-through processing of trade confirmations provides transparency to fixed income trading that helps broker-dealers’ risk management practices. The processing of trades throughout the business day also helps avoid bottlenecks that may affect the timely, accurate, and complete processing of retail customer trade confirmation statements.

[21] From an operational standpoint, we do not see a two hour look-forward/look-back, as the MSRB has proposed, to be different from a full day look back (as FINRA proposes and as the MSRB previously proposed). In both cases a full trading day worth of data must be captured and reviewed at the end of the trading day in order to match certain trades for disclosure purposes.

The Proposals place significant time pressure on the confirmation statement process, particularly in light of current initiatives to shorten the settlement cycle. Exchange Act Rule 10b-10, FINRA Rule 2230 and MSRB Rule G-15 generally require broker-dealers that effect transactions in the account of a customer to provide a confirmation to the customer "at or before the completion of" such transaction. Exchange Act Rule 15c1-1(b) defines "the completion of the transaction" to be, generally, when the customer makes payment to the broker, or when the broker delivers the security to the account of the customer.

As both FINRA and the MSRB are aware, the Depository Trust & Clearing Corporation ("DTCC") is currently leading an industry effort to shorten the U.S. trade settlement cycle for equities, municipal and corporate fixed income bonds, and unit investment trusts ("UITs") from T+3 (trade date plus three days) to T+2 (trade date plus two days).[22] SEC Commissioners Piwowar and Stein have expressed support for the move to T+2 along with SEC Chair Mary Jo White.[23] Moreover, the MSRB has published a request for comment on changes to MSRB Rules to facilitate shortening the securities settlement cycle.[24]

The tension between the Proposals' greater disclosure requirements, which can only be accessed and added to trade confirmation statements at the end of the day, and a shorter settlement cycle, adds complexity and operational risk to the trade confirmation statement process and is a further reason why we believe the Proposals should be withdrawn and alternatives considered.

Certain Aspects of the Proposals Must Be Clarified.

If the Proposals proceed in their current form, certain aspects must be clarified prior to final rulemaking.

Affiliates

Under the MSRB's Proposal, if a municipal securities dealer, on an exclusive basis, acquires municipal securities from [sells to] an affiliate that holds inventory in such securities and transacts with other market participants, the dealer would be required to "look through" the transaction with the affiliated dealer and substitute the affiliates trade with the third party from whom it purchased or to whom it sold the security to determine whether disclosure of the mark-up would be required. In contrast, FINRA proposes to exclude trades where the member's

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[22]Depository Trust & Clearing Corporation, DTCC Recommends Shortening the U.S. Trade Settlement Cycle, April 2014 (advocating for a move to a two-day settlement period).

[23] Commissioners Michael S. Piwowar and Kara M. Stein, Public Statement Regarding Proposals to Shorten the Trade Settlement Cycle (June 29, 2015) *available at*: http://www.sec.gov/news/statement/statement-on-proposals-to-shorten-the-trade-settlement-cycle.html and Letter from Mary Jo White, Chair, Securities and Exchange Commission, to Kenneth E. Bentsen, Jr., President and CEO, Securities Industry and Financial Markets Association, and Paul Schott Stevens, President and CEO, Investment Company Institute (September 16, 2015).

[24]MSRB Regulatory Notice 2015-22 Request for Comment on Changes to MSRB Rules to Facilitate Shortening the Securities Settlement Cycle (November 10, 2015) *available at*: http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2015-22.ashx?la=en

principal trade was executed with an affiliate of the member and the affiliate's position that satisfied this trade was not acquired on the same trading day.

To increase retail customer understanding and to acknowledge efficiencies in market regulation for similar products, FINRA and MSRB confirmation mark-up requirements for principal transactions must be uniform in design and operation. Of the two proposals, we encourage FINRA and the MSRB to follow the MSRB's approach to affiliated dealer trades, which we consider a better approach for retail investors and market participants. If a dealer provides its customers access to a wide selection of secondary market fixed income inventory from multiple sources, the fact that an affiliated dealer is included and treated on par with these sources should not raise regulatory concern. Moreover, as long as the affiliate pricing is competitive with the other sources, the use of an affiliate to the dealer to source the trade should not impact retail customers who ultimately would obtain the best price available for their security.

Use of Standard Mark-up Schedules in lieu of Proposed Disclosure

Certain broker-dealers establish and make available to retail customers schedules of standard charges for fixed income security transactions. To help encourage transparency in fixed income pricing, FINRA and the MSRB should permit broker-dealers to use standard mark-up schedules in place of the proposed mark-up disclosure requirements on retail customer confirmation statements. Standard mark-up schedule disclosure could be conveyed to retail customers via a link to the schedule on the confirmation statement or via annual mailed disclosure in place of the confirmation statement disclosure contemplated by the Proposals. This information would be helpful to retail investors and provide an alternative approach to market participants. Moreover, this approach does not raise operational issues associated with the current Proposals.

Changes to the PMP Should Not Require a New Confirmation Statement

FINRA and the MSRB should clearly state in any final rule that a dealer is permitted, but not required, to resend confirmation statements due solely to a change in the PMP or the differential between the customer price and the PMP. FINRA and the MSRB should also clearly state in any final rule that dealers would expressly be permitted to include a disclaimer on the customer confirmation that the PMP and related differential were determined as of the time of confirmation generation. Among other reasons, from an operational standpoint, in order to resend the confirmation statement, the broker-dealer may need to cancel and rebill the customer's trade to reflect the new reference price. This requirement may contribute to a firm's late trade reporting if such cancel and rebill of the customer trade would be required to be trade reported.

Implementation Timeframe and Cost of Proposals

FINRA and the MSRB have proposed several different methods by which dealers could calculate the proposed mark-up disclosure. Industry participants have similarly proposed alternative methods for this calculation. At this point in time, it is not clear to us which approach will ultimately be taken. We are happy to provide cost estimates on specific aspects of the Proposals once further granularity on the regulatory approach to be taken is available. Similarly, because the time required to comply with the Proposals will depend on the complexity of any final rule, as well as other rules that dealers are asked to implement contemporaneously, we ask FINRA and the MSRB to work with the industry on a proposed implementation timeframe that is responsive to industry needs.

* * * * *

Fidelity thanks FINRA and the MSRB for considering our comments. We would be pleased to provide any further information and respond to any questions that you may have.

Sincerely,

Norman L. Ashkenas
Chief Compliance Officer
Fidelity Brokerage Services, LLC

Richard J. O'Brien
Chief Compliance Officer
National Financial Services, LLC

cc:

Mr. Richard Ketchum, Chairman and Chief Executive Officer, FINRA
Ms. Susan Axelrod, Executive Vice President, Regulatory Operations, FINRA
Mr. Robert Colby, Chief Legal Officer, FINRA

Ms. Lynette Kelly, Executive Director, MSRB
Mr. John A. Bagley, Chief Market Structure Officer, MSRB
Mr. Michael L. Post, Deputy General Counsel, MSRB

Mr. Stephen Luparello, Director, Division of Trading and Markets, SEC
Mr. Gary Goldsholle, Deputy Director, Division of Trading and Markets, SEC
Mr. David Shillman, Associate Director, Division of Trading and Markets, SEC
Ms. Jessica S. Kane, Deputy Director, Office of Municipal Securities, SEC

Fidelity INVESTMENTS

FINANCIAL SERVICES INSTITUTE
VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS
AND INDEPENDENT FINANCIAL ADVISORS

VIA ELECTRONIC MAIL

December 11, 2015

Marcia E. Asquith
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FINRA
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Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
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Re: **FINRA Regulatory Notice 15-36: Pricing Disclosure in the Fixed Income Markets**

MSRB Regulatory Notice 2015-16: Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith and Mr. Smith:

On September 24, 2015 the Municipal Securities Rulemaking Board (MSRB) published Regulatory Notice 2015-16 requesting public comment on proposed recommendations to require confirmation disclosure of mark-ups for specified principal transactions with retail customers.[1] On October 15, 2015 the Financial Industry Regulatory Authority (FINRA) published Regulatory Notice 15-36 requesting public comment on a revised proposal requiring confirmation disclosure of pricing information in corporate and agency debt securities transactions.[2] Both requests represent revised versions of proposals issued for public comment by both self-regulatory organizations (SROs) in November 2014.[3]

The Financial Services Institute[4] (FSI) appreciates the opportunity to comment on these important proposals. We strongly support regulatory actions designed to enhance bond market pricing transparency for retail investors. As we noted in our prior comment letters, we believe that retail investors should have access to timely and complete information regarding fixed income securities to make informed investment decisions. However, we have concerns that the proposals under consideration may detrimentally impact the ability of small firms to service retail bond investors. We respectfully request that FINRA and the MSRB work with the industry to develop a

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[1] Regulatory Notice 2015-16, Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers (Sept. 24, 2015) (MSRB Regulatory Notice).
[2] Regulatory Notice 15-36, Pricing Disclosure in Fixed Income Markets (Oct. 15, 2015) (FINRA Regulatory Notice).
[3] Regulatory Notice 2014-20, Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations (Nov. 17, 2014); Regulatory Notice 14-52, Pricing Disclosure in the Fixed Income Markets (Nov. 17, 2014).
[4] The Financial Services Institute (FSI) is an advocacy association comprised of members from the independent financial services industry, and is the only organization advocating solely on behalf of independent financial advisors and independent financial services firms. Since 2004, through advocacy, education and public awareness, FSI has been working to create a healthier regulatory environment for these members so they can provide affordable, objective financial advice to hard-working Main Street Americans.

joint proposal that achieves its desired goals of ensuring investors have clear understanding of their transactions costs and allows investors to benefit from market competition.

Background on FSI Members

The independent financial services community has been an important and active part of the lives of American investors for more than 40 years. In the U.S., there are approximately 167,000 independent financial advisors, which account for approximately 64.5% percent of all producing registered representatives. These financial advisors are self-employed independent contractors, rather than employees of Independent Broker-Dealers (IBD).

FSI member firms provide business support to financial advisors in addition to supervising their business practices and arranging for the execution and clearing of customer transactions. Independent financial advisors are small-business owners who typically have strong ties to their communities and know their clients personally. These financial advisors provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations and retirement plans with financial education, planning, implementation, and investment monitoring. Due to their unique business model, FSI member firms and their affiliated financial advisors are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their investment goals.

Discussion

Collectively, FINRA and the MSRB request comments on three different pricing disclosure proposals. First, FINRA requests comment on revisions to its matched-trading proposal issued for comment in 2014. Second, both FINRA and the MSRB request comment on an MSRB proposal to require the disclosure of the mark-up or mark-down from the prevailing market price of a security if the firm traded with a retail customer within a two hour time period. Third, the MSRB requests comments on amendments to its matched-trading proposal issued for comment in 2014. We are concerned that each of the proposals under consideration would materially alter the competitive landscape to the detriment of small firms. Additionally, such proposals may result in greater investor confusion. Lastly, we are concerned that should FINRA and the MSRB choose to pursue an incremental approach to pricing disclosure, firms will face materially higher operational and technology expenses. As such, we request FINRA and the MSRB work with stakeholders on a comprehensive pricing disclosure proposal.

In pursuing such a comprehensive pricing disclosure proposal, or any pricing disclosure proposal, we wish to highlight the following items for consideration:

- The disclosure should be based on the prevailing market price for the customer's security;
- The disclosure should leverage existing transparency platforms by requiring the inclusion of links to TRACE and EMMA homepages as well as the time of execution of customer trades on confirmations;
- FINRA and the MSRB should create good faith errors safe harbors for inadvertent mistakes on confirmations; and
- FINRA and the MSRB should undertake initiatives to educate investors on fixed income market structure and the sources of dealer costs in executing trades.

I. FINRA and the MSRB Should Work on a Coordinated Comprehensive Pricing Disclosure Proposal that Preserves the Competitive Landscape

A. Introduction

The proposals raise concerns regarding potential disproportionate impacts on small dealers that ultimately will result in less choice for investors. Regardless of whether pricing disclosure applies to trades within a two-hour time period, or the same day, the proposed disclosure requirements will capture the overwhelming majority, if not the entirety, of transactions executed by smaller dealers, particularly fully-disclosed introducing firms. These dealers do not possess the necessary capital to maintain inventory for a significant time period. We are concerned that mandating disclosure for these transactions may result in the creation of competitive imbalances that will ultimately harm smaller firms to a greater extent than larger dealers and confuse investors seeking to make pricing comparisons across firms of various sizes and models.

In light of the potential detrimental impacts that will be predominantly borne by small firms, we respectfully request that prior to further pursuing rulemaking in this area, FINRA and the MSRB consult with industry stakeholders regarding the entirety of their intentions for fixed income pricing disclosure. We recognize that both FINRA and the MSRB might consider additional bond market pricing transparency initiatives in the future. Such additional measures might capture a larger universe of principal transactions. Understanding the potential for future disclosure requirements will allow regulators and the industry to work together on developing a single comprehensive proposal for providing retail investors with enhanced pricing information. This approach will limit the adverse impacts on small dealers and will ensure that firms are not required to overhaul or rebuild systems shortly after coming into compliance with one of the proposals for which comments are requested.

B. Burdens on Competition

Both FINRA and the MSRB discuss the potential for the proposals to reduce transaction costs and offer customers more competitive prices.[5] The intended goal of pricing disclosure is to incentivize dealers to reduce costs in order to remain competitive in the retail market. However, because the proposals only cover a subset of principal transactions, the proposals will predominantly impact small dealers that primarily transact on a riskless principal basis. Larger dealers that possess the capital to maintain significant inventories could be incentivized to hold positions to avoid disclosure.[6] As such, customers will not be able to effectively compare transaction costs across all market participants. They will not maintain an effective frame of reference to compare transaction costs between smaller introducing firms and larger dealers. Large broker-dealers that can avoid the disclosure period will not feel the downward pressure on their markups, but may paradoxically also receive an influx of new customers. Therefore, we believe that in an effort to ensure an even playing field for firms of all sizes, FINRA and the MSRB should consider a comprehensive pricing disclosure regime that does not limit bond market competition.

Additionally, we are concerned that a disclosure requirement that primarily impacts small dealers may cause these firms to choose to exit the market or only offer investors the opportunity

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[5] FINRA Regulatory Notice, at 9; MSRB Regulatory Notice, at 13-14, 19, 21.
[6] FINRA Regulatory Notice, at 11; MSRB Regulatory Notice, at 16.

to invest in bonds through packaged products such as mutual funds. Sections 15A(b)(9) and 15B(b)(2)(C) of the Securities Exchange Act of 1934 require that FINRA and MSRB rules "not impose any burden on competition not necessary or appropriate in furtherance of the purposes of [the Act]."[7] While we appreciate the SROs including Economic Impact Assessments in accordance with their adopted frameworks, the proposals do not contain detailed discussions or any data regarding the impact on investor choice and access resulting from a reduction in the number of dealers servicing retail investors. Moreover, the proposals do not discuss any potential impacts on issuer borrowing costs or market liquidity that may result from a reduction in dealers. We ask that prior to further pursuing the proposals FINRA and the MSRB analyze the potential for such detrimental impacts and assess all associated costs. We believe that a more comprehensive proposal, rather than an incremental proposal, will help avoid these burdens on competition while increasing transparency for investors.

A comprehensive disclosure regime would also provide operational benefits for firms of all sizes. As we noted in our prior comment letters, confirmation disclosure of any sort, will be a costly and difficult undertaking for firms. These costs will be disproportionately high for small introducing firms which will have to work with clearing firms to alter and design manual systems. Compounding concerns regarding such costs is the possibility that the proposals represent the first step in a process to mandate additional pricing disclosure for all principal fixed income transactions. We are concerned that firms may be asked to build systems and adopt policies and procedures that may be obsolete or require significant overhaul in a matter of several years. In an effort to reduce the implementation burden we request that FINRA and the MSRB consult with the industry on its long-terms plans in an effort for all parties to work together to develop a single proposal that avoids the costs associated with continued incremental enhancements.

C. Regulatory Coordination

It is imperative that any pricing disclosure requirements adopted by FINRA and the MSRB be consistent in design. FINRA and the MSRB seek comment on a variety of proposals, none of which feature complete uniformity in requirements. Consistency is critical to ensure that dealers of all sizes maintain the ability to provide their customers access to a variety of products in a cost effective manner. Differing approaches to disclosure requirements necessitating separate systems and processes for corporate and agency securities as compared to municipal securities will unnecessarily raise compliance costs on broker-dealers. These increased costs may limit the ability of small firms to continue to offer one or more of the subject securities to clients.

Moreover, neither FINRA nor the MSRB has offered justification for differing approaches. The proposals primarily impact back office systems and processes. There is nothing inherently unique to either the market, or the back office systems, for one particular security that necessarily mandates a disclosure regime different from another type of fixed income security. A lack of consistency would only serve to increase costs to firms and confuse investors. A uniform approach is essential to ensuring efficient implementation and management while maximizing investor benefits.

In addition to coordinating with each other, we request that both FINRA and the MSRB work in coordination with the Department of Labor (Department) on its Proposed Class Exemption for

[7] Section 3(f) of the Securities Exchange Act of 1934 also requires the SEC to "consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation" when evaluating a proposed rule.

Principal Transactions in Certain Debt Securities between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs (Principal Transaction PTE).[8] The Department, in conjunction with its proposal to amend the definition of investment advice fiduciary, has proposed to require markup disclosure for principal transactions in the following fixed income securities: U.S. Treasury securities, U.S. agency securities and dollar denominated U.S. corporate securities.[9] The requirement, as proposed, would apply to all principal transactions in those securities.

As we have noted, complying with a pricing disclosure proposal for fixed income transactions presents several operational challenges that will necessitate significant resources by broker-dealers. These challenges will be exponentially increased if firms are required to have different procedures apply to municipal debt securities, corporate and agency debt securities in non-retirement accounts and corporate and agency debt securities in retirement accounts. Such a result could further cause firms to reconsider their ability to offer certain products to investors. It is imperative that FINRA and the MSRB work with the Department to ensure that any markup disclosure requirement that is imposed on firms servicing retirement accounts is consistent with the requirements of a uniform pricing disclosure requirement issued jointly by FINRA and the MSRB.

II. Important Considerations For Pursuing Pricing Disclosure Requirements

A. Introduction

If FINRA and the MSRB further pursue any of the outstanding pricing disclosure proposals, or a more comprehensive proposal, we offer the following recommendations to help create an effective and efficient disclosure regime that is useful to investors. First, we believe that the pricing information to be disclosed should be based on the prevailing market price, which in most cases would be defined as the contemporaneous cost to the dealer. We recommend codifying a conclusive presumption of such definition for situations where there is an offsetting transaction after receiving a customer order. Second, we recommend that confirmations include the URL addresses of the homepages for TRACE and EMMA as well as the time of execution of the customer trade. Third, we suggest creating a good faith error safe harbor for instances where human error has inadvertently resulted in an inaccuracy on a customer confirmation. Lastly, we request that FINRA and the MSRB work with stakeholders to improve investor understanding of the fixed income markets and transaction pricing in an effort to put the disclosed pricing information in proper context.

B. Prevailing Market Price

We recommend that any potential pricing disclosure for transactions in fixed income securities should be based on the prevailing market price for the security at the time of the customer's trade. Utilizing the prevailing market price will ensure customers receive the most reasonably accurate understanding of the cost of their trade. Moreover, structuring pricing disclosure around prevailing market price will align any new disclosure requirements with existing fair pricing policies enforced by both FINRA and the MSRB.[10] We recognize that there may be transactions for which determining the prevailing market price may be complicated. We look forward to

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[8] 80 Fed. Reg. 21989 (April 20, 2015).
[9] *Id.* at 22003. The Department of Labor proposal would prohibit a broker-dealer from transacting in municipal securities with an IRA owner or employee benefit plan as a principal.
[10] FINRA Rule 2121; MSRB Rule G-30.

working with FINRA and MSRB on determining how to represent prevailing market price in situations where it may not be readily determinable.

Additionally, utilizing prevailing market prices would reduce the operational impacts of any pricing disclosure proposal. Small broker-dealers maintain manual processes to input the transaction information into a confirmation system and transmit that information to their clearing firm. The prospect of having to calculate reference prices based on an array of factors has caused some firms to believe they will need to hire additional personnel to handle confirmation inputs. Additionally, the prospect of human error increases in conjunction with an increase in the amount of information that must be inputted. Simplifying the required information to be disclosed should help reduce the costs and ease the implementation burden to be imposed on small dealers.

Lastly, we believe that in establishing the prevailing market price for the customer's security, there should be a rebuttable presumption codified in FINRA and MSRB rules for transactions where the firm refers to its contemporaneous costs. In most retail transactions, contemporaneous costs have long been considered a key factor in determining prevailing market price. We believe that codifying such a rebuttable presumption will provide necessary comfort to firms designing new systems and processes. Moreover, we believe the presumption of contemporaneous costs should be conclusive in situations where the dealer, after receiving an order for a security, executes a transaction to offset the customer's purchase or sale. In such a scenario the offsetting trade is usually very close in time to the customer trade such that considering additional factors for the determination of prevailing market price is unnecessary. We believe firms would appreciate the certainty in codifying a conclusive presumption for such trading scenarios.

C. Requiring Links to TRACE and EMMA

We appreciate FINRA and the MSRB's commitment to pursuing opportunities to increase promotion of the existing pricing transparency platforms, TRACE and EMMA. In our prior letters we recommended including a link to the appropriate website on the back of customer confirmations for fixed income securities trades. In their revised proposals, both FINRA and the MSRB note that these platforms are useful to inform investors of the market for their security at the time of their trade. The MSRB has proposed requiring the inclusion on the confirmations of all transactions for non-institutional customers of a hyperlink and URL address to the Security Details page for the customer's security on EMMA.[11] Additionally, the confirmation must also include a brief description of the type of information available on the page. The MSRB has further proposed to require the disclosure of the time of execution for a customer's trade to nearest minute.[12] Alternatively, FINRA has proposed including a link to TRACE on confirmations for corporate and agency securities.[13]

In assessing the impacts of requiring links to TRACE and EMMA on confirmations we wish to reiterate the importance of a consistent approach by FINRA and the MSRB. Consistent requirements are critical to limiting implementation burdens for firms. We suggest initially requiring a link to the TRACE or EMMA homepage and requiring the disclosure of the time of

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[11] MSRB Regulatory Notice, at 12.
[12] *Id.* at 12-13.
[13] FINRA Regulatory Notice, at 5.

execution of the customer's trade.[14] We believe that including such a link in conjunction with the CUSIP number and time of execution will greatly assist investors in understanding the market for their security at the time of their trade. While including this additional information will necessitate changes to existing systems, we believe such changes are warranted and consistent with our belief that FINRA and the MSRB should seek to leverage existing transparency platforms in adopting pricing disclosure reforms.[15]

D. Safe Harbor for Good Faith Errors

In its proposal the MSRB specifically requests comment on a proposed amendment to its matched trading proposal that specifies that dealers would not be required to resend a confirmation solely due to a change in the reference transaction to be selected, the reference transaction price, or the differential between the customer price and the reference price.[16] We appreciate the MSRB's consideration of such a requirement and respectfully request that a similar provision be included in any proposal adopted by FINRA and the MSRB.

As we have discussed, including additional pricing information on customer confirmations will necessitate significant changes to systems and processes for both introducing and clearing firms. Clearing firms will need to adjust their interfaces to allow introducing firms to manually input the additional fields required on the confirmations. Clearing firms must then capture such information, store it, and provide correspondents an opportunity to review and correct the information to be included on the confirmation. Such manual processes necessitate an investment of time by introducing firm personnel and carry a significant degree of operational risk. These processes carry a significant likelihood of human error that will result in increased costs to firms to correct inaccurate information.

Moreover, these difficulties are further compounded by the shortened settlement cycle initiative that is currently underway.[17] Small firms will typically input and transmit all information to be included on confirmations to their clearing firms at the end of the trade day. Moreover, the matched trading proposals would effectively require such end of day reporting. Requiring additional information to be manually inputted while also shortening the time for completion and transmission of such information only increases the costs and risk to introducing firms.

Therefore, we request that FINRA and the MSRB consider including a good faith safe harbor to ease the burden on small fully-disclosed introducing firms. Such a safe harbor would ensure that dealers would not be required to resend a confirmation, should printed information be mistakenly inaccurate so long as the dealer undertook a good faith effort to include accurate information on the confirmation and the correct identity and pricing information is available to the customer on an account statement or through online account access. Firms wishing to avail

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[14] Limiting the requirement to the TRACE or EMMA homepage would still provide the opportunity to assess whether the inclusion of such a link materially impacts investor traffic to such web-platforms. FINRA and the MSRB could always choose to revise such a requirement to include a security-specific link if it was necessary.

[15] These operational and technological impacts would be significantly greater if a security specific link were to be required. In addition to developing the technology to ensure inclusion of the appropriate link on a transaction-by-transaction basis, dealers would need to adopt policies and procedures to manually check each URL prior to submission to ensure that it is the correct link for the customer's security. We do not believe that the benefits of including a security-specific link outweigh these significant costs.

[16] MSRB Regulatory Notice, at 24.

[17] *See* Letter from Mary Jo White, Chair, SEC, to Kenneth E. Bentsen, Jr., President & CEO, SIFMA & Paul Schott Stevens, President & CEO, ICI (Sept. 16, 2015); *see also* MSRB Regulatory Notice 2015-22.

themselves of such a safe harbor would need to state on the confirmation that in the event printed information contains technical inaccuracies or errors, the corrected information will be available to the client on either an account statement or through online account access. Providing such a safe harbor would significantly reduce the operational impacts on small firms – as well as medium and large firms – and may positively contribute to small firms' decisions to continue to offer fixed income securities to retail investors.

E. Investor Education of Fixed Income Trading and Pricing

Should FINRA and the MSRB choose to pursue pricing disclosure requirements for retail fixed income transactions where the dealer acts as principal, we believe they should also undertake initiatives to seek to better educate investors about the structure of the secondary fixed income markets. Such education is necessary to put pricing information in context. Pricing information absent context may be confusing and inaccurate. Customers need contextual explanations to understand why they were charged for the transaction and why these services are necessary to effect their investment decisions. Educating investors on the roles that broker-dealers play in executing fixed income securities transactions and the steps that must be undertaken to fairly and reasonably fill a customer order are as essential as pricing information. We respectfully request FINRA and the MSRB undertake initiatives to provide such education and we stand ready to assist such efforts in any way we can.

Conclusion

We are committed to constructive engagement in the regulatory process and welcome the opportunity to work with FINRA and the MSRB on these and other important regulatory efforts. We believe that a more comprehensive approach will better balance the importance of increasing transparency for investors with ensuring investor choice and access to firms of all sizes.

Thank you for considering FSI's comments. Should you have any questions, please contact me at (202) 803-6061.

Respectfully submitted,

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LPL Financial

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December 10, 2015

Via Electronic Submission

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Re: *FINRA Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets MSRB Regulatory Notice 2015-16, Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers*

Dear Ms. Asquith and Mr. Smith:

LPL Financial LLC ("**LPL**") welcomes the opportunity to comment on the Financial Industry Regulatory Authority's ("**FINRA**") Regulatory Notice 15-36 ("**FINRA Proposal**") and the Municipal Securities Rulemaking Board's ("**MSRB**") Regulatory Notice 2015-16 ("**MSRB Proposal**", collectively the "**Proposed Rules**").[1] We commend FINRA and the MSRB for the consideration given to the comments provided on the previous proposals and the revisions made to address these comments.

LPL supports the efforts of FINRA and the MSRB to improve transparency for investors regarding fixed income transactions by requiring disclosure of mark-ups and mark-downs on confirmations. We recommend a consistent approach that uses prevailing market price to calculate the mark-up or mark-down. To the extent that regulators anticipate further rulemakings to apply similar disclosure requirements to categories of fixed income securities not addressed by the Proposals, LPL respectfully requests that the MSRB and FINRA consider adopting a standard that could also be applied to those other categories. Given the operational challenges involved in adding the disclosures to confirmations, we recommend that regulators afford 18 to 24 months to implement the ultimate changes resulting from the Proposals. We hope that

[1] *See* FINRA Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets (Oct. 12, 2015), available at: https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-15-36.pdf (last visited Dec. 9, 2015) [referred to herein as the "FINRA Proposal"]; MSRB Regulatory Notice 2015-16, Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers (Sept. 24, 2015), available at: http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2015-16.ashx (last visited Dec. 9, 2015) [referred to herein as the "MSRB Proposal"].

FINRA and the MSRB find our comments helpful and we look forward to continued collaborations with FINRA and the MSRB on these important Proposals.

I. Overview of LPL

LPL is a leader in the retail financial advice market and, as of September 30, 2015, serves about $462 billion in advisory and brokerage assets. LPL is one of the fastest growing RIA custodians and is the nation's largest independent broker-dealer.[2] We provide proprietary technology solutions, comprehensive clearing and compliance services, practice management programs and training, and independent research to more than 14,000 independent financial advisors and over 700 banks and credit unions. Our financial advisors provide financial advice to investors with assets in approximately 4.6 million client accounts. They service an estimated 40,000 retirement plans with an estimated $115 billion in retirement plan assets, as of September 30, 2015. LPL also supports approximately 4,300 financial advisors licensed and affiliated with insurance companies with customized clearing, advisory platforms and technology solutions. LPL and its affiliates have about 3,400 employees with primary offices in Boston, Charlotte, and San Diego.

LPL helps independent financial advisors establish their own successful businesses through which they can offer independent financial guidance and advice to investors. Our independent financial advisors build long-term relationships with their clients and communities across the U.S. by guiding them through the complexities of investment decisions, retirement solutions, financial planning, and wealth management. In addition, LPL supports financial advisors and program managers at community and regional banks and credit unions by enabling them to offer investors a wide array of investment, advisory, and insurance products.

LPL executes fixed income trades for investors on an agency or riskless principal basis. LPL does not take positions in fixed income securities nor does it trade fixed income securities on a proprietary basis.

II. Overview of the Proposals

Both Proposals are designed to provide greater transparency in the area of fixed income mark-ups and mark-downs. The Proposals seek to accomplish this by requiring firms to disclose additional information about the remuneration earned by the firm in fixed income transactions that are executed for retail customers on a principal basis (including riskless principal). The disclosure requirements in the both Proposals are triggered when a firm executes a buy (sell) transaction as principal in the same security as a retail customer's sell (buy) transaction but differ

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[2] *See* C. Paikert, FP50: New Ways to Get Huge, FINANCIAL PLANNING (June 1, 2015), available at: http://www.financial-planning.com/news/industry/fp50-new-ways-to-get-huge-2693025-1.html (last visited Dec. 9, 2015).

with respect to the required timing of those transactions. The FINRA Proposal requires disclosure if the principal transaction is executed within the same day as the customer transaction. The MSRB Proposal, on the other hand, requires disclosure only if the principal transaction(s) is executed by the firm within two hours of the customer transaction.

The Proposals also require firms to disclose different information with respect to mark-ups or mark-downs earned by the firm on the principal transaction. The FINRA Proposal requires disclosure of the price paid by the customer, the price paid by the firm for the principal transaction[3], the differential between the price to the customer and the firm's price, and a hyperlink to additional information on the Trade Reporting and Compliance Engine ("**TRACE**"). In contrast, the MSRB Proposal requires disclosure of the firm's mark-up or mark-down from the prevailing market price expressed as both a total dollar amount and percentage. The prevailing market price for these purposes is derived from the firm's purchases (sales) that meet or exceed the size of the customer's sale (purchase) within two hours of the customer transaction. In addition, firms are required to include a hyperlink to the Electronic Municipal Market Access ("**EMMA**").

III. Recommendations

A. Disclosing Mark-ups and Mark-downs Using Prevailing Market Price

The MSRB Proposal provides statements of the SEC Commissioners calling for disclosure of mark-ups and mark-downs to help investors understand their transaction costs.[4] LPL supports this initiative and recognizes the benefits to investors resulting from increased transparency regarding fixed income securities transactions. In addition to satisfying the SEC's objective, the MSRB Proposal's basis for calculating the mark-ups and mark-downs is consistent with existing regulatory guidance regarding the prevailing market price.[5] LPL supports using the prevailing market price methodology for calculating the mark-up or mark-down and recommends that the proposed approach apply to all categories of retail principal transactions in the categories of securities listed in the Proposed Rule.[6]

[3] The price paid by the firm is referred to by FINRA as the "Reference Price".

[4] *See* MSRB Proposal, notes 15-17.

[5] *See, e.g.*, MSRB Rule G-30.01(d) Supplementary Material (stating in relevant part, "[d]ealer compensation on a principal transaction is considered to be a mark-up or mark-down that is computed from the inter-dealer market price prevailing at the time of the customer transaction"). We do not take a position as to the appropriateness of the different proposed time constraints for identifying prevailing market price.

[6] For firms such as LPL that transact primarily as riskless principal, the prevailing market price presumptively will be the firm's contemporaneous cost.

B. The Proposals Should Be Consistent and Should Strive for Consistency with Potential Additional Proposals Covering Fixed Income Products

By requiring firms to adhere to a single standard – *i.e.*, disclosure of the mark-up or mark-down based on the prevailing market price – firms will only have to implement a single solution to comply with both Proposals.[7] A single standard is operationally more efficient and can still provide investors with transparency about mark-ups and mark-downs. Further, the calculation of mark-ups or mark-downs based on prevailing market price is relevant to retail transactions in all categories of fixed income securities including corporate, agency, and municipal, and any other categories that may in the future become subject to disclosure requirements similar to those discussed in the Proposals. We ask that the proposed disclosure requirements be structured such that they could be consistent with any future requirements for disclosure of mark-ups and mark-downs for other categories of fixed income products.

LPL also notes that the Department of Labor ("**DOL**") has proposed, as part of its fiduciary rule principal transaction exemption proposal, a requirement that firms provide the mark-up or mark-down on a principal transaction to investors before obtaining consent to a transaction, and then again on the confirmation.[8] To avoid requirements that could overlap or be inconsistent with each other, we respectfully request that the regulators coordinate their requirements for confirmation disclosures.

A single standard for confirmation disclosures of mark-ups and mark-downs would be less confusing to investors. One of the primary purposes of the transaction confirmation is to provide "a means by which to evaluate the costs of . . . [a] transaction and the quality of . . . [the] broker-dealer's execution."[9] If the means by which a customer evaluates the cost of a transaction changes with each category of fixed income product, and the customer does not understand the differences between each disclosure requirement, the overall value of the disclosure will diminish. Applying a single standard to all fixed income security transactions will lessen the likelihood of customer confusion while continuing to provide important transparency.

C. Sufficient Time to Implement

Implementing the new confirmation disclosure requirements will be operationally challenging. In order to prepare information for a confirmation that includes the relevant mark-

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[7] *See* FINRA Proposal at 6 (stating, in relevant part: "[w]hile FINRA and the MSRB's revised proposals currently differ, both entities favor a coordinated approach.").

[8] *See* Proposed Class Exemption for Principal Transactions in Certain Debt Securities between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs, 80 FR 21989 (April 20, 2015).

[9] *See* SEC Investor Bulletin, *How to Read Confirmation Statements* (Sept. 2012), available at: https://www.sec.gov/investor/alerts/ib_confirmations.pdf (last visited Dec. 9, 2015).

up or mark-down, firms will likely need to implement time-consuming system changes. Among other things, firms will need to develop real-time systems to identify related transactions and that are capable of identifying and accounting for any cancellations and corrections. Significant coordination will be required with third party vendors that assist with the creation, processing, and distribution of the confirmations. LPL believes the system changes and the testing of those system changes will require significant time to complete, and asks FINRA and the MSRB to consider providing 18 to 24 months for implementation.

* * * * *

We appreciate your consideration of these comments. We respectfully submit that the recommendations discussed in this letter will help to clarify the new rule requirements while fulfilling the key purposes underlying the Proposals. We would be pleased to provide additional information regarding any of these issues. If you have any questions regarding this letter or would like to discuss any of these points further, please do not hesitate to contact me or Sarah Gill, Senior Vice President and Head of Policy, Government Relations, at (202) 510-1025.

Sincerely,

David Berg

David P. Bergers

PIABA
protecting public investors

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December 8, 2015

Submitted via email to pubcom@finra.org
Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Submitted electronically
Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: FINRA Regulatory Notice 15-36: Request for Comment on Pricing Disclosure in the Fixed Income Markets
MSRB Regulatory Notice 2015-16: Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith & Mr. Smith:

I write on behalf of the Public Investors Arbitration Bar Association ("PIABA"), an international bar association comprised of attorneys who represent investors in securities arbitrations. Since its formation in 1990, PIABA has promoted the interests of the public investor in all securities and commodities arbitration forums, while also advocating for public education regarding investment fraud and industry misconduct. Our members and their clients have a strong interest in rules promulgated by the Financial Industry Regulatory Authority ("FINRA") and the Municipal Securities Rulemaking Board (MSRB) relating to both investor protection and disclosures to public investors.

FINRA has reissued its request for comment on a proposed FINRA rule that would require firms to disclose additional information on customer confirmations for transactions in fixed income securities. Specifically, for corporate and agency debt securities, FINRA is proposing that firms disclose the price to the customer, the member's reference price, and the differential between those two prices, along with a reference and hyperlink, if available, to the TRACE publicly available trading data. However, this information must be disclosed only if certain conditions are met. The MSRB has also requested comment on a similar proposal to require confirmation disclosure of mark-ups for specified principal transactions in municipal debt securities.

PIABA generally applauds any effort to provide more transparency in the securities trading arena, and specifically with respect to debt securities. FINRA has restructured the proposed rule to eliminate the “qualifying size” aspect of the previous proposal, replacing it with a “retail customer” standard. PIABA supports this change and agrees that the rule should apply to all retail customer account regardless of the size of the transaction.

The proposed rule limits disclosure of this information to only those transactions where the firm has executed a transaction as a principal in the same security within the same day that equals or exceeds the size of the customer transaction. PIABA believes that this is too limited. PIABA would like to see fixed income trade confirmations disclose the actual markups/markdowns, not only for riskless transactions, but for all fixed income retail transactions.

As the rule stands now, the markup/markdown disclosure would be required only if there are corresponding firm trades on the same day. Regulatory Notice 14-52 provided several examples of possible scenarios which set forth when disclosure would and would not have to be made. For example, in RN 14-52 example 13, disclosure would not be required where Firm A sold 100 XYZ bonds to its customer on Day 2, if 50 of the bonds having been sourced at 15:30:00 PM on Day 1 and 50 of them having been sourced at 10:00:00 AM on Day 2. PIABA would prefer that all of the pricing information be disclosed, regardless of whether the bonds sold to the customer were sourced on Day 1 or Day 2. At a bare minimum, pricing information should be provided for the 50 bonds that were sourced on Day 2 – the day on which the bonds were sold to the client. Absent such a requirement, there is a meaningful incentive for member firms to game the system by sourcing a single bond for each customer sale from old inventory, thereby avoiding entirely the need to disclose the markup/markdown.

With respect to the approach proposed by the MSRB, PIABA feels the MSRB unnecessarily limits the time period it looks at when determining when information needs to be disclosed. The MSRB would only require disclosure if the principal transaction occurs within two hours preceding or following the customer transaction. This is unnecessarily limited. As stated above, PIABA believes this information should be disclosed in all cases, but at a minimum, for transactions occurring in the same day.

The new proposal also permits a firm to not disclose pricing information if there has been a material change in the price of the security between the time of the principal transaction and the customer transaction. PIABA is concerned that the proposal allows the firm to exercise too much discretion in whether to disclose the price along with clarifying information explaining the change in price, or simply not disclose the price at all. FINRA should provide guidance on what it considers a material change. For example, FINRA should provide a minimum percentage change in price or other objective measure.

Further, PIABA does not understand the need for this discretion. The firm should be required to disclose the price and the reason for the material change in price. This information should be readily ascertainable and should be disclosed to the customer. Alternatively, the firm should be required to disclose that there had been a material change in price and that the customer should contact their broker for more information.

PIABA also believes that FINRA should work to unify its rule with the MSRB proposal. Customers should receive uniform information about debt securities, including corporate and agency bonds and municipal bonds. Firms should provide both the reference price and the mark-up or mark-down from the prevailing market price to the extent the two are different. PIABA is supportive of the MSRB proposal in that it looks through the firm to its affiliates for purposes of determining when a transaction is a “principal” transaction.

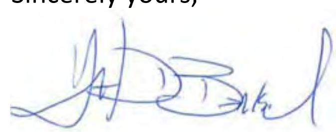
Abuse of undisclosed markups and markdowns is not a hypothetical problem. The last few years have seen FINRA pursue a number of disciplinary actions against member firms concerning excessive markups and markdowns of debt instruments. For example, in 2012, FINRA fined Citi International Financial Services LLC $600,000 and ordered more than $648,000 in restitution and interest to more than 3,600 customers for charging excessive markups and markdowns on corporate and agency bond transactions.[1] In 2013, FINRA fined StateTrust Investments, Inc. over $1 million for charging excessive markups and markdowns in corporate bond transactions and ordered the firm to pay more than $353,000 in restitution and interest to customers who received unfair prices. FINRA found that 85 of the transactions, in particular, operated as a fraud or deceit upon the customers.[2] Also in 2013, FINRA fined Morgan Stanley Smith Barney LLC and Morgan Stanley & Co. LLC $1 million and ordered $188,000 in restitution plus interest for failing to provide best execution in certain customer transactions involving corporate and agency bonds, and failing to provide a fair and reasonable price in certain customer transactions involving municipal bonds.[3] Had the pricing information been available to the customers on the confirmations, perhaps the customers would have been charged fair prices.

To be clear: PIABA supports the amendments to FINRA Rule 2232 and MSRB Rule G-15 insomuch as they create greater transparency in retail fixed income trading. However, PIABA requests the amendments not be limited in scope or time and apply to affiliate transactions and to transactions that occur outside the limited windows proposed by both FINRA and the MSRB. There is nothing to indicate that unfair pricing or excessive markups and markdowns only occur when the transaction is sourced from a same-day principal trade.

Ultimately, PIABA requests that the MSRB and FINRA move forward on these proposals. Both entities issued initial proposals a year ago. The MSRB notes that the SEC has expressed concerns about transparency in the municipal securities market since 2012. The disciplinary actions cited above demonstrate that there have been issued in the corporate and agency debt markets for some time as well. However, neither entity has yet proposed a rule to the SEC. At the current pace, it will be some time before rules are enacted. PIABA urges each entity to expedite this process and act expeditiously to protect customers who are participating in the debt securities markets.

Thank you for the opportunity to comment on the rule proposal.

Sincerely yours,



Hugh D. Berkson
PIABA President

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[1] *See* http://www.finra.org/newsroom/newsreleases/2012/p125821.
[2] *See* http://www.finra.org/Newsroom/NewsReleases/2013/P288973.
[3] *See* http://www.finra.org/Newsroom/NewsReleases/2013/P317817.

charles SCHWAB

December 11, 2015

BY ELECTRONIC MAIL

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Financial Industry Regulatory Authority 1735 K Street, NW
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Ronald W. Smith
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Re: FINRA Regulatory Notice 15-36,
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2015-16,
Request for Comment on Draft Rule Amendments to
Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith and Mr. Smith:

Charles Schwab & Co. Inc. ("Schwab") appreciates the opportunity to comment on the recent rule proposals by the Financial Industry Regulatory Authority ("FINRA") and the Municipal Securities Rulemaking Board (the "MSRB") regarding the disclosure of certain pricing and mark-up or mark-down (collectively "mark-up") information on customer confirmations for qualifying retail transactions in fixed income securities (the "2015 FINRA Proposal", the "2015 MSRB Proposal", and collectively the "2015 Proposals").

Schwab understands that the 2015 Proposals are an attempt to address the comments and concerns raised in response to FINRA Regulatory Notice 14-52 and MSRB Notice 2014-20 (the "2014 FINRA Proposal", the "2014 MSRB Proposal", and collectively the "2014 Proposals").

Schwab has been a long-time proponent of disclosing transaction-related costs across all asset classes and currently provides information on confirmations for customers on its retail platform related to the mark-ups it charges on municipal, corporate, and government agency bond transactions. Schwab believes that it is important for investors to understand how bond pricing works and how the associated costs will ultimately determine the price of the bond they purchase or sell. Schwab has made resources available to its clients that describe how bonds are priced and how those prices can ultimately impact the yield received on a bond transaction. In addition, Schwab makes available to its clients pricing information from both FINRA and the MSRB. Schwab firmly believes that the more investors understand about pricing and the markets, the better they will be able to judge the fairness and value of the services they receive. To that end and as further described below, Schwab believes that an expanded approach to disclosing transaction related costs coupled with consistent and reasonable rulemaking in this area would be helpful to market participants and retail investors alike.

Schwab appreciates FINRA's and the MSRB's willingness to listen to and incorporate some of the feedback provided in response to the 2014 Proposals into the 2015 Proposals. While both sets of Proposals have been an important step toward improving price transparency and better informing retail investors' understanding of the fixed income securities markets, as more fully described below, Schwab believes that an expanded approach to mark-up/pricing disclosure whereby all principal transactions are included can have a greater impact for retail investors and the market as a whole.

Concerns with the 2014 and 2015 Proposals

Schwab, like many other market participants, believes that using a "reference price"[1] as proposed by FINRA would not have the intended effect of increasing transparency into transaction costs and dealer compensation related to fixed income transactions. Rather, we believe that such an approach would be difficult for dealers to implement, potentially difficult for retail investors to understand, and most importantly, may not provide meaningful information related to the costs associated with a particular transaction. As the MSRB succinctly explained in its 2015 Proposal, the reference price approach would, "utilize potentially complicated methodologies to determine which of the potentially many transactions should be used as a comparator for purposes of disclosing to the customer pricing reference information".[2] Schwab believes that such a complicated approach would not necessarily improve transparency nor would it improve retail investors' understanding of the fixed income securities markets. In fact, it has the potential to exacerbate investor confusion.

For example, under the proposed "reference price" methodology, a customer might receive a reference price disclosure for the execution of one lot of a particular order, but no disclosure for another lot of the same order. Another possible scenario is that a particular reference price disclosure would infer that a dealer lost money on a transaction with a customer, even though a mark-up was charged. If a goal of the Proposals is to provide greater transparency into transaction costs and dealer

[1] See FINRA Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets (October 2015).
[2] See MSRB Notice 2015-16, Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers (September 2015).

compensation associated with trading fixed income securities, Schwab believes that a reference price approach would result in many scenarios that would not meet that objective.

While Schwab is in agreement with both FINRA and the MSRB that pricing and mark-up disclosure has the potential to positively impact the market, we believe that the 2015 Proposals are either too complex (as described above), or may not go far enough in providing meaningful pricing/mark-up information to retail investors (as more fully described below).

First and foremost, Schwab believes it is imperative that FINRA and the MSRB coordinate with each other to ensure that their proposals are consistent, except for any differences mandated by the unique market structures of the covered securities. As presently written, the two proposals are markedly different and would be expensive and difficult to implement and maintain in parallel, and ultimately would confuse retail investors and stray from the stated objectives of the Proposals. In addition, FINRA and the MSRB must also consider pending rulemaking by the Department of Labor,[3] which in its present form would impose yet another disclosure regime for certain principal fixed income transactions in retirement accounts.

At a high level, under the 2015 FINRA Proposal, with some exceptions, for specified security transactions occurring on the same trading day, firms/members would be required to disclose on retail customer confirmations: the price to the customer; the firm's "reference price"; and the difference between the two prices. Generally speaking, the "reference price" would be based upon the price at which the firm/member acquired or sold the subject security on the same trading day.

Under the 2015 MSRB Proposal, firms/members would be required to disclose on retail customer confirmations its mark-up or mark-down (collectively "mark-up") from the "prevailing market price" for the security, expressed as a total dollar amount and as a percentage of the principal amount of the transaction for principal transactions for which the firm had transacted on the same side of the market within the two hours preceding or following the customer transaction.

Of the two 2015 Proposals, Schwab believes the 2015 MSRB Proposal has the greatest potential to be effective at achieving the stated goals of FINRA, the MSRB, and the Securities and Exchange Commission[4] in the area of fixed income price transparency. As noted above, under the 2015 MSRB Proposal, the mark-up required to be disclosed would be the difference between the price to the customer and the prevailing market

[3] Department of Labor, Employee Benefits Security Administration. Proposed Class Exemption for Principal Transactions in Certain Debt Securities between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs, Application No. D-11713 [ZRIN: 1210-ZA25], 80 Federal Register 21989 (April. 20, 2015).
[4] U.S. Securities and Exchange Commission, Report on the Municipal Securities Market,(July 31, 2012).

price ("PMP") for the security. The presumption as noted in the 2015 MSRB Proposal is that the PMP for the security would be established by referring to the dealer's contemporaneous cost as incurred, or the contemporaneous proceeds as obtained, which is consistent with applicable MSRB and FINRA rules.[5]

Schwab is concerned that any "reference price" methodology may too often fail to provide customers with clear and accurate disclosure of dealer mark-ups. Disclosure of differences between customer prices and reference prices for dealer risk trades will reflect market price fluctuations and, as previously mentioned, may infer a dealer loss on a transaction with a customer for which the dealer charged a mark-up.

Additionally, proposed reference price differential disclosures would require dealers to delay the confirmation process until the end of the day, potentially presenting significant operational and technological challenges. More importantly, delaying the calculation of the required disclosure until the end of the day would preclude dealers who wish to do so from providing the disclosure to customers at the point of sale. Customers of those dealers who disclose mark-ups at point of sale will inevitably be confused by reference price differential disclosures on trade confirmations that differ from the dealers' point of sale mark-up disclosures. This is one reason Schwab believes it is imperative that the disclosure requirement be based on a price that already exists at the time of trade, such as the PMP, rather than on prices that occur in the future.

<u>Schwab Supports Expanding the MSRB's Proposal to Include All Principal Trades</u>
While we agree with the general principles of the MSRB's Proposal, Schwab recommends going further. We believe that disclosing the mark-up from the PMP for all principal trades in municipal, corporate, and government agency bonds regardless of the time frame or whether the dealer had transacted on the same side of the market would provide even greater transparency into the compensation and costs associated with the execution of transactions and would provide significantly more benefits to investors and to the marketplace as a whole. In addition to providing increased benefits to retail investors, Schwab believes that such an approach would also more closely align the fixed income markets with the disclosure requirements currently in place in the equity markets.

As noted in the 2015 MSRB Proposal, in principal transactions, "...the total transaction price to the customer must bear a reasonable relationship to the prevailing market price of the security at the time of the customer transaction, and the mark-up, as part of the aggregate price, must also be fair and reasonable. For purposes of [MSRB] Rule G-30, the mark-up is calculated based on the inter-dealer market price prevailing at the time of the customer transaction." As the MSRB notes in their Proposal, dealers are already subject to regulatory obligations related to the fairness and reasonableness of mark-ups, and the determination of PMP in connection with the establishment of a fair price, as such, it is a reasonable assumption that dealers should be able to provide the

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[5] See MSRB Rule G-30 and FINRA 2120.

amount of the mark-up over the PMP for all principal transactions, not just those for which they've transacted on the same side of the market within two hours of the customer's transaction or during the same trading day.

Under this expanded disclosure approach, dealers and customers would not have to interpret newly defined terms such as "reference price", "complex trades", or the timing of "specified principal transactions." Nor would dealers need to determine if there is a specified trade size associated with the customer's transaction. As the MSRB notes in its 2015 Proposal when discussing an alternative regulatory approach which would include all principal transactions, "[S]uch a requirement may eliminate the need for dealers to develop any type of matching utility to determine which customers receive disclosure and would allow confirmations to be printed immediately following the customer's transaction." Dealers would simply need to disclose the mark-up from the PMP which they presumptively have already calculated. This approach would be consistent with current requirements to disclose agency commissions on fixed income transactions. As long as dealers are held to the same standards for calculating PMP, Schwab believes that this approach would provide investors with even greater transparency into the compensation of their dealers and the costs associated with the execution of their transaction. Schwab believes that this approach would also simplify dealer obligations under the 2015 Proposals and mitigate behavior, intentional or not, that could lead to the appearance of circumventing the intended benefits of the 2015 Proposals.

While Schwab believes that this approach is more straightforward and would achieve both FINRA's and the MSRB's stated objectives, it would likely require updated guidance from both FINRA and the MSRB on the determination of PMP and on what constitutes a mark-up. Collectively, this guidance could equate to a "reset" for dealer expectations and go a long way toward ensuring a level playing field going forward.

Additional Comments

Disclosure Format
Schwab is supportive of the MSRB's proposal to express the mark-up both as a total dollar amount and as a percentage of the principal of the customer transaction. Schwab requests that sufficient time be allowed for required system updates to be made in order to implement these changes.

Retail Customers in the Secondary Market
Schwab supports using a definitional approach in identifying which trades would be subject to the disclosure requirements of the 2015 Proposals. Schwab feels that a "retail account" or "non-institutional account" as defined by FINRA and MSRB rules is a more appropriate method to capture covered transactions as opposed to the $100,000 par amount threshold put forth in the 2014 Proposals. In addition, Schwab supports limiting disclosure obligations to transactions which occur in the secondary market.

"Look Through" for Specified Trading Structures

Schwab strongly believes that any final rule must include a "look through" provision for specified trading structures. Schwab agrees with the MSRB assertion that such a provision would ensure that the mark-up disclosed is a more accurate indication of the compensation paid by customers when affiliated dealers effectively function as a single entity for the purposes of executing customer transactions. If such transactions were not captured by the rule, Schwab believes that customers of firms who have separate trading desks within affiliated entities would not be afforded the benefits intended by the 2015 Proposals. Such disclosure would, in our opinion, help ensure a level playing field for all market participants.

Functionally Separate Trading Desks

While Schwab understands and generally agrees with the reasoning behind excluding transactions effected on functionally separate trading desks from the disclosure requirements of the 2015 Proposals, we believe that such exclusions must be coupled with information walls and rigorous oversight. Lack of such controls could limit the manifestation of the 2015 Proposals' stated objectives.

Security-Specific Link to EMMA and TRACE, and Time of Execution

Schwab is supportive of the proposal to add a security-specific link to EMMA and FINRA's TRACE websites. Schwab believes that the additional information available on EMMA and TRACE can be a valuable resource for investors and market participants. As both FINRA and the MSRB can appreciate, the provision of security-specific links will require a great deal of coordination with industry participants to ensure that links remain functional and accurate. FINRA and the MSRB would have to commit to a process by which they notify industry participants of planned updates and outages of their systems to ensure ongoing connectivity. In addition, due to already limited physical space on customer confirmations, such URLs would need to be appropriately sized to ensure that firms can fit them into the limited space available on confirmations. Should the MSRB and FINRA adopt Schwab's proposal to disclose mark-ups from the PMP, we believe that time of execution would not be a necessary data point for confirmations.

In general, Schwab believes that evaluating the costs and burdens of any new rule requirements and weighing those costs against any benefits derived from them is critical to ensure efficient and effective rulemaking. Before any new requirements are created, FINRA and the MSRB should conduct a thorough cost-benefit analysis of requirements set forth in these Proposals.

Thank you for your consideration of the points we have raised in this letter and we hope that you find that our comments are useful in helping to formulate your final rules. Please feel free to contact Michael Moran at (415) 667-0902 if you have any questions.

Sincerely,

Jason Clague

Jason Clague
Senior Vice President
Trading & Middle Office Services
Charles Schwab & Co., Inc.

sifma
Invested in America

December 11, 2015

BY ELECTRONIC MAIL

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Re: FINRA Regulatory Notice 15-36
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2015-16,
Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith and Mr. Smith:

The Securities Industry and Financial Markets Association[1] ("SIFMA") appreciates the opportunity to comment on the Financial Industry Regulatory Authority's ("FINRA's") Regulatory Notice 15-36 and the Municipal Securities Rulemaking Board's ("MSRB's") Regulatory Notice 2015-16 (together the "Revised Proposals" or the "Proposals"). SIFMA submits this letter as a supplement to its submission of January 20, 2015 regarding FINRA's Regulatory Notice 14-52 and the MSRB's Regulatory Notice 2014-20 (the "Initial Proposals"). We incorporate by reference our prior comment in this proceeding.

SIFMA strongly supports efforts to enhance bond market price transparency in a way that provides retail investors with useful, clear, and consistent insight into their

[1] SIFMA is the voice of the U.S. securities industry, representing the broker-dealers, banks and asset managers whose 889,000 employees provide access to the capital markets, raising over $2.4 trillion for businesses and municipalities in the U.S., serving clients with over $16 trillion in assets and managing more than $62 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

transactions, and appreciates the deep engagement with our members by both FINRA and the MSRB over the past several months concerning this issue.

As a preliminary matter, any new confirmation disclosure requirement must be uniform in design and operation. As we emphasized throughout our prior comments, there is no policy justification for adopting divergent approaches or terminology in this context. Unfortunately, the Proposals provide two fundamentally different formulations for what any confirmation disclosure should entail. FINRA and the MSRB have not identified any benefit to requiring firms to implement, at enormous cost, two different rules. We again urge FINRA and the MSRB to adopt a uniform rule with identical requirements and language.

Consistent with our earlier comments, SIFMA continues to maintain that the Proposals impose unjustified costs and burdens and that investors would be better served by alternatives that focus exclusively on increasing usage of the abundance of market data and investor tools already available on TRACE and EMMA. Nevertheless, while we believe our arguments in this regard are correct, we focus this letter on FINRA's and the MSRB's determination to implement rules requiring confirmation disclosure related to bond pricing.

Although we continue to believe that any retail confirmation disclosure with specific pricing information should apply solely to trades in which no market risk attaches to the dealer effecting the transaction (*i.e.*, "riskless principal transactions"), we understand that FINRA and the MSRB have favored a more expansive approach. Accordingly, we believe strongly that, should some form of the Proposals proceed, FINRA and the MSRB should embrace a two-hour time frame for disclosure of firm and retail customer trades. A two-hour window, as proposed by the MSRB, would capture nearly all of the relevant universe of firm and customer trades and is a more reasonable proxy for contemporaneous trade disclosure than the same-day window proposed by FINRA. As the time period between firm and customer trades increases, any disclosure requirement becomes considerably more complex for dealers to implement and, given the difficulty of matching trades in complex scenarios separated by time, price fluctuations and market volatility, more difficult for customers to understand.

Should some version of the Proposals proceed, SIFMA urges FINRA and the MSRB to adopt a uniform rule that provides firms with the flexibility to adopt a matching framework, a prevailing market price framework, or an alternative readily determinable price reference framework, subject to further regulatory guidance. For example, one potential alternative approach is a daily volume weighted average (market) price ("VWAP"). While some firms already have adopted a prevailing market price framework, such approach may be difficult for firms with different business models to implement. Given the diversity of business models and technology configurations among firms, FINRA and the MSRB should allow for a level of flexibility among these frameworks and not impose a rigid model on the entire securities industry that imposes disparate burdens and unnecessary costs. With or without that flexibility, additional guidance may be necessary for implementation across the marketplace. In addition, while FINRA and the MSRB have addressed some of our concerns with the Initial Proposals, serious structural and operational issues with the Revised Proposals must be addressed.

Accordingly, if some form of the Proposals does proceed, FINRA and the MSRB must provide clear and uniform guidance that leads to relevant customer disclosure, is administratively and operationally feasible, and maintains the liquidity of the debt marketplace. We would welcome the opportunity to engage further with FINRA and the MSRB to help define specific guidance in that regard.

DISCUSSION

I. ANY NEW FINRA AND MSRB CONFIRMATION DISCLOSURE REQUIREMENTS MUST BE UNIFORM IN DESIGN AND OPERATION.

As a preliminary matter, any new FINRA and MSRB confirmation disclosure requirements must be uniform in design and operation. As SIFMA stressed in its initial comment letter, there is no policy justification for having divergent approaches or terminology in this context. Recognizing that there is no reason for two completely different disclosure regimes in this area, FINRA and the MSRB again have promised that "both entities favor a coordinated approach" to potential rulemaking.[2] We urge FINRA and the MSRB to embrace uniformity and not simple coordination by adopting a harmonized rule that provides firms with the flexibility to adopt various methodologies for compliance as described in Part IV.

Unfortunately, this "coordinated approach" has thus far failed to produce a uniform proposed rule and has instead provided two fundamentally different formulations for what any confirmation disclosure should entail. As described in Part III, FINRA's Proposal requires disclosure of firm and retail customer trades within an expansive same-day window, while the MSRB's Proposal targets a two-hour window. As described in Part IV, FINRA's Proposal suggests a reference price matching framework, while the MSRB's Proposal suggests a prevailing market price standard. The Proposals fail to articulate any benefit to requiring each firm to implement, at

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[2] FINRA Regulatory Notice 15-36 at 6 ("While FINRA and the MSRB's revised proposals currently differ, both entities favor a coordinated approach. Accordingly, FINRA is inviting comments on the MSRB's proposal in comparison to FINRA's revised proposal, and whether the MSRB's proposal, or elements of the proposal, may be an appropriate alternative to FINRA's revised proposal."); *see also* MSRB Regulatory Notice 2015-16 at 1 ("The MSRB and the Financial Industry Regulatory Authority (FINRA) have been engaged in ongoing dialogue regarding potential rulemaking in this area.").

enormous cost, two conceptually divergent rules regarding what any new confirmation disclosure obligation should entail. FINRA and the MSRB must adopt a uniform rule.

Assuming FINRA and the MSRB agree on a uniform approach, no purpose would be served by differently worded rules that are intended to operate identically. Unfortunately, in addition to the obvious differences associated with two divergent conceptual approaches, FINRA and the MSRB continue to use different terms and organization to describe similar concepts, creating unnecessary ambiguity and compliance risk. For example, FINRA's Proposal requires disclosure of "the differential between the price to the customer and the member's Reference Price," without specifying whether such differential should be expressed as a dollar amount and/or in percentage terms, while the MSRB's Proposal requires disclosure expressed both "as a total dollar amount and as a percentage of the principal amount of the transaction."[3] FINRA's Proposal requires a reference and hyperlink to the TRACE "publicly available trading data" without specifying whether the reference and hyperlink should point to a particular TRACE page, while the MSRB's Proposal requires both a hyperlink to the Security Details page on EMMA as well as a description of the type of information available on that page.[4] Similarly, FINRA and

[3] The FINRA Proposal states, "(3) with respect to a sale to (purchase from) a non-institutional customer in a corporate or agency debt security, if the member also executes a buy (sell) transaction(s) as principal with one or multiple parties in the same security within the same trading day that equals or exceeds the size of the customer transaction: (A) the price to the customer; (B) the member's Reference Price; (C) *the differential between the price to the customer and the member's reference price*; and (D) a reference, and hyperlink if the confirmation is electronic, to the Trade Reporting and Compliance Engine (TRACE) publicly available trading data." FINRA Regulatory Notice 15-36 at 20 (emphasis added). The MSRB Proposal states, "the confirmation shall include the dealer's mark-up or mark-down from the prevailing market price for the security, *expressed as a total dollar amount and as a percentage of the principal amount of the transaction* . . . ." MSRB Regulatory Notice 2015-16 at 29 (emphasis added).

[4] The FINRA Proposal states, "(3) with respect to a sale to (purchase from) a non-institutional customer in a corporate or agency debt security, if the member also executes a buy (sell) transaction(s) as principal with one or multiple parties in the same security within the same trading day that equals or exceeds the size of the customer transaction: (A) the price to the customer; (B) the member's Reference Price; (C) the differential between the price to the customer and the member's reference price; and (D) *a reference, and hyperlink if the confirmation is electronic, to the Trade Reporting and Compliance Engine (TRACE) publicly available trading data*." FINRA Regulatory Notice 15-36 at 20 (emphasis added). The MSRB Proposal states, "(4) The confirmation for a transaction executed for an account other than an institutional account (as defined in MSRB Rule G-8(a)(xi)) *shall include a hyperlink and uniform resource locator address to the Security Details page for the customer's security on EMMA, along with a brief description of the type of information available on that page*." MSRB Regulatory Notice 2015-16 at 29 (emphasis added).

the MSRB employ different terminology to describe transactions executed by "functionally separate" trading desks[5] and positions acquired by an affiliate.[6]

Regarding potential rulemaking in this area, these types of differences create unnecessary ambiguity and can result in divergent regulatory approaches and interpretive guidance over time. While differences in the corporate and municipal debt securities markets may sometimes require differing approaches to regulation, there is no justification for the differences in terminology or formulation in this context and the Proposals should be made identical.

Moreover, as FINRA and the MSRB are aware, the Department of Labor ("DOL") is currently engaged in rulemaking that would require disclosure for certain fixed income transactions executed as principal in connection with the provision of investment advice to retirement accounts.[7] FINRA and MSRB rules will apply across retirement and non-retirement accounts. We have raised our concerns with the DOL with regard to the unworkability of their current proposal. Should the DOL proposal proceed in some form, we are hopeful that the DOL will recognize and leverage the work by FINRA and the MSRB rather than proceed on a divergent path, however, the

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[5] The FINRA Proposal states, "A member is not required to consider a principal trade where: (i) the member's principal buy (sell) transaction was executed by a trading desk that was *functionally separate from the trading desk that executed the non-institutional customer order*, including that the transactions and positions of the separate desk are *not regularly used to source the retail transactions at the other desk* . . . ." FINRA Regulatory Notice 15-36 at 21 (emphasis added). The MSRB Proposal states, "[A] dealer shall not be required to disclose the mark-up if: (a) the customer transaction was executed by a principal trading desk that is *functionally separate from the principal trading desk within the same dealer that executed the dealer purchase (in the case of a sale to a customer) or dealer sale (in the case of a purchase from a customer)* of the security; and (b) the functionally separate principal trading desk through which the dealer purchase or dealer sale was executed *had no knowledge* of the customer transaction." MSRB Regulatory Notice 2015-16 at 30 (emphasis added).

[6] The FINRA Proposal states, "A member is not required to consider a principal trade where: . . . (ii) The member's principal trade was executed with an affiliate of the member, where the affiliate's position that satisfied this trade was not acquired on the same trading day." FINRA Regulatory Notice 15-36 at 21. The MSRB Proposal states, "The term 'inventory-affiliate model' shall mean a business model in which the dealer, on an exclusive basis, acquires municipal securities from or sells municipal securities to an affiliated dealer that holds inventory in municipal securities and transactions with other market participants." MSRB Regulatory Notice 2015-16 at 30.

[7] Definition of the Term "Fiduciary"; Conflicts of Interest Rule – Retirement Investment Advice, 80 Fed. Reg. 21928 (April 20, 2015); Proposed Class Exemption for Principal Transactions in Certain Debt Securities between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs, 80 Fed. Reg. 21989 (April 20, 2015). *See also* SIFMA, Comment Letter to the U.S. Department of Labor on Its Fiduciary Rule Proposal – Principal Transactions (July 20, 2015), *available at* http://www.sifma.org/issues/item.aspx?id=8589955454.

increased risk of conflict and investor confusion by the DOL's efforts highlights the importance of FINRA and the MSRB adopting a uniform rule.

II. TO MINIMIZE THE RISK OF INVESTOR CONFUSION, ANY NEW RETAIL CONFIRMATION DISCLOSURE OBLIGATION WITH SPECIFIC PRICING INFORMATION SHOULD APPLY SOLELY TO RISKLESS PRINCIPAL TRANSACTIONS.

For the reasons articulated in our initial letter, SIFMA continues to believe that any retail confirmation disclosure obligation that involves narrowly comparing the customer's trade price to another specific trade price by that same firm should apply solely to riskless principal transactions. Although the technology and compliance costs of implementation of even this riskless principal approach would be significant, disclosure of mark-ups on riskless principal trades would reduce complexity for dealers in matching trades across time in complex scenarios, relative to an approach that required reference prices to be included on non-riskless principal trades. In addition, a riskless principal approach would minimize the possibility of investor confusion from the aggregation of compensation paid by the customer with price changes due to normal market volatility. Further, limiting reference price disclosures to riskless principal trades would be most consistent with the stated initial objective of the Proposals to provide investors with reliable insight into the transaction costs associated with their fixed income trades.[8]

As we have emphasized previously, disclosure associated with riskless principal trades is most similar to the type of mark-up disclosure that the SEC has proposed on four previous occasions and would be most consistent with the recommendation in the SEC's 2012 Report on the Municipal Securities Market ("Municipal Report").[9] Notably, the SEC has found that the mark-up or mark-down in riskless principal transactions is "readily determinable" – an acknowledgement that alternative disclosure formulations would be more complicated and potentially confusing and misleading to retail investors if implemented.[10]

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[8] MSRB Regulatory Notice 2015-16 at 19. *See also* FINRA Regulatory Notice 15-36 at 12 ("Does the revised proposal alter investors' ability to obtain greater transparency into the compensation of their broker-dealers or the costs associated with the execution of their fixed income trades?").

[9] U.S. Securities and Exchange Commission, Report on the Municipal Securities Market, 148 (July 31, 2012) ("The MSRB should consider requiring municipal bond dealers to disclose to customers, on confirmations for riskless principal transactions, the amount of any markup or markdown.") [hereinafter *Municipal Report*].

[10] *Municipal Report* 148 ("Because riskless principal transactions are very similar, as a practical matter, to agency transactions, and the amount of the markup or markdown is readily

Notwithstanding our well-documented concerns associated with even a riskless principal disclosure obligation, SIFMA recognizes that FINRA and the MSRB appear to favor the adoption of a more expansive regulatory regime that would extend beyond the SEC's recommendations in this area. For this reason, we offer our additional feedback on the Revised Proposals below.

III. IF SOME FORM OF THE PROPOSALS DOES PROCEED, FINRA AND THE MSRB SHOULD EMBRACE A TWO-HOUR DETERMINATION WINDOW.

A two-hour time frame, as proposed by the MSRB, would capture nearly all of the relevant universe of "paired" firm and customer trades and is a more reasonable proxy for contemporaneous trade disclosure than a same-day window.[11] Under the MSRB's Revised Proposal, dealers would be required to disclose the mark-up on retail customer transactions "only where the dealer's same-side of the market transaction occurs within the two hours preceding or following the customer transaction."[12] In contrast to the MSRB's more targeted approach, FINRA's Revised Proposal would require "disclosure of pricing information for trades in the same security where the firm principal and the customer trades occur on the same trading day."[13] Whether FINRA and the MSRB adopt a two-hour or same-day framework, there will be operational challenges associated with delaying the confirmation process for hours after the time of the customer trade.

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determinable, confirmation disclosure of a municipal bond dealer's compensation in these circumstances should allow customers to more effectively assess the fairness of the prices provided by dealers."). *See also, e.g.*, Mary Jo White, Chair, SEC, Remarks at the Economic Club of New York, Intermediation in the Modern Securities Markets: Putting Technology and Competition to Work for Investors (June 20, 2014) *available at* http://www.sec.gov/News/Speech/Detail/Speech/1370542122012 ("Markups – the dealer's compensation – for these transactions can be readily identified because they are based on the difference in prices on the two contemporaneous transactions, which already must be reported promptly to FINRA and the MSRB for public posting after the trade.").

[11] Rather than relying on an interval of time between transactions as a proxy for riskless principal, FINRA and the MSRB could look to whether transactions were in fact intended to be offsetting. *See* Letter from Roger D. Blanc, Chief Counsel, Division of Market Regulation to Buys-MacGregor, MacNaughton-Greenwalt & Co. (Jan. 2, 1980), 1980 SEC No-Act. LEXIS 2851.

[12] MSRB Regulatory Notice 2015-16 at 8.

[13] FINRA Regulatory Notice 15-36 at 11.

A. A two-hour window would provide pricing information that is more representative of the market at the time of the customer transaction and already incorporates a mitigating time cushion to address gaming concerns.

To be clear, SIFMA continues to believe that any confirmation disclosure obligation with specific pricing information should apply solely to riskless principal transactions with retail investors. Moreover, as described below in Part V.B, there are several structural and operational issues with the MSRB's Revised Proposal as currently drafted. Nonetheless, a two-hour window generally would provide pricing information that is more representative of the market at the time of the customer transaction, and therefore is a better point of reference to consider the fairness and reasonableness of the price that the customer received. According to the MSRB, more than 96% of all trades that were followed by another trade in the same municipal security on the same day had the second trade occur within two hours.[14] Similarly, FINRA has found that 98% of retail-sized customer trades in corporate debt securities with same-sized corresponding principal trades occurred within 2 hours.[15] Accordingly, we believe that using a two-hour window provides the investor with all necessary information and that a broader approach could not be reasonably justified on a cost-benefit analysis – especially given the risk of increased investor confusion.[16]

In addition, a two-hour window already incorporates a mitigating time cushion to address any theoretical concerns that a firm might delay trading activity to avoid disclosure requirements. According to studies of secondary market transactions, all or nearly all of the relevant universe of "paired trades" occur within a very short window calculated to be between 5 and 15 minutes.[17] Indeed, FINRA's Proposal acknowledges that "TRACE data indicate[s] that a majority of firm and customer trades occur within 30 minutes of each other."[18] As described below, we believe that any theoretical gaming concerns are overstated and would be best addressed through required firm supervisory policies and procedures, as well as examination and enforcement. To the extent, however, that FINRA continues to harbor such concerns, a two-hour window

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[14] MSRB, Report on Secondary Market Trading in the Municipal Securities Market (July 2014) at 24 (Figure III.F).

[15] FINRA Regulatory Notice 15-36 at 7. *See also* FINRA Regulatory Notice 15-36 at 18 n.21 ("These statistics were similar for trades in agency debt securities. For example, customer trades with same-sized corresponding principal trades occurred . . . within 2 hours for more than 98 percent of the trades.").

[16] *See infra* Part V.E.

[17] MSRB, Report on Secondary Market Trading in the Municipal Securities Market (July 2014) at 24 (Figure III.F).

[18] FINRA Regulatory Notice 15-36 at 11.

would provide a considerable safeguard given that the majority of relevant activity is centered within only a 30 minute window.

B. FINRA's same-day Proposal gives undue weight to theoretical gaming concerns while sacrificing a great deal of clarity and effectiveness regarding the disclosure itself.

FINRA's same-day window would capture more trades for which the dealer has been subject to market risk. As we articulated in our earlier comments, disclosure in such circumstances may be confusing to the customer whose trade is being confirmed, as the disclosure would reflect trading profit or loss resulting from market volatility and price fluctuations. Moreover, for certain methodologies, a same-day window would create additional operational burdens associated with holding confirmations until the end of the trading day. Unnecessarily confusing and potentially misleading disclosures may in turn trigger unfounded customer complaints, which could require disclosures on a registered representative's Form U4. FINRA's Proposal does not address whether such costs and complexities have been evaluated, other than an acknowledgement that the liquidity in the fixed income market is a relevant consideration.[19] Conversely, having considered these issues, the MSRB emphasized that "the additional costs and complexities associated with the broadening of this time trigger to a full-day time period might not be justified."[20] SIFMA agrees that the additional costs and complexities to dealers, particularly those dealers that maintain inventory, as well as the risk of confusion to customers, outweigh any potential benefits of extending the window.[21]

In recommending a same-day window for determining a reference price to print on a customer's trade confirmation, FINRA appears to be making a conscious decision to address theoretical gaming concerns while at the same time sacrificing a great deal of clarity, consistency, and effectiveness regarding the disclosure itself. In particular, FINRA acknowledges that "[w]hile the TRACE data indicated that a majority of firm and customer trades occur within 30 minutes of each other," a same-day standard "will help reduce the concern that a firm might delay trading activity to avoid triggering the disclosure requirements."[22] FINRA, however, does not explain why such a same-day window is appropriate given that the capture of unrelated trades under any same-day pairing framework will reduce the relevance of the disclosure itself, increase complexity for dealers that carry inventory, and create customer confusion.

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[19] FINRA Regulatory Notice 15-36 at 15.

[20] MSRB Regulatory Notice 2015-16 at 8.

[21] *See supra* note 10.

[22] FINRA Regulatory Notice 15-36 at 11.

As SIFMA has emphasized throughout this process, our members are concerned about their ability to explain the rationale and composition of pricing disclosure to the retail investors that FINRA and the MSRB are attempting to serve. A same-day window for disclosure greatly increases these concerns. As noted above, the vast majority of trades occur well within the two-hour window proposed by the MSRB. SIFMA believes that firms are highly unlikely to materially change their trading practices merely to avoid price disclosure, as doing so would greatly increase their exposure to regulatory and market risk. Moreover, it is not sensible to impose significant costs on an entire industry because of potential abuse by a few. Such abuse could be readily addressed through examination and enforcement activity. Rather than impose a same-day window to address theoretical gaming concerns, any final rule could require firms that carry bond inventories to adopt policies and procedures, as well as corresponding surveillance systems, to monitor that traders are not delaying trading activity beyond a two-hour window with the intent to avoid triggering the disclosure requirements. This is a more direct way to address any theoretical gaming concerns, without creating unnecessary customer confusion about quality of execution that would result from an overbroad same-day framework.

The relevance of the price at which a dealer transacted in a particular bond compared to the price charged to the customer decreases over time. A two-hour window would better serve the regulatory objective and provide more clear and effective disclosure for retail customers than a same-day window. Nevertheless, we remain concerned that FINRA and the MSRB will continue to give undue weight to theoretical gaming concerns even though the marginal benefit of capturing the limited number of trades occurring outside the two-hour window is outweighed by the complexity, cost, and risk of confusion resulting from a same-day period.

IV. IF SOME FORM OF THE PROPOSALS DOES PROCEED, FINRA AND THE MSRB SHOULD ADOPT A UNIFORM RULE THAT PROVIDES FIRMS WITH THE FLEXIBILITY TO ADOPT A MATCHING FRAMEWORK, A PREVAILING MARKET PRICE FRAMEWORK, OR AN ALTERNATIVE READILY DETERMINABLE PRICE REFERENCE FRAMEWORK.

If some form of the Proposals does proceed, FINRA and the MSRB should adopt a uniform rule that provides firms with the flexibility to adopt a matching framework, a prevailing market price framework, or an alternative readily determinable price reference framework, subject to further regulatory guidance. For example, one alternative approach is for FINRA and the MSRB to provide readily determinable price references for each CUSIP, such as the VWAP over the course of each day, for dealers to include on each customer confirmation.

We recognize that one of the primary regulatory objectives associated with requiring enhanced price disclosure on retail customer confirmations is to allow investors to evaluate more readily their transaction costs. FINRA has expressed concerns that "investors in fixed income securities currently are limited in their ability to understand and compare transaction costs associated with their purchases and sales."[23] Similarly, the MSRB suggests that "if an investor believes that a disclosed mark-up is higher than he or she might have received from another dealer, the investor may be incentivized to seek out other dealers offering lower transaction costs for future trades."[24]

We believe that a uniform rule which provides firms with the flexibility to adopt either a matching framework, a prevailing market price framework, or an alternative readily determinable price reference framework, subject to consistent application across retail customers and clearly documented policies and procedures, would provide meaningful information and investor protection in this regard. In the absence of one uniform rule, FINRA and the MSRB should each permit that same flexibility. As described below, some firms already have adopted a prevailing market price disclosure framework. However, based on a firm's business model and technology configuration, other approaches may be more reasonable to implement while still providing equally meaningful disclosure. For firms that maintain substantial balance sheets and regularly deal in fixed income securities, a prevailing market price framework would likely be costly to build while alternative methodologies may be more readily automated and would reduce the cost and risk in implementation and compliance. Given the diversity of business models among firms, FINRA and the MSRB should allow for a level of flexibility and not impose a rigid model on the entire industry that imposes disparate burdens and unnecessary costs.

A. FINRA and the MSRB should provide firms with the flexibility to adopt the matching framework or the prevailing market price standard presented in the Proposals, subject to further guidance.

The Proposals already each put forth different methodologies and as a general matter, SIFMA believes that firms should be afforded a level of flexibility to adopt the matching framework presented in the FINRA Proposal, the prevailing market price standard presented in the MSRB Proposal, or the alternative disclosure framework described in Part IV.B, as long as the chosen standard is applied consistently across retail customers and is clearly documented in policies and procedures. Nonetheless, the Proposals as currently drafted impose unnecessary regulatory risk on dealers and additional guidance regarding each approach is needed.

With respect to the matching framework, firms should be afforded the flexibility to determine the appropriate methodology for the determination of the reference price as suggested in FINRA's Proposal. In its Initial Proposal, FINRA detailed a number of specific methodologies that could be acceptable in this regard,

[23] FINRA Regulatory Notice 15-36 at 6.

[24] MSRB Regulatory Notice 2015-16 at 15.

including average weighted price, last in/first out, and closest in time. The price reference rule should outline a clear and uniform framework for firms and explicitly state that these given methodologies are permissible and will be deemed to be compliant so long as firms apply their selected methodology consistently across their retail customer base and that such methodology is clearly documented in a firm's policies and procedures. While firms may choose to seek regulatory guidance on the use of variant matching methodologies, it should be clear that certain core matching methodologies are permitted so that no unnecessary regulatory compliance risk is introduced for implementation thereof.

In proposing a prevailing market price standard, the MSRB has emphasized that firms already have processes and systems in place designed to ensure that mark-ups on principal transactions are fair and reasonable, and therefore the "prevailing market price and resultant mark-up on the customer's security should be more readily determinable."[25] We agree that, in some cases, the prevailing market price methodology would be the more readily implementable and most cost effective approach for some dealers, while still providing meaningful disclosure to retail investors consistent with the regulatory objectives. Additionally, firms that choose a prevailing market price framework would be able to calculate mark-up disclosure in real-time with the trade and would avoid any challenges associated with holding a confirmation to the end of the trading day. The flexibility to use a prevailing market price framework recognizes that some firms have developed such disclosure methodologies. For those firms that do adopt a prevailing market price methodology, we believe a rebuttable presumption for opposing trades of the same size that occur in a very narrow time window may be reasonable such that the disclosure is presumed to be the difference between the two trades in these cases. Policies and procedures would need to properly address these contemporaneous trades.

While it is true that a prevailing market price standard is used today to ensure fair and reasonable pricing to customers, a requirement to delineate an exact prevailing market price on a customer confirmation requires some additional guidance. In that context, we are primarily concerned about trades that are not contemporaneous and ensuring that there is relative consistency in approach across firms. Given the variety of indicia that may inform a determination of prevailing market price, two firms may reasonably come to different conclusions and different disclosures with similar facts, but additional guidance should reduce such variability. We are happy to engage further with FINRA and the MSRB to help define some guidance concerning how to reasonably calculate a prevailing market price.

Given the significance of confirmation disclosure, firms need comfort that they are able to satisfy fully their obligations under Rule 10b-10 under the Exchange Act for any permitted methodology. Rule 10b-10 generally requires that broker-dealers

[25] MSRB Regulatory Notice 2015-16 at 9.

provide customers with a written confirmation of a transaction disclosing certain information. Absent further guidance regarding expressly permitted matching methodologies and the determination of a prevailing market price, SIFMA is concerned that firms may be taking on material risk regarding the disclosures they include in their customer confirmations.

B. In addition, FINRA and the MSRB should provide firms with the flexibility to adopt an alternative readily determinable reference price framework.

As an alternative to the matching or prevailing market price frameworks articulated in the current Proposals, FINRA and the MSRB should also provide firms with the flexibility to adopt an alternative readily determinable reference price framework. An alternative readily determinable reference price, such as a daily VWAP, could provide for consistency and reduce complexity while also giving retail investors equally meaningful disclosure consistent with the regulatory objectives. An alternative readily determinable reference price provides useful context about the market as well as comparative pricing in the security being traded. To that end, we believe that several different price reference approaches (*e.g.*, VWAP, high/low trades) could accomplish the regulatory objective and in some circumstances may be more reasonable to implement and a more useful method of disclosure for both the dealer and its retail customers.

For example, FINRA and the MSRB could calculate an industry-wide daily VWAP for every CUSIP and publish the data relatively instantaneously at the end of the trading day. A dealer could extract the relevant CUSIP-specific VWAP for printing on individual customer confirmations. The VWAP for a CUSIP over the course of that day would serve as a meaningful price reference, providing some greater context to where the client purchased the bond in relation to market activity that day. In addition, a VWAP may in some ways be easier for dealers to explain and easier for customers to understand relative to the formulations contemplated by the existing Proposals.

The VWAP approach also has the benefit of substantially lowering the cost of implementation, as firms would not need to develop an internal calculation methodology, and instead could focus on a process to pull information on confirmations from an external source. Moreover, this approach offers firms the ability to eliminate any regulatory and compliance costs associated with reaching a reference price or prevailing market price determination, as firms would be transmitting to customers an objective and observable reference price provided by FINRA and the MSRB. In the same way, a daily VWAP would eliminate any theoretical gaming concerns for those firms choosing such methodology.

As an alternative to providing an industry-wide daily VWAP, FINRA and the MSRB could publish an industry-wide daily high/low for every CUSIP, and each dealer in turn could extract the relevant CUSIP-specific high/low for individual customer confirmations. The readily determinable and objective nature of such statistics can offer benefits in both the implementation and clarity to customers. Such methodologies should be embraced as meaningful and valuable alternatives.

In addition, firms could be permitted to calculate an internal VWAP or some other readily determinable reference price on an individual firm basis subject to regulatory approval. Notably, FINRA's Proposal recognizes that this type of daily VWAP is an appropriate reference price in certain contexts.[26] We believe that such internal VWAP should be acceptable as a general matter.

V. ALTHOUGH FINRA AND THE MSRB HAVE ADDRESSED SOME OF THE ISSUES WITH THE INITIAL PROPOSALS, SPECIFIC STRUCTURAL AND OPERATIONAL PROBLEMS WITH THE REVISED PROPOSALS DEMONSTRATE THE NEED FOR AN ALTERNATIVE APPROACH OR SIGNIFICANT REVISION.

It is clear that FINRA and the MSRB were responsive to some of our major concerns with the Initial Proposals, however, serious structural and operational issues remain with the Revised Proposals. Accordingly, the Proposals are unworkable as currently formulated and an alternative approach or significant revision is necessary.

A. The Revised Proposals address some, but not all, of the major structural and operational issues with the Initial Proposals.

While we continue to have concerns with certain details of the Revised Proposals, SIFMA acknowledges and appreciates that the Revised Proposals address some of the major structural and operational issues that we identified with the Initial Proposals.

1. "Functionally separate" trading desks

Notwithstanding our concern that there is no justification for the usage of different terminology to describe the same concepts, SIFMA generally agrees with the approach to "functionally separate trading desks" in the Revised Proposals.[27] As we

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[26] Under FINRA's Proposal, "where there are one or more intervening principal trades between the same or greater size trades within the same trading day, the member may use an alternative methodology to determine the Reference Price." FINRA Regulatory Notice 15-36 at 22. Such methodology must be "an average weighted price of the member's same-day principal trades that either equal or exceed the size of the customer trade, or is derived from the price(s) of the member's same-day principal trades and communicates comparable pricing information to the customer." *Id.*

[27] *See supra* note 5.

emphasized in our earlier comments, the Initial Proposals failed to address whether member firms would be obliged to treat trades on a separate institutional desk in the same legal entity as reference trades for retail customer transactions, or whether they must evaluate trading activity on the proprietary desk as potential reference transactions. Given the substantive and operational complexity associated with incorporating reference data from separate institutional or proprietary desks onto retail confirmations, FINRA and the MSRB are correct to exempt such transactions in the Revised Proposals.

2. Exclusion for fixed price new issues

We agree that transactions that are part of fixed price new offerings should be excluded from the Revised Proposals.[28] The Initial Proposals were unnecessarily vague as to their intended applicability to new issues. Consistent with our earlier comments, the Revised Proposals properly note that such offerings already provide significant disclosure regarding the underwriter's compensation.[29]

3. Exclusion for transactions involving an "institutional account"

We agree that any confirmation disclosure obligation should be tailored to apply only to retail customers by using defined terms to exclude institutional and other sophisticated investors. Under the Revised Proposals, the "qualifying size" of 100 bonds or less or bonds with a face value of $100,000 or less in the Initial Proposal would be replaced with an exclusion for transactions that involve an "institutional account," as defined in FINRA Rule 4512(c) and MSRB Rule G-8(a)(xi).[30]

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[28] The FINRA Proposal states, "A member is not required to consider a principal trade where: . . . (iii) The member acquired the security in a fixed-price offering and sold the security to non-institutional customers at the fixed price offering price on the day the securities were acquired." FINRA Regulatory Notice 15-36 at 21. The MSRB Proposal states that the mark-up disclosure requirement "shall not apply to a customer transaction that is a 'list offering price transaction' as defined in paragraph (d)(vii) of Rule G-14 RTRS Procedures." MSRB Regulatory Notice 2015-16 at 30.

[29] *See* MSRB Regulatory Notice 2015-16 at 10 ("Such transactions are executed at the same publicly announced price to investors and offering documents for new issues already provide disclosure regarding underwriting fees and selling concessions.").

[30] Under FINRA Rule 4512(c), "the term 'institutional account' shall mean the account of: (1) a bank, savings and loan association, insurance company or registered investment company; (2) an investment adviser registered either with the SEC under Section 203 of the Investment Advisers Act or with a state securities commission (or any agency or office performing like functions); or (3) any other person (whether a natural person, corporation, partnership, trust or otherwise) with total assets of at least $50 million." Under MSRB Rule G-8(a)(xi), "the term 'institutional account' shall mean the account of (i) a bank, savings and loan association, insurance company, or registered investment company; (ii) an investment adviser registered

B. Certain aspects of the Revised Proposals require clarification or significant revision.

1. Clarify that a two-hour window would not extend to the previous or following trading day

Should the final rule adopt a two-hour window as we suggest, clarification that the window would not extend to the previous or following day is needed. As currently drafted in the MSRB's Proposal, dealers would be required to disclose the mark-up or mark-down on retail customer transactions "only where the dealer's same-side of the market transaction occurs within the two hours preceding or following the customer transaction."[31] Given that the two-hour window is intended as a proxy for contemporaneous transactions, there is no basis for such window to extend beyond the same trading day. The final rule(s) should make this explicit clarification.

Whether FINRA and the MSRB adopt a two-hour or same-day window, the beginning and end of the trading day must be clearly defined in order for firms to process confirmations. In this regard, FINRA and the MSRB should consider the existing operating hours for TRACE and the RTRS facility. Standard TRACE system hours begin at 8:00 a.m. and close at 6:30 p.m. Eastern Time, while the RTRS "Business Day" begins at 7:30 a.m. and ends at 6:30 p.m. Eastern Time. We are happy to engage further with FINRA and the MSRB regarding how to balance effectively the need for a uniform rule and the operational considerations associated with these divergent timeframes.

2. Eliminate the requirement that time of execution be printed on the customer confirmations

The MSRB's Proposal would require inclusion on all customer confirmations the "trade date and time of execution, accurate to the nearest minute."[32] FINRA's Proposal contains no such requirement. As the MSRB notes in its Proposal, Rule G-15 already provides that a dealer must either disclose the time of execution or provide the customer with a statement that the time of execution will be furnished upon written request.[33] The MSRB has not provided any basis for changing this approach. Given

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either with the Commission under Section 203 of the Investment Advisers Act of 1940 or with a state securities commission (or any agency or office performing like functions); or (iii) any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least $50 million."

[31] MSRB Regulatory Notice 2015-16 at 28.

[32] MSRB Regulatory Notice 2015-16 at 22.

[33] *See* Rule G-15(a)(i)(A)(2) ("Trade date and time of execution. The trade date shall be shown. In addition, either (a) the time of execution, or (b) a statement that the time of execution will be furnished upon written request of the customer shall be shown.").

that this proposed requirement would provide no clear benefit, would be a material deviation from long-standing practice, and would impose significant implementation costs, any such requirement should be removed from any final rule(s).

3. Permit firms to adopt reasonable policies and procedures to assess what constitutes "an unusual and material change in the price of a bond"

SIFMA supports the exception in FINRA's Proposal that "would permit firms to either not disclose the reference price, or disclose with the reference price clarifying information, where the firm can demonstrate that there was an unusual and material change in the price of the bond between the time of the firm principal and the customer transactions."[34] However, other than a reference to "a material event such as a credit downgrade or breaking news," FINRA does not provide any guidance as to what would constitute "an unusual and material change" in price, and in fact excludes market volatility and price movements from consideration.[35] This exception is so narrowly drawn that, in the absence of further guidance, a dealer seeking to rely on it would in most instances be taking a significant enforcement risk. Accordingly, FINRA and the MSRB should permit firms to adopt reasonable policies and procedures to assess what constitutes "an unusual and material change in the price of a bond" in a way that is consistent across the marketplace. In particular, firms should be permitted to consider the impact of market- and sector-related developments on the price of a bond, rather than be limited strictly to CUSIP-specific developments.

4. Narrow the disclosure requirement to apply only to principal trades that are the same size or larger than the customer trade

Under the MSRB's Proposal, dealers would be required to disclose their mark-up or mark-down where they purchase a security "in one or more transactions in an aggregate trade size meeting or exceeding the size of [the customer's sale or purchase] within two hours of the customer transaction."[36] Under FINRA's Proposal, "[w]here a single principal trade is not the same size or greater than the customer trade or where there are one or more intervening principal trades between the same or greater size trades within the same trading day, the member may use an alternative methodology to determine the Reference Price."[37] Such aggregation does not occur often enough to justify the significant costs and operational complexities associated with such an approach. In this regard, FINRA and the MSRB should narrow the disclosure

[34] FINRA Regulatory Notice 15-36 at 4.

[35] *Id.*

[36] MSRB Regulatory Notice 2015-16 at 29.

[37] FINRA Regulatory Notice 15-36 at 22.

requirement to apply only to principal trades that are the same size or larger than the customer trade.

5. Provide clear and uniform guidance regarding the treatment of transactions by affiliated firms

As we emphasized in our earlier letter, transactions between affiliates should not be treated as one leg of a paired trade. SIFMA appreciates FINRA's and the MSRB's efforts to address this in their respective Proposals, but urge FINRA and the MSRB to adopt a uniform requirement that would require firms to "look through" a transaction with an affiliated broker-dealer and use that affiliate's transaction with a third party to determine the required disclosure. Under the MSRB's Proposal, a dealer operating under an inventory-affiliate model "would be required to 'look through' the transaction with the affiliated dealer and substitute the affiliate's trade with the third party from whom it purchased or to whom it sold the security to determine whether disclosure of the mark-up would be required."[38] FINRA's Proposal provides a similar but not identical requirement that would exclude trades "where the member's principal trade was executed with an affiliate of the member and the affiliate's position that satisfied this trade was not acquired on the same trading day."[39] FINRA and the MSRB should provide clear and uniform guidance regarding the treatment of inter-affiliate, dealer-to-dealer transactions under the Proposals.

6. Confirm that firms will not be required to cancel and correct confirmations due solely to a change in the reference transaction price

As we explained in our earlier letter, FINRA and the MSRB should confirm that any new confirmation requirement should not require confirmations to be cancelled and corrected due solely to a change in the reference transaction price. FINRA's Proposal confirms that, where a firm trade used to calculate the reference price is later cancelled, "FINRA would not require the firm to recalculate the reference price or re-issue a confirmation, but the firm would be permitted to do so at its discretion."[40] The MSRB's Revised Proposal suggests a "possible clarification" to its Initial Proposal that firms "would not be required to resend confirmations due solely to a change in the reference transaction to be selected, the reference transaction price, or the differential between the customer price and reference transaction price."[41] In addition, dealers would be permitted to include a disclaimer on confirmations "that the reference price and related differential were determined as of the time of confirmation

[38] MSRB Regulatory Notice 2015-16 at 10.

[39] FINRA Regulatory Notice 15-36 at 6.

[40] FINRA Regulatory Notice 15-36 at 16 n.7.

[41] MSRB Regulatory Notice 2015-16 at 24.

generation."[42] With respect to any matching framework, any final rule(s) should make this clarification explicit.

7. Permit dealers to disclose a standard mark-up schedule in lieu of the confirmation disclosure of the Proposals

As we explained in our earlier letter, certain dealers may use a standard mark-up schedule that details the compensation that the firm and its salesperson receive for retail bond transactions. As an alternative to the disclosure contemplated by the Proposals, these dealers should be given the option to disclose that schedule to customers via a link to the schedule on the confirmation or annual mailed disclosure. To be clear, SIFMA opposes the mandatory adoption of mark-up schedules generally, however, we believe this approach should be considered as an alternative option available to dealers that have established a standard mark-up schedule.

C. Any requirement to include a reference and/or hyperlink to TRACE and EMMA must be uniform, helpful to customers, and easy to implement.

If some form of the Proposals does proceed, any additional disclosure obligation related to TRACE and EMMA should be uniform, helpful to customers, and easy for dealers to implement. The MSRB's proposed configuration unfortunately has the potential to be overly complex and difficult to implement, as it would require a link customized to each security on all trades for all non-institutional accounts. Given that this specific disclosure is not the primary disclosure point, the cost of implementation should be kept to a minimum. To that end, and as an initial step, SIFMA encourages FINRA and the MSRB to adopt the approach in FINRA's Proposal, which would require a reference and hyperlink to the TRACE "publicly available trading data," without requiring such reference and hyperlink to point to a CUSIP-specific page. Accordingly, FINRA and the MSRB should specify the exact uniform resource locator ("URL") – *i.e.*, web address – that should be printed on customer confirmations. These URLs should be as short as possible so that they may be easily communicated to and entered without error by customers.[43] In addition, FINRA and the MSRB should clarify that firms will not be held responsible for any inaccurate or misleading information presented on TRACE and EMMA.

To the extent that any TRACE or EMMA reference or hyperlink must point to CUSIP-specific webpages, FINRA and the MSRB must provide shortened URLs for every CUSIP to make the disclosure more intuitive for investors, as well as easier and more succinct for the dealers to implement. In this regard, FINRA and the MSRB

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[42] *Id.*

[43] For example, a link to the URL http://emma.msrb.org/ would be intuitive for customers and simple for dealers to implement.

should develop a clear protocol whereby shortened URLs would be based on CUSIPs. Dealers, in turn, could follow such protocol for the construction of the link on the customer confirmation. Should FINRA and the MSRB pursue this approach, they should ensure that every URL remains unchanged indefinitely, such that customers will always be directed to the relevant information.

D. FINRA and the MSRB should provide examples of how required information would be expected to appear on trade confirmations.

SIFMA is concerned that FINRA and the MSRB may not have focused on the practical question of how and where the newly required confirmation disclosures could be presented within the confines of the current market's required paper-based confirmations. In particular, guidance is needed as to how such information can be provided, given the space constraints, in a manner that avoids investor confusion and the possibility of misleading investors. FINRA and the MSRB should provide specific, non-exclusive examples of how they envision such information to be included within the types of trade confirmations currently in use. To be sure, firms would require a level of flexibility given the differences in firm systems and technology configurations. Nevertheless, we believe that such an exercise can both assist FINRA and the MSRB in understanding the concerns expressed in this letter and in comments of other market participants regarding the problematic nature of attempting to include this type of information on trade confirmations, and, should FINRA and the MSRB demonstrate appropriate means of presenting such information, provide extremely useful guidance on how they expect such information to appear.

As a related matter, FINRA and the MSRB must provide uniform and clear guidance regarding the form and content of any required disclosure, including whether such disclosure should be expressed in dollar or percentage terms. As noted above, the Proposals use inconsistent language to describe the form of disclosure that would be expected to appear on trade confirmations. Under FINRA's Proposal, regarding retail customer trades, members would be required to disclose "(A) the price to the customer; (B) the member's Reference Price; [and] (C) the differential between the price to the customer and the member's reference price."[44] Under the MSRB's Proposal, disclosure of the dealer's mark-up or mark-down from the prevailing market price must be expressed "as a total dollar amount and as a percentage of the principal amount of the transaction."[45] There is no policy justification for two inconsistent approaches in this context and, should some form of the Proposals proceed, the disclosure requirement for all permitted methodologies should reflect the price to the customer, the reference price, and the differential as FINRA suggests. We believe any further configuration or representation, especially the inclusion of a total dollar amount, could lead to confusion as to what the disclosure represents.

[44] FINRA Regulatory Notice 15-36 at 20.

[45] *See supra* note 3.

E. The costs associated with implementation of the Proposals and ongoing compliance would far outweigh the potential benefits.

As we stressed in our earlier letter, FINRA and the MSRB must consider the significant burdens on competition presented by the Proposals and whether their adoption would impede the operation of the capital markets, including the secondary market for debt securities. To this end, FINRA and the MSRB must each conduct a robust cost-benefit analysis that demonstrates that the Proposals are needed, that the costs associated with them are necessary, and that no other less burdensome alternatives would meet the objective. Such an examination would reflect that the risks of even a small reduction in retail bond market liquidity could easily injure investors far more seriously than any benefit to be gained by the Proposals.[46]

The costs and burdens associated with implementation of the Proposals and ongoing compliance would be enormous. As we described in our initial comments, preliminary assessments suggest that technology costs for introducing firms would range from $500,000 for a smaller firm to as much as $2.5 million for large diverse organizations. Clearing firms may need to expend in excess of 5,000 man hours to alter their systems. Front-end vendor licensors also expect to incur substantial costs in association with any implementation process. These initial estimates do not include any of the significant ongoing costs related to additional surveillance, personnel, and system maintenance resulting from these Proposals. The implementation and ongoing legal and compliance costs associated with the Proposals are also substantial. Implementation of far-reaching changes such as those contemplated by the Proposals requires upfront and ongoing costs related to training of personnel, revision of written supervisory procedures, ongoing compliance reviews and internal audits, explaining procedures to FINRA examiners as well as annual reviews of procedures and supervisory controls processing. FINRA and the MSRB have not addressed adequately the enormous costs that the Proposals would impose on introducing firms, clearing firms, and front-end vendors. We acknowledge that providing firms a level of flexibility among methodologies in the manner that we suggest may alleviate costs to some degree.

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[46] Several recent judicial decisions have emphasized that, under the Administrative Procedure Act, the Commission must conduct a robust cost-benefit analysis as part of any rulemaking process. *See, e.g.*, *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011) (finding that the Commission failed to assess the economic consequences of its rule); *American Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166 (D.C. Cir. 2010) (finding that the Commission failed to define an appropriate economic baseline against which to measure the likely benefits and costs of its rule); *Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005) (finding that the Commission failed to identify and consider reasonable alternatives to its rule). While we recognize the differences inherent in SEC and SRO rulemaking, we think it is important that FINRA and the MSRB justify their rulemaking with the same level of rigorous cost-benefit analysis.

As a general matter, SIFMA notes that, although FINRA and the MSRB typically have control of the timing of their proposals and can delay releasing them until they have taken whatever time they think is necessary to undertake such analyses in support of such proposals, commentators must try to generate meaningful data in the short windows typically provided by FINRA and the MSRB for submitting comments. Even assuming that market participants stand ready to begin economic analysis immediately upon a proposal being introduced, it is readily apparent that such an analysis – entailing understanding and analyzing the proposal, determining what data is relevant in addressing the proposal, gathering such data, analyzing such data, reaching conclusions on such data, and reviewing the analysis and conclusions – will almost invariably take considerably longer than the one or two months provided for by FINRA and the MSRB. SIFMA believes that FINRA and the MSRB should provide much longer comment periods – from four to six months – for proposals that entail more than a limited amount of potential costs to market participants.

F. FINRA and the MSRB must consider whether the Proposals will promote efficiency, competition, and capital formation.

Exchange Act Section 15A(b)(9) and 15(B)(2)(C) require that FINRA and MSRB rules "not impose any burden on competition not necessary or appropriate in furtherance of the purposes of [the Act]." Further, Exchange Act Section 3(f) requires the SEC, when reviewing a proposed rulemaking, to "consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation." Consistent with these requirements, both FINRA and the MSRB have adopted frameworks for conducting economic impact assessments when engaged in the rulemaking process.[47] The frameworks require FINRA and the MSRB to consider the distributional impacts of any rule proposal, particularly with respect to efficiency, competition, and capital formation. Nonetheless, FINRA's Proposal does not address and the MSRB's Proposal contains only a brief acknowledgment of the effect of the proposed rules on efficiency, competition, and capital formation. In particular, given that larger firms have a greater ability than smaller firms to bear any implementation and ongoing costs associated with the Proposals, FINRA and the MSRB should conduct a thorough analysis regarding whether the Proposals will accelerate industry consolidation or force smaller firms from the market. The Proposals should be revised to include a detailed assessment regarding the impact of the Proposals on efficiency, competition, and capital formation.

[47] FINRA, *Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking* (September 2013); MSRB, *Policy on the Use of Economic Analysis in MSRB Rulemaking*, http://www.msrb.org/Rules-and-Interpretations/Economic-Analysis-Policy.aspx (last visited Dec. 7, 2015).

G. FINRA and the MSRB should provide for an implementation period of at least three years.

Without a clear and uniform proposal, it is difficult to provide a proposed implementation timeline. Nonetheless, given that the Proposals would require a fundamental reorientation of firm infrastructure and technology at enormous cost to the industry, our initial assessment is that FINRA and the MSRB should provide for, at a minimum, a three-year implementation period from the time of any rule filing. As detailed in our previous letter, the Proposals would require substantial system enhancements by introducing firms, clearing firms, and third-party vendors of front-end systems. The Proposals would require dealers to implement costly and complex modifications to front, middle, and back-office systems. At the onset and on an ongoing basis, firms may be required to coordinate across multiple entities in order to generate compliant confirmations. For example, certain information may be with the introducing broker, other information with the clearing broker, and other information with third-party vendors servicing either one. FINRA and the MSRB must consider fully the enormous operational and programming challenges related to the implementation of the Proposals.

Further complicating any effort to implement the Proposals is the fact that the securities industry will be consumed over the next 18 to 24 months with implementing a two-day settlement cycle (T+2), which presents its own set of challenges related to the confirmation statement delivery process. The same technology and operational experts working on implementing a shortened settlement cycle will be necessary to any effort to implement a new confirmation disclosure obligation. Given the substantial technical and programming challenges to implementation, the difficulties associated with coordinating data across various entities, and the limited resources available due to other regulatory objectives, FINRA and the MSRB should provide, at minimum, three years to implement and test such a large and highly complex information technology project. This timeframe may vary depending on the complexity of any rule and how many different groups are impacted. We ask that FINRA and the MSRB work with the industry on a proposed implementation that is reasonable and consistent with the multiple regulatory demands firms must address.

CONCLUSION

SIFMA thanks FINRA and the MSRB for the opportunity to comment on the Revised Proposals. We support the objective to provide retail investors with helpful and clear bond pricing information. To that end, we continue to believe that any new confirmation disclosure obligation with specific pricing information should be limited solely to riskless principal trades.

We emphasize that any confirmation disclosure obligation with specific pricing information must accommodate a market involving thousands of CUSIPs and a diverse set of fixed income products representing a wide range of trading patterns, qualities, and characteristics. Should some form of the Proposals proceed, FINRA and the MSRB should adopt a two-hour reference window and should permit flexibility among several alternative methodologies to determine that price reference. As currently formulated, the Proposals lack necessary specificity, present unworkable challenges in application and operation, risk misleading the very customers they are intended to protect, and have the potential to undermine bond market liquidity. These shortcomings demonstrate the need for further revisions and guidance in the manner we suggest.

SIFMA welcomes the opportunity to discuss the Proposals, SIFMA's comments, and the various alternatives that would best serve the objective to enhance bond market price transparency for retail investors. Should you have any questions, please do not hesitate to contact the undersigned or Bruce Newman, SIFMA's outside counsel at Wilmer Cutler Pickering Hale and Dorr LLP, at 202.663.6000.

Respectfully submitted,

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Morgan Stanley

December 11, 2015

BY ELECTRONIC MAIL

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: FINRA Regulatory Notice 15-36,
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2015-16,
Request for Comment on Draft Rule Amendments to
Require Dealers to Provide Pricing Reference
Information on Retail Customer Confirmations

Dear Ms. Asquith and Mr. Smith:

Morgan Stanley Smith Barney LLC ("MSSB") is pleased to provide comments on behalf of itself and its affiliate, Morgan Stanley & Co LLC ("MSCO" and together with MSSB, "Morgan Stanley"), to the Financial Industry Regulatory Authority's ("FINRA") Regulatory Notice 15-36 (the "FINRA Proposal") and the Municipal Securities Rulemaking Board's ("MSRB") Regulatory Notice 2015-16 (the "MSRB Proposal," and together with the FINRA Proposal, the "Proposals").

MSSB is dually registered as a broker-dealer and an investment adviser, and MSCO is a registered broker-dealer. MSSB operates one of the largest wealth management organizations in the world, with nearly $2.0 trillion in client assets as of September 30, 2015. MSSB offers personalized services to its wealth management clients through its more than 15,800 financial advisors. MSSB and MSCO maintain an extensive inventory of fixed income securities and also source securities from third parties, in each case to provide liquidity on both sides of the market to customers of both broker dealers.

Morgan Stanley continues to support FINRA's and MSRB's goal of enhancing fixed income price transparency for retail investors and appreciates the opportunity to comment on the Proposals.

Morgan Stanley generally supports the views advanced by the Securities Industry and Financial Markets Association ("SIFMA") in its forthcoming comment letter on the Proposals (the "SIFMA Letter"). However, given the size and unique characteristics of our retail and institutional businesses and our experience in fixed income markets generally, we wish to comment on particular aspects of the Proposals:

1. The Importance of Objective Disclosure Methodology

Morgan Stanley is concerned the Proposals do not adequately provide for objectively determined disclosures and, as a result, risk causing confusion for the very investors they are designed to benefit while exposing dealers to the risk of liability if their methodology and disclosures are subsequently challenged. Morgan Stanley notes that customer trade confirmations currently contain objective, factual information, including data about the security and transaction that are obtained from third party data providers or calculated using clearly defined inputs and formulas (such as accrued interest and yield to worst). Morgan Stanley is supportive of providing additional confirm disclosure for its retail investors, but any such disclosure should be formula based and not subject to interpretation.

While the Proposals on their surface may appear to call for objectively determined disclosures, they lack the specificity and guidance necessary for that end. Even with the narrower window proposed by the MSRB, determination of an exact mark-up is challenging at best in the fixed income over the counter marketplace. This is particularly difficult for firms that maintain substantial balance sheets of continuously changing inventory and that often transact in and out of cusips in the course of their market-making activities to meet the demands of customers and counterparties. Moreover, intervening market, sector and issuer events can render a potentially contemporaneous transaction an unreliable indicator of prevailing market price. In contrast, while the FINRA Proposal advances a formulaic, objective approach, it does not offer enough specificity or establish a particular regulator-approved methodology that firms could employ consistently in compliance with any eventual rule.

Accordingly, Morgan Stanley supports the adoption of an alternative readily determined price reference framework as described in the SIFMA Letter. Specifically, Morgan Stanley believes that disclosure of VWAP and the differential as a percentage of par between VWAP and the price to the customer provide investors with valuable insight into the quality of their execution in the context of the broader market for their securities. Further, VWAP could be consistently disclosed across firms, would be easily explained to, and understood by, retail investors, would not be misleading and would be objectively determined. In addition to these benefits, we believe the cost of implementation would be lessened as VWAP could be calculated by FINRA and MSRB and imported onto confirms like other referential data is disclosed. For the same reasons, Morgan Stanley would also support other objective disclosures referenced in the SIFMA Letter, such as 'high/low' reported trade prices.

While VWAP or another readily determined price reference framework offers considerable advantages to customers and firms alike and achieves meaningful disclosure, Morgan Stanley would also support a matching framework consistent with the SIFMA Letter, provided that FINRA and MSRB adopt one or more approved objective methodologies in the Proposals. The FINRA Proposal advances a matching framework but requires more guidance and specificity for firms so they can be assured of being in compliance with any disclosure requirements. Morgan Stanley also supports an exclusion from the disclosure requirements as described in the FINRA Letter due to an "unusual and material change in the price of a bond;" however, any such exclusion should also permit firms to factor in market- and sector-related developments in determining whether disclosures are required.

2. Time Frame for Disclosure

Consistent with the SIFMA Letter, Morgan Stanley believes a two-hour time frame for disclosure is appropriate and supported by FINRA's and MSRB's data which demonstrate that the vast majority of all "paired" trades occur within a very narrow window of time (see, for example, Section IIIA and the corresponding footnotes in the SIFMA Letter), which is well short of the two-hour window in the MSRB Proposal. Moreover, a narrower window substantially mitigates the risk of volatility and investor confusion and would reduce the likelihood firms would need to subjectively determine whether an intervening event was impactful enough to warrant not providing the disclosure.

Morgan Stanley respectfully submits that concerns around the risk of gaming in the context of a narrower window are misplaced. Considering the vast majority of paired trades occur well within the two-hour period, it seems highly unlikely firms would change trading patterns and materially increase risk exposure by holding positions longer merely to avoid disclosure, in particular considering the risk of non-compliance. Any remaining concerns about firms delaying executions can be substantially mitigated by supervisory policies and procedures (including surveillance) and regulatory examination and enforcement activities.

3. Uniform FINRA and MSRB Disclosure Rule

Morgan Stanley agrees with SIFMA and wishes to emphasize the importance of FINRA and MSRB developing a uniform, harmonized disclosure requirement. The risks presented by inconsistent requirements, the resulting investor confusion and the costs of implementation of two frameworks would greatly exceed the benefit (if any) of having discrete requirements under applicable FINRA and MSRB rules. Further, the timeline for implementing different FINRA and MSRB methodologies would significantly extend the period firms would require to conform to any eventual disclosure requirements.

4. Inter-Affiliate Transactions

Morgan Stanley appreciates MSRB's and FINRA's treatment of affiliate transactions under the Proposals, but as noted in the SIFMA Letter and above, Morgan Stanley requests a harmonized approach. Echoing our comments on the earlier MSRB and FINRA proposals, MSSB and MSCO fulfill client trades using inventory held by both dealers. The "trade" between these dealers is tantamount to a booking move across entities and should not be construed as a matched or reference transaction under the Proposals. Investors should not receive different disclosures depending upon whether their dealer utilizes the inventory of one or more affiliated entities.

5. Implementation Costs and Challenges

Finally, Morgan Stanley stresses the significant implementation costs and challenges associated with the Proposals, both for firms individually and when aggregated across the industry. These costs and burdens should be viewed in light of the broader concerns expressed above and in the SIFMA Letter and should be compared against the costs and benefits of the approaches to increase transparency in the fixed income markets suggested by Morgan Stanley and SIFMA. Specifically, a simple, consistent application of a clearly defined reference price (whether that reference price is VWAP, a matched price or a price determined from an alternate approach) that is not subject to a large number of inputs or contingencies would not only mitigate the potential for investor confusion, but would also make implementation less expensive.

Conclusion

In conclusion, rather than implement overly complex, confusing, costly and inconsistent disclosure requirements, Morgan Stanley respectfully requests FINRA and MSRB explore the alternatives suggested by Morgan Stanley and SIFMA to address the policy objectives set forth in the Proposals. In particular, Morgan Stanley urges FINRA and MSRB to develop a uniform approach to pricing disclosure which would permit firms to adopt an objective readily determined price reference framework as described above. Such a framework would provide meaningful, consistent disclosures to clients and increased transparency in the marketplace. An alternative matching framework could also address the concerns Morgan Stanley has with the Proposals, so long as FINRA and MSRB provide the necessary specificity concerning regulator-approved matching methodologies.

We appreciate the opportunity to provide comments to FINRA and MSRB on the Proposals and look forward to a continuing dialog on this important rulemaking initiative. We would be pleased to discuss any questions FINRA or MSRB may have with respect to this letter.

Respectfully submitted,

Elizabeth Dennis
Managing Director
Morgan Stanley Smith Barney LLC

DIAMANT
INVESTMENT CORPORATION

Comprehensive Portfolio Management

November 30, 2015

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K St. NW
Washington, DC 20006-1506

RE: FINRA Proposed Ruling 15-36

Dear Ms. Asquith,

Diamant Investment Corporation (Diamant) is making the below constructive comments regarding the above proposed ruling detailed in the FINRA Proposed Ruling 15-36 (Proposal). The reason for making these comments is that is after reading the text of this proposed rule change, it became clear that FINRA, a regulatory authority charged with creating rules for the corporate bond industry, is continuing to demonstrate excessive regulatory overreach to a properly functioning bond marketplace, without an understanding of damages the Proposal will have for the very retail customer they are claiming to help. As this Proposal is essentially identical to the 14-52 Proposal with only very minor changes, it becomes imperative that the FINRA Board take a step back from the minutia of this Proposal and grasp the enormity of what such a Proposal as 15-36 will do to the corporate bond industry.

The Corporate Bond Business

Diamant is a small, self-clearing, bond dealer that has been in business for over 40 years serving the investment needs of retail investors. I have developed considerable expertise in the retail bond business, having worked full time at Diamant, our family owned business, for over 37 years. Although the Proposal was clearly written by articulate policy makers and lawyers, it is remains very clear they have a near complete lack of understanding of the way bonds trade.

In the fixed income marketplace, business is conducted in large, but imperfect auction market. It is an auction marketplace that is dependent on bids and offers from a diverse group of bond dealers that position bonds for future sale. In the corporate bond market, bonds are not fungible, many CUSIPS trade infrequently (i.e. are not actively traded), and there are different characteristics between bond issues. There are complexities in locating and evaluating fixed income bonds that do not exist in other markets.

This auction market for fixed income bonds is completely different than transactions in the stock market. In the stock market, as little as 5,000 stocks trade in a manner where the same CUSIP can be traded on any given day in the year. With stocks, a customer order can be directed and executed on a listed stock exchange in a riskless agency transaction. It is important to recognize that bonds simply do not work this way. This is all pretty basic stuff, but apparently this point continues to be missed when proposals like this effectively treat corporate bond trading just like a riskless agency transaction.

Many broker/dealers engage in transaction in bonds. If riskless agency trading of bonds actually worked over time for broker/dealers, then competitive market forces would force agency trading to become widespread in the bond industry. Given the characteristics of corporate bonds (as described above), effecting principal trades in the auction market place is the method that nearly every broker/dealer uses to transact business.

Despite the use of computers and various bond listing systems, the bond industry remains a fragmented auction market place where large bond dealers, mid-size bond dealers, and small bond dealers all co-exist, with each type of firm providing strength to a part of the market place. Just because this industry remains an auction market does not mean the current system is broken, or needs substantial regulatory interference in the guise of helping the customer.

Economic Baseline Assumptions

The data presented in this Proposal does not support passing this Proposal. Using recent trade data, we now know that 93% of same sized corresponding corporate bond trades occur within 10 minutes. The average price spread is 0.73%. As with any average, there are trades with larger price spreads. There is no indication that these 93% of the corporate bonds trades harmed the customer. And there may be circumstances that justify a trade with higher spreads. Such a trade may have been for a small piece (such as a 5M piece); combined with either a long maturity; or a lower quality credit that trades with larger spreads; or an infrequently traded bond. Perhaps such a trade simply required more retail costs to properly handle the customer needs. This information is interesting to learn. Yet it does not indicate any violation of FINRA rules.

Although I have no reason to doubt the integrity of the people preparing the statistics, these economic baseline assumptions are missing trade information. All these trades occurred during a period of time when the capital markets have been distorted by actions of the Federal Reserve. Interest rates have been artificially low for seven years. With the certainty of losing principal value when rates increase, smaller, professional broker/dealers like Diamant have steered customers away from buying corporate bonds. Thus trade spreads and time frames from such broker/dealers are not part of the FINRA statistics. Since firms like Diamant do not trade bonds within these short times, the absence of such firms materially trading in the time frames analyzed suggest the data presented in this Proposal does not truly reflect the entire corporate bond auction market place in a normal economic environment.

No Need For The Proposed Rule

In the section titled "Need for the Rule" the assertion is made that the need for this Proposal is because FINRA is concerned investors are limited in their ability to understand and compare transactions costs. Why is the need to understand and compare the transaction costs of a bond dealer important to a customer unless they plan on becoming a bond dealer? Over the last several decades that I have been following the bond markets, FINRA has not reported a substantial pattern of pricing abuse within the corporate bond auction marketplace, and they would have already taken action to remedy such issues. So this Proposal is not based on a real problem with retail trades, but rather on an unproven premise that it would be somehow helpful for a bond dealer to provide a customer with the gross markup in certain bond trades. Without demonstrating a real need, FINRA is practicing regulatory overreach in creating rules to solve a problem that does not exist.

Still A Very Bizarre Line Of Reasoning

This entire Proposal is based on the premise that markups are somehow bad. This presumption has little to do with "helping" the customer with confusing partial disclosure. We all must recognize it has the feel of a politically driven effort to penalize a business sector by attempting to eliminate profits in the fixed income bond business. Which industry will be next?

There seems to be a misguided belief that securities bond dealers can continue to operate in a compliant manner in an already heavily regulated industry; can add substantive additional compliance and operational costs to attempt to adhere to this Proposal; can continue to risk capital to provide a supply of securities to their customers; and can provide associated ongoing investment securities services to their customers; all while earning little or any gross profit. This theory simply will not work in the business world.

The reasoning behind this Proposal is that by forcing disclosure of the gross trade profit of a bond dealer, customers will somehow be better informed about the characteristics of the corporate bond investment they are making. By itself this is a very bizarre line of reasoning that is not used in any other decision making in the purchase of either small or large ticket items. Again, to illustrate just a few examples:

> When a customer purchases either a new or used car, they never see the gross profit that the car manufacturer and/or the car dealer is making, as their focus properly is on securing a piece of transportation that meets their needs.
>
> When a customer renovates or purchases a house, they never see the gross profit of the builder or the individual seller, as their focus properly is on whether the location and structure is suited to their needs for shelter.
>
> When a customer purchases food at their local supermarket, they never see the gross profit in each item in their cart, as their focus is on shopping in a convenient location for quality merchandise that meets their needs of nourishment.

From an ethical viewpoint, once a business sector (like bond dealers) is forced to disclose its gross profits on a transaction, in an effort to achieve truly full disclosure, such disclosure should also be mandated on every transaction that a retail customer engages in during the conduct of their daily activity. Prior to turning this Proposal into a regulatory ruling, FINRA should first coordinate with all regulatory entities throughout the Federal Government and force all sectors of the U.S. economy to make similar disclosures. This would have a chilling negative impact on all sectors of the U.S. economy, and would have a near universal outcry of "big brother" or "big government" impeding free market capitalism. Yet this is exactly what this Proposal as written achieves, and it creates the ground breaking precedence to affect this disclosure on other industries.

Trading with Proposed Disclosure Rules

In the corporate bond business, the retail customer needs the assistance of a professional to navigate the selection of available fixed income products. When a client buys corporate bonds, their most important decision points may include: the income stream (coupon); years until their principal is returned (maturity date); return on the investment (yield which presumably is competitive to other similar bonds); what events can cause the principal to be returned early and what is the impact (call price and yield to call); what happens to this investment when rates move (duration); what revenue streams secure the interest payment; what assets secure the principal payment; what other alternatives are available; whether this investment should be made now revisited at another time; and whether the bond fits into a customer portfolio. Successful fixed income investment decisions have always been made on these types of important information.

What continues to make this Proposal so bizarre is that FINRA now believes customers should focus their attention not on important information described above, but instead on the disclosure of a gross trade profit number that should not be terribly relevant to the overall decision to purchase a bond.

As the FINRA Board must be well aware of, typically a bond dealer uses the gross profit from principal trading firm to cover costs that include: paying the trader; the registered representative that handled the customer discussion; the manager who oversees the trading desk and retail broker; any market risks that may occur in placing bonds into firm position; the back office operations staff that clears the trade; the external clearing costs incurred by the broker/dealer; the ongoing annual custody costs of collecting income along with any calls or maturities on the bond; the compliance and audit costs to maintain regulatory compliance within the firm; the normal costs to maintain a business such as rent and communications costs; and the ability of the broker/dealer to earn a profit for its shareholders.

The unstated objective of this Proposal is to force dealers to make a lower gross profit. Of the above costs involved with a bond trade, what part of the trade should be cut out without harming the customer? If the salesperson is compensated less to communicate with their customer, or if the trader is not paid to search the market, and/or the firm no longer wants to bother holding inventory, this all seems to run counter intuitive to "helping" the customer make prudent investment decisions in buying a corporate bond. For trades that would occur with a disclosure requirement, FINRA should expect that the customer will no longer receive the needed attention to the above critical decision points inherent in a trade, as such disclosure may reduce or eliminate the gross compensation of a dealer to provide these tasks.

Is it really helpful for a retail customer to see the gross profit printed on a bond trade? I would expect nearly every customer will call their registered representative to complain about the gross profit, regardless what the number actually is. The registered representative is not earning the gross profit, and likely is unaware of the number until after the confirmation is mailed. Why would the registered representative want to have such a conversation with their customer? In this scenario, most registered representatives will simply stop selling corporate bonds to retail customers, as it is much easier to sell other investment products with a higher sales load.

And if this gross trade profit appears on the confirmation that is received by the customer on or after settlement date, is the intent of this disclosure to permit customers to break trades because a gross profit was different than they expected? If so, then any of the specific trades that meet the disclosure requirement will have to be considered as un-firm, or incomplete transactions that may have to be reversed sometime in the future. In the future, would it not be advantageous for a customer to review trades over the past six years of disclosure, select all the trades which declined in market value, and return the trades back to the bond dealer using the reasoning the gross profit was too high on the selected trades? How would a regulator expect bond dealers to haircut their net capital for incomplete trades when the dealer does not know which trades may be returned in future periods? Clearly no bond dealer would ever want to sell bonds to customers with this type of liability.

In a recent Wall Street Journal article (October 24, 2015 page B1), a finance professor carefully picked an example of a corporate bond he felt had a high markup. On a 30M piece, he calculated a gross profit of $187.50. After a careful reading of this article, one must question his "apples to oranges" comparison of this bond trade to the ~$10 cost of a stock trade effected at a deep discount brokerage firm. Another comparison is made between the spread of a corporate bond and the bid/offering spread of a stock listed on the NYSE. Any arguments that compare exchange listed stock trading with the auction market place of corporate bond trading confirms a fundamental misunderstanding of how the corporate bond market place actually works. Thus I would discount the rationale from any academic who make such arguments.

Nonetheless, in this example, if a broker/dealer was to make the disclosure of $187.50 gross profit without explanation, how does this serve the customer? Perhaps such disclosure should detail the costs to handle the transaction to illustrate a net profit. Attempting to explain a gross profit on certain trades, versus a net profit, will hinge on the linguistic ability of the legal counsel of each bond dealer. With good lawyers, bond trades will become an event that results in both misleading and confusing customers over an irrelevant decision point.

Unintended Consequences

Smaller firms will conclude that offering corporate bonds to retail customers is not worth the added compliance costs. Diamant's proprietary back office system currently handles all customer functions related to the purchase or sale of corporate bonds. Diamant also has sufficient regulatory compliance to monitor corporate bond activity under existing regulatory rules. Yet this time tested, compliant system does not have the ability to link separate principal trades to another. It would be a major undertaking in terms of operational and software costs to re-build a back office system that could identify transactions subject to disclosure, and then place disclosure information specific to that particular trade on the confirmation. In addition, there are additional regulatory compliance costs of creating special written procedures to identify trades that would require gross profit disclosure, legal costs to prepare prudent disclosure text, along with the ongoing compliance effort to demonstrate adherence to this unprecedented trade policy and procedures.

As Diamant cannot justify the added operational costs to rebuild a back office system, the only way to comply with this Proposal is to prohibit any retail trades that fall under this Proposal as currently written. This is not a decision we take lightly, as we have been offering retail customers the ability to trade corporate bonds since 1974. Our decision to prohibit certain retail trades in corporate bonds will be based solely on this FINRA ruling.

When a seasoned broker/dealer makes such a decision as the only way to comply with this Proposal, it is easy to envision a marketplace where retail corporate bonds will be concentrated in even fewer large institutions. Concentrating trading to a handful of firms places these firms firmly in the "too big to fail" category. This means that the new definition of a fair and orderly auction marketplace will have less competition with fewer smaller firms participating. This is contrary to the concept of capitalism, but this clearly will be the outcome of this ruling, and the FINRA Board must recognize this outcome when casting their votes.

Experienced corporate bonds traders will leave the broker/dealer business. Trading will be handled by a small number of less experienced traders. As volumes pick up and trades are concentrated among a handful of firms, we should all expect more pricing errors by the remaining overworked traders. With an auction marketplace that may move towards an electronic bulletin board with fewer bids and offerings, the likely scenario is that an institutional type of customer will evolve that is not regulated by FINRA. Such an entity will use the electronic bulletin board to provide the needed liquidity for the retail customers at spreads that will benefit the institutional customer, not the retail customer.

The remaining broker/dealers handling corporate bonds will be focused on demonstrating the soundness of their compliance systems and procedures instead of the focusing on the retail customer, and will simply trade whatever is available on the electronic bulletin board. This unintended negative impact will be very beneficial to the professional traders not regulated by FINRA. As corporate bonds will then be essentially priced and offered by professional traders that are unregulated by FINRA, customers will likely pay more for the bonds regardless of what gross profit disclosure appears on a confirmation. Thus this Proposal is a no-win situation, in that the broker/dealer incurs great economic costs, potentially harms customer relationships, and the customer in the end does not gain any of the perceived benefits intended by the regulators.

A Better Time Frame

If FINRA finds itself in a political position where it need to show some action, then FINRA should design a disclosure timeframe based on its own research set forth in this Proposal. If 93% of same sized corresponding corporate bond trades occur within 10 minutes of each other, and FINRA decides to negatively impact such trading, then disclosure should occur on principal trades where matching buy and sell trades occur in this time frame. Instead an unworkable 1 day time frame from the perspective of our back office system, this disclosure timeframe should be 10 minutes. Or it could be 30 minutes, 1 hour, or even 2 hours. Any of these timeframes cover the trading identified in the Proposal. The benefit of these shorter timeframes is that small businesses, like Diamant, would be able to set up a manual review process in the back office to identify trades subject to disclosure. The shorter time frame would make it possible for smaller firms to set up procedures that use existing back office systems to achieve regulatory compliance with such a Proposal. By keeping compliance and software costs manageable, smaller firms could become, or remain active, in the business of trading corporate bonds.

Conclusion

After reviewing the Proposal and alternatives, FINRA needs to recognize this Proposal will do more harm than any good. The disclosures will clearly mislead and confuse retail investors to a degree that cannot be remedied by education, explanations, or descriptive documents accompanying a confirmation. Harming the relationship between the customer and the bond dealer, and having bond dealers reduce or eliminate retail trades, all for the sake of this misguided Proposal, simply does not add any benefit to the retail customer.

The auction marketplace has many intertwined industry participants that include retail customers; institutional customers; corporate bond dealers that trade mainly with other corporate bond dealers; and corporate bond dealers that trade mainly with their customers. All these participants within this large auction market will be adversely impacted. The larger harm will come from the auction marketplace having limited liquidity from fewer broker/dealers, or liquidity from professional institutions not subject to FINRA rules. These are very realistic outcomes from this Proposal.

To continue to maintain an orderly and regulatory compliant market in corporate bonds, FINRA must recognize the complexity within the entire fixed income marketplace, review the alternatives of enforcing existing rules, focus on firms that may fit a pattern of having a material price difference on trading corporate bonds, and commit to taking no action on the entire Proposal.

Yours truly,

Herbert Diamant
President

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF THE
INVESTOR ADVOCATE

December 11, 2015

Submitted Electronically

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
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Marcia E. Asquith
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FINRA
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RE: MSRB Regulatory Notice 2015-16
Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

RE: FINRA Regulatory Notice 15-36
Request for Comment on Revised Proposal Requiring Confirmation Disclosure of Pricing Information in Corporate and Agency Debt Securities Transactions

Dear Mr. Smith and Ms. Asquith:

Pursuant to Section 4(g)(4) of the Securities Exchange Act of 1934 ("Exchange Act"), the Office of the Investor Advocate[1] at the U.S. Securities and Exchange Commission ("Commission" or "SEC") is responsible for, among other things, analyzing the potential impact on investors of proposed rules of self-regulatory organizations ("SROs").[2] In furtherance of this objective, we routinely review significant rulemakings of the Municipal Securities Rulemaking Board ("MSRB" or the "Board") and the Financial Industry Regulatory Authority ("FINRA"). We also make recommendations and utilize the public comment process to help ensure that the interests of investors are given appropriate weight as rules are being considered. As required by law, we report to Congress regarding our objectives and activities, which includes a summary of the recommendations we make and the responses to those recommendations.[3]

[1] This letter expresses solely the views of the Investor Advocate. It does not necessarily reflect the views of the Commission, the Commissioners, or staff of the Commission, and the Commission disclaims responsibility for this letter and all analyses, findings, and conclusions contained herein.
[2] 15 U.S.C. § 78d(g)(4).
[3] 15 U.S.C. § 78d(g)(6).

As indicated in our Report on Objectives for Fiscal Year 2016, our Office is currently focused on municipal market structure and any corresponding reform initiatives that may impact investors.[4] Thus, we appreciate this opportunity to provide comments in regard to MSRB Regulatory Notice 2015-16, Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers ("MSRB Notice 2015-16"), and FINRA Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets ("FINRA Notice 15-36").

I. Background

Currently, broker-dealers are required to provide retail customers with confirmation statements following fixed income transactions, but they are under no regulatory obligation to include detailed pricing information on those trade confirmations. We are not aware of any regulatory barrier preventing firms from providing enhanced and effective pricing disclosures to their retail customers on a voluntary basis. Nevertheless, current industry practices only satisfy broker-dealers' regulatory obligation to investors, and the resulting confirmation statements generally provide no more than the price that the customer paid or received for a fixed income security. Because industry practices have not addressed the longstanding problem of transaction transparency, retail investors remain disadvantaged by the lack of information they receive in confirmation statements. As a result, a regulatory solution appears necessary.

Previous Proposals

Previously, the MSRB and FINRA requested comment on related draft rule proposals, MSRB Regulatory Notice 2014-20 and FINRA Regulatory Notice 14-52. These proposals generally were consistent with each other and were designed to work in tandem to provide retail investors with better price transparency in corporate and municipal bond transactions.

The draft amendments for MSRB Regulatory Notice 2014-20 would have "require[d] dealers to disclose on the customer confirmation the price to the dealer in a 'reference transaction' and the differential between the price to the customer and the price to the dealer for same-day, retail-size principal transactions."[5] The MSRB defined the "reference transaction" as one in which the dealer purchases or sells the same security on the same date as the customer trade.[6] The proposed rule would have required dealers to "calculate and disclose the difference in price between a reference transaction disclosed on the confirmation and the price to the customer receiving the confirmation."[7] The proposed disclosure requirement would have applied to transactions involving 100 or fewer bonds or bonds in a par amount of $100,000 or less.[8]

[4] *See* Office of the Investor Advocate, Report on Objectives for Fiscal Year 2016, June 30, 2015, http://www.sec.gov/advocate/reportspubs/annual-reports/sec-office-investor-advocate-report-on-objectives-fy2016.pdf.
[5] MSRB, Regulatory Notice 2014-20, Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations, at 1 (Nov. 17, 2014), http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-20.ashx?n=1.
[6] *Id.* at 8.
[7] *Id.* at 8-9.
[8] *Id.* at 9.

The draft amendments for FINRA Regulatory Notice 14-52 took a very similar approach. FINRA proposed that "where a firm executes a sell (buy) transaction of 'qualifying size' with a customer and executes a buy (sell) transaction as principal with one or multiple parties in the same security within the same trading day, where the size of the customer transaction(s) would otherwise be satisfied by the size of one or more same-day principal transaction(s), confirmation disclosure would be required."[9] FINRA's proposal defined the term "qualifying size" as a transaction of 100 bonds or less or bonds with a face value of $100,000 or less.[10] The proposed customer confirmation disclosure would have included the price to the customer, the price to the member of a transaction in the same security, and the differential between those two prices.[11]

We supported these steps of the MSRB and FINRA to improve the availability of pricing information and concurred, generally, with the goals underlying both MSRB Regulatory Notice 2014-20 and FINRA Regulatory Notice 14-52.[12] We encouraged the MSRB and FINRA to adopt their respective proposed amendments because we believe that retail investors would benefit from the inclusion of additional pricing transparency on their customer confirmations.[13] We indicated that disclosing the same-day price reference information would provide retail investors with more effective tools to evaluate their transactions and the quality of service provided.[14] However, after receiving public comment, the MSRB and FINRA issued revised proposals instead of adopting the rules as proposed.

<u>Current Proposals</u>

FINRA Regulatory Notice 15-36 retains the same basic approach as the prior FINRA proposal. If a firm sells to a customer as principal on the same day it buys the security from another party, the firm would be required to disclose on the customer confirmation the price to the customer, the price to the firm of a same-day trade (reference price), and the difference between the two prices.[15] However, the disclosure requirement would now only apply to bond trades on behalf of non-institutional accounts, no matter the size of the trade.[16] In addition, FINRA's new proposal would allow for alternative calculation methods for more complex trade scenarios and would permit member firms to provide clarifying information when there has been a material change to the price of a security between the reference transaction and the customer transaction.[17] It also would require member firms to include a hyperlink to relevant Trade Reporting and Compliance Engine (TRACE) data on the customer confirmation.[18]

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[9] FINRA, Regulatory Notice 14-52, Pricing Disclosure in the Fixed Income Markets, at 3 (Nov. 17, 2014), http://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_14-52.pdf.
[10] *Id.*
[11] *Id.* at 1.
[12] *See* Comment Letter, Rick A. Fleming, Investor Advocate, SEC, *RE: MSRB Regulatory Notice 2014-20, Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations* (Jan. 20, 2015), http://www.msrb.org/RFC/2014-20/USSEC.pdf; *see* Comment Letter, Rick A. Fleming, Investor Advocate, SEC, *RE: FINRA Regulatory Notice 14-52, Request for Comment on Pricing Disclosure in the Fixed Income Markets* (Jan. 20, 2015), http://www.finra.org/sites/default/files/notice_comment_file_ref/SEC.pdf.
[13] *Id.*
[14] *Id.*
[15] FINRA, Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets, at 1 (Oct. 12, 2015), http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-15-36.pdf.
[16] *Id.* at 3. As noted above, qualifying size was defined as 100 bonds or less, or face value of $100,000 or less.
[17] *Id.*at 3-4.
[18] *Id.* at 5.

In contrast, MSRB Regulatory Notice 2015-16 takes a significantly different approach from the earlier MSRB Regulatory Notice 2014-20. The new proposal would require customer confirmations to disclose the "mark-up" for principal transactions when the dealer transacts in a municipal security in a specified trade size on the same side of the market as the customer.[19] Under the proposed new calculation, the security's mark-up would be the difference between the price to the customer and the "prevailing market price" for the security at the time of the customer's transaction.[20] Moreover, under the proposed amendment, the dealer's responsibility to disclose the mark-up would be triggered only when the dealer engaged in its own same-side transaction within two hours of the customer transaction.[21] Transactions occurring the same day but outside of that two-hour window would not be subject to mandatory pricing disclosure.[22]

In addition, the new MSRB proposal would incorporate changes similar to those in the new FINRA proposal. For example, MSRB Regulatory Notice 2015-16 would require mark-up disclosure for "non-institutional" account transactions, which is already defined within the MSRB rules, as opposed to transactions of a certain size.[23] Further, it requires dealers to disclose a hyperlink and URL address to the "Security Details" page for the customer's security on the MSRB's Electronic Municipal Market Access (EMMA) service, along with a brief description of the type of information available on that page.[24]

FINRA and the MSRB both propose new exceptions to the required pricing disclosure. Neither would require disclosure of reference pricing in transactions related to offerings of new issues.[25] Additionally, each would provide exceptions for certain transactions involving functionally separate trading desks.[26]

II. Evaluation

As an initial matter, we believe investors would be poorly served by pricing disclosures that are different for corporate bonds as compared to municipal bonds. To avoid investor confusion, it is important for FINRA and the MSRB to adopt consistent rules related to confirmation disclosure. Toward that end, we submit this single comment letter in response to both proposals, and we suggest which of the competing ideas should be adopted by both MSRB and FINRA.

Timeframe

As noted above, FINRA proposes to require disclosure when the initial and subsequent transactions occur on the same trading day.[27] The MSRB, however, has proposed to shorten the relevant

[19] MSRB, Regulatory Notice 2015-16, Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers, at 1 (Sept. 24, 2015), http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2015-16.ashx?n=1.
[20] *Id.* at 8.
[21] *Id.*
[22] *Id.*
[23] *Id.* at 9 n.25; *see also* MSRB Rule G-8(a)(xi) (defines institutional account).
[24] *Id.* at 12.
[25] *Id.* at 9-10. *See supra* note 15, at 3; *see supra* note 19, at 10.
[26] *See supra* note 15, at 3; *see supra* note 20, at 11.
[27] *Supra* note 15, at 2.

window of time to two hours on either side of the customer trade.[28] According to the MSRB, its revised window would still require mark-up disclosure for at least half of all retail-sized customer trades in the secondary market.[29]

We strongly oppose the proposed two-hour window. We believe the minimum window of time for disclosure should be the full trading day. Although dealers often trade within two hours under existing rules, dealers could easily adjust their behavior to avoid the new disclosure requirements by trading a few minutes outside of the proposed two hour window. Therefore, current trading behavior is not necessarily indicative of trading behavior that will occur if the revised proposal is implemented.

Disclosure avoidance would be much more difficult under the timeframe in the FINRA proposal, which requires disclosure for transactions occurring on the same trading day. A dealer takes on much greater balance sheet risk by holding inventory overnight, which would deter dealers from separating transactions in order to avoid disclosure. Thus, we encourage the MSRB to forgo the proposed two-hour window. At a minimum, both FINRA and the MSRB should require pricing disclosure for transactions occurring within the same trading day.

Mark-Up vs. Reference Price

Although we oppose the MSRB's proposal to shorten the relevant trading window to two hours, we support moving forward with mark-up disclosure as described in the new MSRB proposal. Initially, we supported the MSRB's original proposal for price reference disclosure because it was a significant improvement over the *status quo*. In addition, the price reference proposal appeared to have the advantage of simplicity, meaning that the required disclosures would be relatively easy for dealers to ascertain. For similar reasons, we supported the original FINRA proposal for price reference disclosure.

From the investor perspective, however, there are advantages to the new MSRB mark-up proposal. Admittedly, it may lead to disclosure of a smaller cost to investors under certain circumstances. For example, if a dealer purchases a security and there is a significant positive market move prior to the resale to a retail customer, the amount of the mark-up would only be the difference between the price of the resale and the "prevailing market price" at the time of the resale, instead of the full difference between the original purchase and the subsequent resale. However, the MSRB proposal provides investors with the relevant information about the actual compensation the investor is paying the dealer for the transaction. It reflects market conditions and has the potential to provide a more accurate benchmark for calculating transaction costs.[30]

Importantly, we note also that the calculation of a true mark-up, once established under these rules, need not be limited to a single trading day. After the systems are in place for disclosing mark-ups on same-day transactions, dealers may decide for competitive reasons to disclose mark-ups on all transactions. Moreover, FINRA and the MSRB could choose to require disclosure beyond the one day window after assessing the implementation of the new rules. In contrast, a price reference disclosure model does not account for intervening market events that affect the value of the bond during the lag between the reference transaction and the customer transaction, so the disclosure becomes less

[28] *Supra* note 19, at 8.
[29] *Supra* note 19, at 8 n.22.
[30] It is our understanding that the process for calculating mark-up under the MSRB revised proposal may build upon existing systems. To that end, it may be easier for industry to implement disclosure under the MSRB's revised proposal.

meaningful as the window for disclosure increases. Thus, for disclosure of pricing information beyond a one day window, a mark-up model could serve as a better framework than a price reference model.

Although we support a move to disclosure of a mark-up that is based upon a prevailing market price, we are concerned with potential manipulation of the prevailing market price calculation. Errors in the calculation, whether intentional or not, could significantly alter the information provided to investors. With this in mind, we encourage the MSRB and FINRA to monitor carefully the industry's implementation of the rules to ensure that dealers appropriately determine the prevailing market price.

The MSRB proposes to express the mark-up as both a total dollar amount and percentage of the principal amount of the customer transaction. FINRA's proposal would disclose a differential only as a numeral. We believe that disclosing a mark-up as a total dollar amount and a percentage would more effectively enable retail investors to evaluate their transaction costs and monitor the quality of service provided by dealers. Thus, we support the MSRB approach.

Functionally Separate Trading Desk Exception

Both the MSRB and FINRA revised proposals include an exception for transactions involving "functionally separate" trading desks. Although we do not oppose an exception of this nature, both proposals could be strengthened by incorporating greater precision or guidance relating to the meaning of "functionally separate." For example, would FINRA anticipate applying similar standards to those that it currently employs when evaluating whether broker-dealer self-trades are *bona fide* or fraudulent "wash sales" under Supplementary Material .02 to FINRA Rule 5210, or does FINRA believe that a different standard would be appropriate here?[31] To avoid the possibility of such an exception becoming a loophole or blanket exception, we strongly encourage both the MSRB and FINRA to provide robust guidance surrounding the meaning and requirements concerning functionally separate trading desks.

We also believe the final rules should incorporate the strongest features of both proposals. Thus, at a minimum, a 'functionally separate' trading desk exception should require that the trading desks through which transactions are made have no knowledge of the customer transaction and that the transactions and positions of the separate desk must not regularly be used to source retail transactions at the other desk.

III. Conclusion

We appreciate the MSRB's and FINRA's acknowledgement of the information disparity inherent in fixed income market transactions, and we support your corresponding efforts to address retail customers' information disadvantage by increasing price transparency and the availability of pricing information. While we regard both proposals as improvements upon the *status quo*, we believe that combining the MSRB's mark-up disclosure methodology with FINRA's same day window would best serve the interest of investors. We also believe that the rules must be enforced rigorously to prevent manipulation of the information provided to investors.

[31] *See* Order Approving Proposed Rule Change, as Modified by Amendment No. 1, Relating to Self-Trades and FINRA Rule 5210, Exchange Act Release No. 34-72067 (May 1, 2014) [79 FR 26293 (May 7, 2014)], at n.12 ("Transactions that originate from unrelated algorithms or from separate or distinct trading strategies, trading desks, or aggregation units that are frequent or numerous may raise a presumption that such transactions were undertaken with the intent that they cross and may, therefore, be intended as manipulative or fraudulent.").

Such changes could have a significant impact on the behavior of dealers and individual investors. Individual investors engaged in retail-size trades will be better equipped to evaluate the transaction costs and the quality of service provided to them by their dealers. This, in turn, should promote competition and improve market efficiency among dealers. The changes will help ensure that the prices and markups are appropriate in light of the market for the particular security.[32]

Should you have any questions, please do not hesitate to contact me or Senior Counsel Ashlee Connett at (202) 551-3302.

Sincerely,

Rick A. Fleming
Investor Advocate

cc (electronically): Lynnette Kelly, Executive Director, MSRB
Robert Fippinger, Chief Legal Officer, MSRB
Michael Post, General Counsel – Regulatory Affairs, MSRB
Patrick Geraghty, Vice President, Market Regulation, FINRA
Cynthia Friedlander, Director, Fixed Income Regulation, FINRA
Andrew Madar, Associate General Counsel, FINRA

[32] *Supra* note 5, at 7.

Consumer Federation of America

December 11, 2015

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Ronald W. Smith
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Re: FINRA Regulatory Notice 15-36; MSRB Regulatory Notice 2015-16
Pricing Disclosure in the Fixed Income Markets

Dear Ms. Asquith and Mr. Smith:

I am writing on behalf of the Consumer Federation of America (CFA)[1] regarding FINRA's and MSRB's revised proposals to require confirmation disclosures for retail fixed income transactions. In January 2015, CFA expressed its strong support for FINRA's and MSRB's initial proposals to require heightened confirmation disclosures, which we thought provided critical cost information that would benefit retail investors significantly.[2] After receiving feedback, FINRA has proposed certain technical adjustments to its proposal that would improve the rule's workability without undermining the regulatory goals of allowing retail investors to make more informed investment decisions and fostering increased price competition in fixed income markets. However, the same cannot be said for MSRB's revised proposal, which would allow firms to easily evade their confirmation disclosure requirements, thus undermining the goals the disclosures are seeking to promote.

While regulatory coordination and consistency are desirable goals, they must not be used as justifications for weakening crucial investor protections. Toward this end, if both SROs favor a coordinated approach, they should finalize a rule that closely tracks FINRA's revised proposal, not the MSRB's.

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[1] CFA is a non-profit association of nearly 300 national, state, and local pro-consumer organizations. It was formed in 1968 to represent the consumer interest through research, advocacy and education.
[2] FINRA Regulatory Notice 14-52; MSRB Regulatory Notice 2014-20, http://consumerfed.org/pdfs/FINRA-MSRB-proposed-rules-01-20-2015.pdf

I. FINRA's revised approach requiring disclosures for same-day transactions still achieves the goals that these disclosure are intended to promote, while MSRB's revised approach requiring markup disclosures based on a narrow two hour timeframe undermines the goals these disclosures are intended to promote. MSRB must return to a same-day transaction approach if it hopes to provide retail investors with critical cost information.

FINRA's revised proposal refines without undermining its initial proposal to require firms to disclose additional pricing information for retail customer trades in corporate and agency debt securities. As in the initial proposal, firms that buy (sell) as principal with their customers in corporate and agency debt security transactions and on the same day sell (buy) the same securities must disclose on their customer confirmations the price to the customer, the price to the firm of the transaction in the same security, and the differential between those two prices.

Reiterating our previous comments, we strongly support requiring disclosure of pricing information for all trades in the same security on the same day of trading rather than limiting disclosure to riskless principal markups. Requiring disclosure for all same-day trades would allow for a more mechanical analysis by firms which, in turn, would make it easier for investors to compare transaction costs across firms. Disclosing riskless principal markups, on the other hand, would reduce the comparability of transaction cost information across firms. Because what is considered a riskless principal markup is susceptible to varying and often arbitrary interpretations, using a riskless principal markup standard could result in inconsistent markup calculations.

Requiring disclosure for all same-day trades would also decrease the possibility of evasion, as this time-frame is broad enough to capture the vast majority of trades that are currently made on a matched basis or can reasonably be expected to be made under the rule. Requiring disclosure for a narrower window, however, would create incentives for firms to hold positions long enough to avoid their disclosure obligations and, perversely, encourage firms to remain exposed for longer periods throughout the day. As a policy matter, a rule that requires enhanced disclosure should neither be gameable nor encourage risky behavior. FINRA's same-day trading approach achieves those goals, though we encourage FINRA to continue to monitor trading practices after the rule is adopted to ensure that the rule is not being gamed.

In contrast, it is difficult to see how MSRB's revised approach requiring disclosure of markups only for dealer trades that occur within two hours of a customer's transaction achieves any sensible or meaningful policy goals. If, in order to evade the rule's requirements, a significant number of firms hold onto positions beyond the 2 hour window, retail customers would not receive pricing disclosure and would be no better off than they are today. That is a predictable outcome of the rule. While saying that it is not proposing to use a two-hour timeframe to define what a "riskless principal" transaction is, that is effectively what MSRB is doing for purposes of this proposal. And, by saying that two hours is "sufficient to cover transactions that could be considered 'riskless principal' transactions under any current market understanding of the term," it is implying that anything longer might not be considered "riskless." As with other approaches to considering what a riskless principal transaction is, this two-hour approach is arbitrary, as it is based neither on function nor on known or expected market dynamics.

The two-hour timeframe also would create incentives for firms to hold positions long enough to evade the rule's disclosure requirements. Firms that currently match trades in under 30 minutes would have an incentive under the rule to delay their trading for 2 hours and 1 minute to avoid their disclosure obligations. So, while *current* TRACE and EMMA data indicate that the vast majority of same day retail-size match trades occur within 30 minutes of each other, regulators should not infer that those trading behaviors would remain under the rule. And, while FINRA's proposal states that the revised FINRA approach and the MSRB's approach would produce similar outcomes "in many circumstances," that statement is reflective of what the outcomes would be under current market conditions, not under different incentives that would likely alter trading behavior. Further, as FINRA's proposal makes clear in footnote 31, MSRB's approach is likely to be much narrower in practice than FINRA's approach and result in less disclosure to retail investors. According to TRACE data from the first quarter of 2015, for example, 38 percent more retail-size trades would have received FINRA's proposed reference price information than had those trades been limited to riskless principal trades. Thus, even under current market dynamics, a riskless principal markup approach would result in retail investors' receiving less price disclosure than they would under a same-day approach. Instituting a riskless principal markup approach that changes firms' incentives to hold past the point they are required to disclose would result in even less disclosure than that.

The two-hour timeframe would also encourage firms to remain exposed for longer periods throughout the day than they might otherwise be. Under firms' current regulatory incentives, the threat of firms' being exposed to disadvantageous market movements mitigates firms' incentives to remain exposed longer than necessary. However, this rule introduces a new incentive, avoiding disclosure, which counteracts that threat. In most circumstances, holding onto positions for a few extra hours will not materially increase firms' risk profiles, which may push them to holding positions longer. However, should there be material changes to the prices of securities during an unexpected period of high volatility, which will inevitably happen from time to time, a firm's exposure could result in serious losses to the firm. It is inappropriate for regulators to introduce incentives that encourage such risky behavior, even if the circumstances that can lead to serious losses occur rarely.

It appears from footnote 19 in MSRB's reproposal that the MSRB has revised its approach in response to substantial broker-dealer industry opposition to MSRB's and FINRA's initial proposals. Specifically, MSRB cites to comments by the Securities Industry and Financial Market Association (SIFMA), Morgan Stanley Smith Barney, LLC and Wells Fargo Advisors, LLC claiming that markup disclosure on riskless principal transactions "could achieve similar or greater benefits than the pricing reference proposal but at significantly lower cost" and comments by Bernardi Securities, Financial Services Roundtable (FSR) and Hilliard Lyons, favoring limiting any disclosure to riskless principal transactions. But the role of regulators is not simply to take their cues from members of industry, who have obvious incentives to curtail the information they provide to investors. The role of the MSRB, as it notes in its mission statement, is to "protect investors, municipal entities and the public interest by promoting a fair and efficient municipal market, regulating firms that engage in municipal securities and advisory activities, and promoting market transparency."

Despite this investor-focused mission, nowhere in its comments does MSRB even acknowledge CFA's initial comment expressing strong support for the same-day pricing reference approach, much less respond to our comments expressing support for that approach. Instead, MSRB merely adopts the same view as the industry "based on careful consideration of all of the comments received on the pricing reference proposal…" The inherent lack of balance in the regulatory process, which results from the fact that industry comments will *always* outnumber comments from investors and investor advocates, is made worse when regulators choose simply to ignore the investor comments they do receive. By focusing exclusively on industry objections and ignoring investor benefits of its original approach, MSRB has proposed an approach that would allow firms to disclose pricing information to the extent it is most conducive to those firms, rather than what is most conducive to market integrity and retail investor protection.

For the above reasons, we urge MSRB to return to its original approach, which better protects investors, does more to promote market transparency, and more closely tracks FINRA's approach requiring disclosures for same-day transactions.

II. FINRA's and MSRB's replacement of a size-based disclosure threshold with a retail customer standard better captures trades that are likely to most benefit from enhanced price disclosures.

In their initial proposals, FINRA and MSRB used a size-based requirement to trigger disclosure requirements, whereby disclosure would apply to a transaction with a customer to purchase or sell 100 bonds or less or bonds with a face value of $100,000. While we understood that such a size-based standard had the potential to be both over-inclusive, in that it might capture small institutional trades, and under-inclusive, in that it might not capture large retail investor trades, we still thought it was a reasonable approach to capturing those trades that are retail in nature and would most benefit from enhanced price disclosures. In our initial comments, we urged FINRA and MSRB to continue to monitor market activity in relation to the definition of "qualifying size" to determine whether that standard should be modified.

The revised proposal replaces the "qualifying size" threshold with a retail customer account standard. This strikes us as a better approach toward capturing trades that are likely to benefit most from enhanced price disclosures. Under the revised approach, all retail transactions will receive confirmation disclosures regardless of how large they are, and no institutional transactions will receive confirmation disclosures regardless of how small they are. This is an appropriate distinction for the purposes of this rule, as institutional investors are typically more sophisticated and better-informed than retail investors and, as a result, should already understand the transaction costs they are paying.

III. The proposed exemptions to the revised proposals are, by and large, reasonable, with a few exceptions. FINRA and MSRB must ensure that those exemptions are not used to evade disclosure obligations.

FINRA has proposed to allow firms the flexibility to establish a reasonable alternative methodology for determining the reference price when more complex trades are made. Under FINRA's proposed approach, if one or more intervening principal trades of a different size are made, firms have two options. They can employ the average weighted price of the firm trades that equal or exceed the size of the customer trade, or the price of the last same-day trade executed as principal by the firm prior to the customer trade (or closest in time if executed after). Further, the firm must consistently apply that methodology across the member's retail customer base and clearly document that methodology in written policies and procedures.

Allowing firms to choose between these options, but requiring firms to consistently apply whichever methodology they choose and clearly document that methodology in written policies and procedures, would constrain firms from adopting novel and complex methodologies on the fly that render their calculations meaningless, inaccurate, or deceptive. We urge FINRA to retain these requirements in its final rule, and we urge MSRB to adopt them as well, alongside its return to the original approach proposed. Failing to do so would create a huge loophole, enabling firms to evade their responsibility to provide meaningful, accurate, and consistent price reference calculations.

FINRA has also proposed to allow firms to elect whether to disclose the reference price for transactions in which there are material changes to the price of a security or to disclose instead the reference price together with a statement explaining such price change. Under the proposal, firms could elect not to disclose after documenting and demonstrating that a material change has occurred.

It is not clear how this exemption would work in practice, first, because it's not clear what standard a firm would need to meet to document and demonstrate that a material change has occurred, and second, because "material change" is not defined. The only guidance that is provided is that this provision could be used when there is a material change in the market price, due to, for example, a credit downgrade or breaking news regarding the obligor, and that this exemption is not intended to be used when the price of the security has changed due to normal price fluctuations or general market volatility. While a credit downgrade is a concrete occurrence that is not likely to occur with regularity, it is not clear what would qualify as breaking news. Given that we live in an era when constant Twitter updates can affect companies' and municipalities' securities prices, it could be too easy for firms to make a colorable argument, based on any breaking "news source," that a material change to a price has occurred, in which case the firm could avoid its disclosure obligations.

Instead of attempting to determine what standard a firm would need to meet to document and demonstrate that a material change has occurred and define what constitutes a "material change," we urge FINRA to require disclosure in all instances in which there is a material change to the price of a security. If firms wish to provide clarifying information with that disclosure explaining the material change in price, they are free to do so. Our suggested approach would address firms' stated concern that disclosing reference prices during volatile trading days might cause investors to be confused about the prices they see. Our suggested approach would also address another concern that firms have expressed previously, that providing disclosure in some cases but not in others would also lead to investor confusion.

FINRA and MSRB have also proposed to exclude from the proposed disclosure requirements trades that are conducted by a department or desk that is functionally separate from the retail-side desk. FINRA's description of this exemption states that, to qualify for the exemption, the firm must demonstrate through policies and procedures that the firm-side transaction was made by an institutional desk for an institutional customer that is separate from the retail desk and the retail customer. We strongly support this language, as it will help to ensure compliance. However, the policies and procedures language does not appear to be incorporated in the rule language. Considering similar policies and procedures language is incorporated in the rule text relating to firms' establishment of reasonable alternative methodologies, we think it would be helpful to eliminate this ambiguity by adding the policies and procedures language to the rule for the functionally separate desk exemption as well.

MSRB uses the same functionally separate language, but does not define what that means or require firms to demonstrate through policies and procedures that a non-retail desk is indeed functionally separate. We urge MSRB to add policies and procedures language that tracks the language FINRA uses in its description of the exemption. MSRB also has a requirement that the functionally separate principal trading desk through which the dealer purchase or sale was executed had no knowledge of the customer transaction. It's not clear how anyone could ever prove that a trading desk had no knowledge of the customer transaction, as it would require proving a negative and divining a desk and its traders' states of mind. We urge MSRB to eliminate this requirement. Replacing it with the policies and procedures language will better ensure firms' compliance and regulators' review of firms' compliance.

Conclusion

It is long overdue that firms provide essential cost disclosures to retail investors in fixed income markets. The fact that many firms currently don't provide that information and have so strongly opposed regulatory efforts to require providing it reflects their interest in preserving an opaque market that allows them to extract rents from their less well-informed retail customers.

FINRA's revised approach would fundamentally change this troubling dynamic by requiring firms to provide critical confirmation disclosures to their retail customers. It would result in retail investors' receiving more and better disclosure that would allow them to make better informed investment decisions, and it would foster increased price competition in fixed income markets. In contrast, it is not clear MSRB's revised approach would fundamentally change current market dynamics, as it would allow firms to easily evade their confirmation disclosure requirements. If firms do take advantage of loopholes in the MSRB rule to evade their obligations, retail investors will be no better off than they are currently. We urge MSRB to reconsider its approach and return to a rule that closely tracks FINRA's. And, for all the reasons explained above, under no circumstances should FINRA adopt an approach that tracks MSRB's reproposal.

Respectfully submitted,

Micah Hauptman

Micah Hauptman
Financial Services Counsel

THOMSON REUTERS

Via Electronic Delivery

December 11, 2015

Marcia E. Asquith
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Ronald W. Smith
Corporate Secretary
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Re: MSRB Regulatory Notice 2015-16: Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers; FINRA Regulatory Notice 15-36: Pricing Disclosure in the Fixed Income Markets

Dear Ms. Asquith and Mr. Smith:

Thomson Reuters appreciates the opportunity to comment on MSRB Regulatory Notice 2015-16 (the "MSRB re-proposal") and FINRA Regulatory Notice 15-36 (the "FINRA re-proposal').[1] Thomson Reuters[2] through our Financial & Risk business unit provides buy-side, sell-side and corporate customers with information, analytics, workflow, transaction and technology solutions and services that enable effective price discovery and support efficiency, liquidity and compliance. In particular, our wealth management offerings[3] include a complete suite of products that enable retail and institutional brokers to manage the daily tasks of their front, middle and back office operations. As a service provider, Thomson Reuters would like to offer an implementation perspective on the re-proposals.

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[1] Note the original proposals from the MSRB and FINRA are MSRB Regulatory Notice 2014-20 and FINRA Regulatory Notice 14-52.
[2] Thomson Reuters is the world's leading source of intelligent information for businesses and professionals. Combining industry expertise with innovative technology, it delivers critical information to leading decision makers in the financial and risk, legal, tax and accounting, intellectual property and science and media markets powered by the world's most trusted news organization. For more information about Thomson Reuters, please go to www.thomsonreuters.com.
[3] For more information on Thomson Reuters Wealth Management offerings, see here.

Align MSRB and FINRA Approaches to Mark-Up Confirm Disclosure

The FINRA re-proposal notes that both the MSRB and FINRA have discussed a coordinated approach to confirm disclosure rule-making. We believe it is imperative that the MSRB and FINRA agree on a single set of uniform rules regarding mark-up confirm disclosures. We have seen harmonization between MSRB and FINRA on other initiatives including the no-remuneration indicators set for implementation on May 23, 2016. We see no reason why coordinated rule-making as it relates to mark-up disclosure is not possible.

This approach has a number of benefits including rationalizing implementation effort, reducing investor confusion and rationalizing internal and external training. At many firms, developers and business analysts that program for MSRB reporting changes are the same resources as those responsible for TRACE-related changes. Common definitions and methodologies allow firms to develop a consistent set of modifications with respect to both reporting regimes in a timelier manner. Testing is also simplified if test scripts can be leveraged for both sets of changes. Investor confusion is reduced for those investors that trade both corporate and municipal bonds given that modifications will be consistent across asset classes. Finally, consistency simplifies the training and education that will be required for both internal staff and external clients.

We recommend alignment not only on the definition of the mark-up disclosure but also in the following areas:

- For all confirms, include a link to a search page on the TRACE or EMMA website, as applicable. Retail investors are accustomed to using search engines for financial research. Rather than a security-specific page as proposed by the MSRB, a link to an EMMA or TRACE search page, depending on the security type, which allows a user to input a CUSIP would quickly take retail investors to the data they require without requiring individualized hyperlinks on every confirm. Operationally, this is simpler to maintain for industry participants as well as for FINRA and the MSRB. Deep linking to a specific security increases the likelihood of errors and would require testing of every link to ensure it resolves to the correct webpage. Linking to a search page addresses these issues and is consistent with other retail investor information sites like FINRA's BrokerCheck. Any explanatory text placed on the confirm regarding this link should be concise, taking into account the limited space available on confirms.

- Include time of execution on retail customer confirms based on the time of execution reported to TRACE and EMMA for trade reporting today. This would allow retail investors to more easily identify relevant trade data on the EMMA and TRACE websites.

- Specify dollar amount as the disclosure format. This maintains consistency with equity confirms.

- Eliminate the requirement to "look through" to an affiliate. This is operationally challenging due to information barriers and system limitations. In many cases, affiliates operate as separate broker dealers with policies and procedures prohibiting sharing proprietary data outside of the firm.

Eliminate Look-Forward Component of Re-Proposals

Both the MSRB and FINRA re-proposals would require firms to not only look at preceding transactions within the 2-hour or same day window but also look forward to transactions occurring after a trade is executed in order to determine whether the trade requires a mark-up disclosure. The need to look forward to transactions occurring after the trade will disrupt confirmation processes currently in place. Delays could undermine efforts to maintain operational efficiency and achieve straight through processing. We recommend requiring firms to look back only to preceding transactions that took place in the current business day. By doing this, relevant mark-up prices and disclosure text can be added to the trade ticket and maintain current workflows. Without mark-up information on the trade ticket, we are concerned that an elaborate cancel/re-bill process will be required to accurately reflect the mark-up to be disclosed on confirms.

Exempt DVP/RVP Accounts That May Not Meet Institutional Account Definition

We applaud the MSRB and FINRA for establishing consistent definitions of retail accounts in scope to include those accounts outside of the institutional account definitions established in MSRB Rule G-8(a)(xi) or FINRA Rule 4512(c). However, we are aware that small institutions may not meet those defintions even though they trade via DVP/RVP accounts and rely on institutional confirm processes.[4] DVP/RVP account holders that do not meet the institutional account definitions are typically small investment managers and hedge funds with total assets under $50 million. We respectfully request that MSRB and FINRA exempt DVP/RVP accounts from the scope of this rule. We believe this is consistent with the intent of the re-proposals to focus on the retail segment of the market.

Consider Simplifying Definition of Mark-Up

In order to minimize implementation effort, we recommend simplifying the definition of the term mark-up to mean the differential between the customer price and the price of the inventory account trade. From an implementation perspective, disclosing the inventory account trade price would be the most feasible alternative and provide meaningful insight into broker-dealer compensation. Given that the inventory account trade price is on the trade ticket today, implementation would be limited to establishing mechanisms to add this information to the confirm. This would be a simpler approach as opposed to creating new fields and disclosure text that will be required under either re-proposal. Additionally, it would have no impact on real-time confirmation processing.

[4] Typically, firms use Omgeo's TradeSuite ID confirm process for meeting institutional confirm obligations.

Another benefit of this approach is its consistency with equity preferred confirms which currently provide mark-up disclosures based on inventory account trade price.

If a broader definition of mark-up based on either the FINRA or MSRB re-proposals is required to achieve policy goals, we have identified the following additional issues with both the FINRA reference price and the MSRB prevailing price concepts that we believe must be considered and resolved.

FINRA Reference Price

FINRA's re-proposal has a number of operational challenges based on the complex requirements of the re-proposal including the following:

- The need to address complex scenarios[5] and determine reasonable alternative methodologies. While the FINRA re-proposal offers firms flexibility, the implementation effort required to ensure that permissible methodologies are employed will be a challenge for development and testing.

- The need to evaluate a reference price to determine if a material change in the price of the security warrants excluding the reference price from the confirm or requiring additional disclosures. Firms will need to develop logic to review reference prices for their validity and establish parameters to determine if a material change occured. Guidance would be required to ensure the determination of material change is consistent across the industry.

- The lack of consistency in the determination of the reference price or its inclusion on the confirm will make programming difficult given the number of exceptions and degree of subjectivity involved in making determinations.

- The requirement to add new fields and disclosure text. This is further complicated by the multiple workflows that exist within the fixed income marketplace. Firms use of internal or third party order management systems, trading systems, alternative trading systems (ATSs), back office service providers and confirm vendors will create a number of integration touch points where mark-up data will need to be stored and passed.

MSRB Prevailing Price

While firms are required to determine prevailing market price today, this information is not currently systematized to allow for the population and communication of fields to downstream systems. Similar to the FINRA re-proposal, systematizing this information will mean the creation of new fields and associated integration work.

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[5] Complex scenarios include those where there is not a same (or greater) size principal and customer trade or there are one or more intervening principal trades of a different size,

The methodology for determining prevailing market price may differ as described in FINRA Rule 2121 and MSRB G-30 as well as associated Supplementary Materials in both rules. For illiquid securities especially, methodologies other than contemporaneous price will need to be considered, e.g., comparison to similar securities based on yield benchmarking. As noted in FINRA Regulatory Notice 15-46 which provides guidance on best execution obligations for fixed income and other markets: *"FINRA also notes that prices of a fixed income security displayed on an electronic trading platform may not be the presumptive best price of that security for best execution purposes, especially for securities that are illiquid or trade infrequently."* Without an independent source of the prevailing market price, firms will face difficulties in providing this information in a manner that is consistent across the industry. FINRA and the MSRB must address this issue in order for the prevailing market price to be meaningful to investors.

Perform Cost/Benefit Analysis

Given the complexities of the re-proposals outlined above, we recommend performing a detailed cost/benefit analysis of the proposals that are ultimately submitted to the SEC. We note that both the MSRB and FINRA have committed to performing cost/benefit analyses. FINRA indicates that a more fulsome impact analysis is suitable for "significant new rule proposals.[6]" Additionally, the MSRB states that, "The economic analysis drafted for the SEC rule filing should capture the analysis provided in the request for comment but should be more complete as it should also capture relevant information and arguments made during the public comment period and take into account any alterations to the proposed rule made during the rulemaking process.[7]" Firms spend signifcant resources today to maintain and enhance trade reporting. Opportunities to leverage the EMMA and TRACE web portals should be explored as part of this analysis.

As part of the cost/benefit analysis, we believe that policy goals should be clarified in terms of the intent associated with the scope of mark-up disclosures. If expansion of mark-up disclosures to more retail transactions is the ultimate goal, it may be possible to reduce programming costs associated with determining in-scope trades by expanding scope at the outset to eliminate a phased approach to mark-up disclosures. If policy goals will ultimately require an expansion of scope, the costs associated with multiple phases of the project should be evaluated and mitigated. It should be noted that while expanding scope to all retail transactions may address investor confusion and complaints associated with having the mark-up disclosure on only some confirms, determination of the mark-up may be more difficult.

[6] Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking, September 2013

[7] Policy on the Use of Economic Analysis in MSRB Rulemaking at http://www.msrb.org/Rules-and-Interpretations/Economic-Analysis-Policy.aspx

Provide Sufficient Implementation Time

We expect that determination of the reference price or prevailing market price will be performed within OMS/trading systems. However, new fields for the mark-up disclosure and any required disclosure text will need to be passed to back office systems on trade tickets and then on to confirm systems. There are a number of implementation activities that need to be considered across the workflow including precise definition of what price will be disclosed, establishment of new fields to be populated and passed, determination of disclosure text. It will be important for the MSRB and FINRA to work with the industry in establishing a common implementation methodology and industry standards, where possible. We believe that there will be a need for additional implementation guidance from both MSRB and FINRA if rules are ultimately approved.

Once a common approach is proposed by the MSRB and FINRA, we will be better positioned to provide more feedback on implementation issues and timeframe. It is worth noting that recent MSRB trade reporting changes have afforded market participants with twelve month implementation time periods.[8] Changes to confirm processing typically are more complex given the number of integration touch points.

Thank you for the opportunity to comment on the re-proposals. Changes to confirms directly impact our systems and those of our clients; we appreciate the willingness of MSRB and FINRA to consider our comments.

Regards,

Manisha Kimmel

Manisha Kimmel
Chief Regulatory Officer, Wealth Management
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[8] See MSRB Regulatory Notice 2015-07 published May 26, 2015 announcing a May 23, 2016 implementation date.

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December 11, 2015

Via e-mail: ***pubcom@finra.org***
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RE: FINRA Regulatory Notice 15-36: Pricing Disclosure in the Fixed Income Markets; MSRB Regulatory Notice 2015-16: Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith & Mr. Smith:

Wells Fargo Advisors, LLC ("WFA") appreciates the opportunity to comment on the Financial Industry Regulatory Authority's ("FINRA") Proposed Rule Requiring Confirmation Disclosure of Pricing Information in Corporate and Agency Debt Securities Transactions and the Municipal Securities Rulemaking Board's ("MSRB") Proposed Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers (together, the "Proposal" or "Revised Proposal").[1]

WFA is a dually registered broker-dealer and investment advisor that administers approximately $1.4 trillion in client assets. We employ approximately 14,988 full-service financial advisors in branch offices in all 50 states and 3,838 licensed financial specialists in retail bank branches across the country.[2] WFA and its affiliates help millions of customers of varying means and investment needs obtain the advice and guidance they need to achieve financial goals. Furthermore, WFA offers access to a full range of investment products and services that retail investors need to pursue these goals.

I. EXECUTIVE SUMMARY

WFA supports FINRA's and MSRB's objective of improving price transparency in the fixed income markets and applauds the efforts to enhance access to meaningful pricing information for retail investors. As a broker-dealer vested with the responsibility of seeking best execution on transactions for over 7.5 million customer accounts, we support regulatory initiatives to provide clear and useful information to retail investors regarding transactions in the fixed income markets. We also thank both FINRA and MSRB for seeking out and incorporating comments pertaining to their original disclosure proposals. However, the core concerns expressed in WFA's response to FINRA and MSRB's original proposals remain unresolved, particularly our concern regarding the client utility and potential misunderstanding of the disclosure information.[3]

We continue to believe retail investors are best served by continuing to focus on providing meaningful information about prevailing market conditions, ideally via real-time price dissemination tools. Consequently, we believe there should be greater focus on the use of the Trade Reporting and Compliance Engine ("TRACE") and the Electronic Municipal Market Access ("EMMA") price dissemination platforms which provide additional near real-time pre-trade market information to retail investors. We are supportive of including a

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[1] FINRA Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets – FINRA Requests Comment on a Revised Proposal Requiring Confirmation Disclosure of Pricing Information in Corporate and Agency Debt Securities Transactions, October 12, 2015, *available at*: http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-15-36.pdf. MSRB Regulatory Notice 2015-016 - Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers, September 24, 2015, *available at:* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2015-16.ashx?la=en.

[2] WFA is a non-bank affiliate of Wells Fargo & Company ("Wells Fargo"), a diversified financial services company providing banking, insurance, investments, mortgage, and consumer and commercial finance across the United States of America and internationally. Wells Fargo's retail brokerage affiliates also include Wells Fargo Advisors Financial Network LLC ("WFAFN") and First Clearing LLC, which provides clearing services to 78 correspondent clients, WFA and WFAFN. For the ease of discussion, this letter will use WFA to refer to all of those brokerage operations.

[3] See Correspondence from Robert J. McCarthy to Ronald W. Smith and Marcia E. Asquith, dated January 20, 2014, *available at:* http://www.finra.org/sites/default/files/notice_comment_file_ref/Wells%20Fargo.pdf.

hyperlink to these platforms and enhancing educational efforts for retail investors to better understand the information presented. Moreover, we believe a proposal that mandates the disclosure of the mark-up in riskless principal transactions in conformity with the recommendations set forth in the SEC's 2012 Report on the Municipal Securities Market[4] would provide meaningful information to clients in connection with their transactions. We are concerned that disclosures on other trades will not be subject to uniform processes across the industry and may lead to customer confusion, particularly where market movements or material events (e.g. credit rating change) may occur between the time of the reference trade and the customer transaction. Finally, FINRA and MSRB should align their prescribed approaches so that one method of disclosure results for all fixed income transactions. There is no compelling case for differential regulatory requirements.

II. BACKGROUND

In November 2014, both FINRA and MSRB issued Regulatory Notices[5] (together, the "Initial Proposal") seeking comment on the respective proposals to require firms to disclose additional pricing information for retail-size customer trades in corporate and agency debt securities. Specifically, the Initial Proposal required that, if a firm sells to a customer as principal and on the same day buys the same security as principal from another party, the firm would have to disclose on the customer confirmation (i) the price to the customer; (ii) the price to the firm of the same-day trade (reference price); and (iii) the difference between those two prices.

Over thirty comment letters were received in response to the Initial Proposal. Many of the commenters expressed concern that the specific information proposed to be included on the customer confirmations could be misinterpreted by retail clients. Further, industry members raised significant technical and operational hurdles that would impede member firms from complying fully with the proposal. Finally, commenters advised that the Initial Proposal undermined previous and current efforts to provide greater price transparency through the continued development of TRACE and EMMA price dissemination platforms to provide additional near real-time pre-trade market information to investors.

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[4] Securities and Exchange Commission Report on the Municipal Securities Market (July 31, 2012), *available at*: http://www.sec.gov/news/studies/2012/munireport073112.pdf.

[5] Regulatory Notice 14-52, Pricing Disclosure in the Fixed Income Markets – FINRA Requests Comment on a Proposed Rule Requiring Confirmation Disclosure of Pricing Information in Fixed Income Securities Transactions, November 17, 2014, *available at*: http://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_14-52.pdf; MSRB Notice 2014-20 - Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations, November 17, 2014, *available at:* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-20.ashx?n=1.

III. DISCUSSION

WFA supports FINRA's and MSRB's objective of improving price transparency in the fixed income markets and applauds efforts to enhance access to meaningful pricing information for retail investors. Unfortunately, we believe the revised proposals from FINRA and MSRB miss the mark in addressing many of the concerns expressed on the Initial Proposal. We offer the following discussion to highlight the inherent problems with the Revised Proposal and respectfully offer suggestions for a more workable, consistent and meaningful approach.

A. FINRA and MSRB Should Propose a More Coordinated Approach.

Under the Revised Proposal, FINRA and MSRB have offered very different approaches. Each proposal has specified a different time frame under which the required fixed income pricing disclosure is to be computed.

MSRB's revised proposal would require the dealer to disclose the mark-up on retail customer confirmations for principal transactions when they transact on the same side of the market as the customer in the customer's municipal security in one or more transactions that in the aggregate meet or exceed the size of the customer's transaction. Disclosure would be required only where the dealer's same-side of the market transaction occurs *within two hours* preceding or following the customer transaction.

FINRA's revised proposal provides that, for non-complex scenarios (firm principal transaction of the same or greater size without intervening principal trades within the same trading day), the price of the principal trade should be used as the reference price. For complex scenarios (no same or greater size principal and customer trade), firms may employ a reasonable alternative methodology, such as average weighted price of the firm trades that equal or exceed the size of the customer trade, or the price of the last same-day trade executed as principal by the firm prior to the customer trade. The firm must adequately document and consistently apply its chosen methodology.

WFA requests that FINRA and MSRB align their revised proposals. We believe compliance with the two conflicting sets of standards is virtually impossible. Consequently, varying proposals would make it extremely difficult to develop disclosure solutions.

B. The Proposed Confirmation Disclosure Requirements Are Difficult, If Not Impossible, To Effectively Implement.

The process for creating a customer confirmation is currently a complicated activity which relies on inputs from multiple systems to generate a transaction confirmation that complies with existing regulatory requirements. These inputs include, but are not limited to, trade files, security master files and customer files. Additional data points include accrued interest, price and yield information and total funds. The information needed to produce a confirmation is captured at the time of transaction execution, thus permitting firm systems to efficiently process the necessary information for inclusion on a transaction confirmation.

As outlined in the Revised Proposal, in certain circumstances, firms would be required to gather a portion of the trade data for the customer confirmation hours after the customer trade was executed. Firms would have to undo real-time trade processing, currently used industry-wide, and create a system whereby an alternative methodology may need to be employed to properly calculate the reference price required for the customer confirmation. Specifically, compliance with the Revised Proposals would require technological architecture that does not currently exist in the industry. For example, the additional trade data sought by the Revised Proposal may not currently be retained; thus system enhancements would be necessary to comply with the proposed retention and transmission requirements.

Furthermore, the revised proposed requirements undermine industry efforts to move towards real-time processing as well as making real-time access to trade data available. Today, customers are able to view their trades on-line, should they so choose. Customers have also been encouraged to access EMMA and TRACE to view market and trade data real-time and/or post trade. The proposed requirements seem to deemphasize use of these beneficial industry advances by urging investors to rely on “recreated” data in a paper confirmation to be delivered post-trade, as opposed to more dynamic information in real-time.

C. <u>FINRA and MSRB Should Revive Mark-up Disclosure for Riskless Principal Transactions As A Workable Alterative.</u>

Most importantly, WFA does not believe the confirmation disclosure in the Revised Proposal furthers an understanding by retail investors of prevailing market conditions at the time of transaction execution. Under the Revised Proposal, in many instances a customer may believe the information on the reference trade reflects the prevailing market price at the time of their transaction. However, this may be misleading or inaccurate in instances where there are intervening market movements or significant events. For example, the downgrade in the rating of a particular bond or the occurrence of a catastrophic event may adversely impact the price of a security. This can result in the customer being confused as to whether the difference between the identified price differential is due to mark-up, mark-down or other factors.

WFA also believes that a mark-up disclosure for riskless principal transactions would provide investors with information that is not impeded by various outside market factors and would sustain the current confirmation generation process, as broker-dealers already have the necessary information at the time of trade to initiate the process.

D. <u>FINRA Must Exempt Institutional Customers From the Revised Proposal.</u>

The Revised Proposal states that the customer confirmation disclosure requirements are applicable to non-institutional customers. A non-institutional customer is defined as a customer account that is not an institutional account. For purposes of clarity, WFA requests that the Revised Proposal be updated to affirmatively exempt both institutional accounts and DVP/RVP institutional accounts[6] from the customer confirmation disclosure requirements of FINRA Rule 2232.

E. <u>The Proposal Undermines Prior/Current Efforts To Provide Greater Price Transparency For Retail Investors (TRACE And EMMA).</u>

For over twenty years, the SEC, FINRA and MSRB have favored development of price dissemination platforms as a more effective alternative to confirmation disclosure. WFA strongly feels that the data currently available, both pre-trade and post-trade, through TRACE and EMMA is far more effective in putting real-time information in the hands of investors than relaying information to customers that may be confusing if not misleading, in a confirmation roughly three days after the trade.

WFA believes the Revised Proposal undermines the use of price dissemination platforms by the introduction of confirmation disclosure that has repeatedly been deemed an inferior alternative. Therefore, investors will be better served by expanding access to price dissemination platforms that provide better insight, in a near real-time manner, into prevailing market conditions.

F. <u>There Should Be Clear Cost/Benefit Analysis Of The Proposed Disclosure Requirements and Substantial Time To Allow For Implementation.</u>

Neither FINRA nor MSRB have provided any statistical information or studies which indicate that retail investors lack sufficient information or are unable to obtain relevant pricing information prior to or after trading in fixed income products. WFA requests that prior to issuing such potentially burdensome regulations on the industry, both FINRA and MSRB undertake objective studies which illustrate that disclosure on a customer confirmation is preferential to the near real-time price dissemination currently available to retail customers. Further, due to the substantial systemic requirements within the Revised Proposal, WFA also requests a minimum three year implementation period.

IV. CONCLUSION

WFA believes investors are best served by the industry continuing to focus on providing meaningful information about contemporaneous market conditions via more advanced near real-time price dissemination tools. Consequently, WFA respectfully recommends the Proposal be withdrawn or in the alternative, significantly altered as described above.

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[6] Delivery Versus Payment (DVP) and Receive Versus Payment (RVP) accounts do not meet the “institutional account” definition, but rely on the institutional confirmation process.

WFA appreciates the opportunity to respond to FINRA and MSRB's Proposal. Although WFA believes the Proposal as currently structured should be withdrawn, we remain willing to assist FINRA and MSRB in achieving greater price transparency for retail investors. WFA welcomes additional opportunities to respond as this Revised Proposal evolves. If you would like to further discuss this issue, please contact me at (314) 242-3193 or robert.j.mccarthy@wellsfargoadvisors.com.

Sincerely,

Robert J. McCarthy
Director of Regulatory Policy

Ms. Asquith:

Thank you for the opportunity to comment on proposed required confirmation disclosures contained in Notice 15-36. The new proposal is a substantial improvement over that originally published in Notice 14-52. The removal of the size requirement, exempting most new issues and requiring a TRACE link all improved the functionality of the proposal. However, in order to limit a potential unintended consequence of the proposal, FINRA should adopt the MSRB time threshold of two hours.

The proposed required confirmation disclosures are part of a concerted effort on the part of regulators to improve the market efficiency obtained by retail investors. It is believed that by requiring a dealer to disclose “mark-up” or whatever one chooses to call the profit the dealer makes on the transaction and by referencing the source of available pricing data, a retail purchaser will be more likely to act rationally and choose to trade with dealers who work for less spread. (Disregard for the moment the reality that many clients by bonds on yield, not price.) The problem is that many retail clients trade with only one broker and will follow the instructions of that broker, particularly when it comes to fixed income product. These clients are also the ones most likely to disregard the “mark-up” information. Furthermore, there will be broker dealers that simply refuse to sell fixed income inventory to retail clients until the required mark-up disclosure period has ended, thus preventing retail access to the most advantageously priced offerings. This is most likely to occur in very large firms with complex business models and where retail clients are less likely to analyze competing bond offerings. Consequently, it would be most advantageous to retail investors if the disclosure period were shortened, otherwise almost every offering many clients see will be stale. Additionally, this would reduce the anti-competitive aspect of the proposal.

Ideally, it would be understood that clients buy bonds based upon yield and the profit earned by the dealer should be irrelevant. Unfortunately, many bond investors are not selecting bonds based upon an analysis of what is available in the market and it is understandable that regulators would want to provide these investors with additional protection. FINRA will best accomplish its goal by adopting the two hour period chosen by the MSRB.

Thank you again for the opportunity to comment.

Chris Melton
Executive Vice President
Coastal Securities

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December 11, 2015

Submitted Electronically

Marcia E. Asquith
Senior Vice President and Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: **FINRA Regulatory Notice 15-36: FINRA Requests Comment on a Revised Proposed Rule Requiring Confirmation Disclosure of Pricing Information in Corporate and Agency Debt Securities Transactions**

MSRB Regulatory Notice 2015-16: Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith and Mr. Smith:

On behalf of the Bond Dealers of America ("BDA"), I am pleased to submit this letter in response to Financial Industry Regulatory Authority ("FINRA") Regulatory Notice 15-36 and Municipal Securities Rulemaking Board Regulatory Notice 2015-16 (the "Notices"), requesting comment on proposed rules to require the disclosure of market or pricing reference information on retail-trade confirmations for municipal, corporate, and Agency fixed-income securities. BDA is the only DC based group representing middle-market securities dealers and banks focused on the United States fixed-income markets and we welcome this opportunity to present our comments on the Notices.

BDA believes that increasing transparency by providing an additional pricing disclosure to retail investors could be beneficial to the marketplace if it can be done at reasonable cost to dealers by utilizing and leveraging the transaction information that regulators are required to receive after each transaction. Additionally, to be valuable, the rule must be understood by retail investors. BDA strongly urges regulators to pursue a harmonized rule that represents the least cost, least complex, and most understandable disclosure method. BDA believes neither the MSRB nor FINRA have put forth a proposed rule that fulfills those criteria or enables retail investors to compare their trading costs to other retail investors in the market. Also, BDA does not believe that estimating the regulatory cost impact of this rule is even possible at this point.

BDA's Markup Disclosure Recommendations

- Methodology: BDA recommends that FINRA and MSRB work with dealers to develop a lower-cost solution that leverages the transaction data that is centrally reported to TRACE and EMMA. This would allow for retail confirmations to include a price comparison to the average inter-dealer daily trade price.

- Scope: The disclosure should be required for retail trades where the dealer has entered into a same-day principal transaction on the same side as the retail investor and the quantity of the dealer principal trade is the same size or greater than the retail trade.

- Timeframe: The disclosure should be based on the full trading day basis outlined in FINRA's notice in order to minimize technology costs and operational complexity associated with a shorter time period.

- Disclosure Format: The disclosure should be displayed in dollar terms or as a percentage of the markup relative to the inter-dealer price.

- Harmonize: BDA strongly urges regulators to publish a fully harmonized rule. BDA members have spent an enormous amount of time and resources reacting to and researching solutions to the 2014 proposed rules and the current proposals.

- Reduce Complexity: Broker-dealers urge regulators, as part of a coordinated rulemaking process, to focus on proposing the least complex, least-cost methodology that best achieves the stated goals of the regulation.

BDA still believes these rules are based on a fundamental misconception of market risk. Dealers have multiple bond positions in inventory. Some bonds are held for a day or less and others are held for several days or weeks because investor demand does not materialize to the extent that the dealer expected due to basic market dynamics. Unless there is an existing contra side order, a dealer is at risk when it purchases a security. Therefore, BDA would prefer that regulators publish a truly "riskless principal" rule for fixed income, similar to SEC Rule 10b-b, that applies to equity transactions, where dealer cost basis is disclosed and the trade is truly "riskless."

BDA appreciates the improvements that regulators have made to the proposals.

BDA appreciates the improvements that regulators have made to the confirmation disclosure proposals compared to the 2014 proposals.

Retail Focus

The Notices are now explicitly focused on retail customers. This was a significant concern for BDA members that routinely transact with institutional customers in trade sizes that would have been considered 'retail size' by the previously proposed rules. A retail-account-focused rule proposal is superior. Although, there are some concerns with the potential application of this rule to smaller institutions that are below the quantitative thresholds.

Secondary Market Trades

Additionally, BDA believes that the Notices are improved by the exclusion on new issue transactions at the "list-offering price" from the scope of the rule proposals. As MSRB's Notice notes, in these instances, the offering documents contain ample information, including the public offering price and underwriter compensation.

Link to Trading Data Pages

BDA believes leveraging the data reported to TRACE and EMMA and increasing awareness of the comprehensive pricing information available on these sites is important. The proposals do seem to differ on where on the website the investor would be directed to. BDA believes a general link to the main page of EMMA and TRACE would be operationally easier to achieve than directing investors to a security specific page.

BDA believes the proposals are too complex.

Specifically, the Notices outline two different methodologies for computing the retail confirmation disclosure and for the format of the disclosure. The MSRB proposes to require a retail confirmation disclosure of a markup relative to the prevailing inter-dealer price at the time of the retail trade. Alternatively, FINRA has proposed a requirement for a confirmation disclosure based on the differential between a retail transaction price and a dealer's same day principal trade in the same security. BDA observes some unique challenges with each of the complex proposed methodologies.

FINRA's complex methodology would require dealers, of all sizes, to implement a technologically intensive and expensive solution that would require significant new operational and trading systems to be put in place, including working with third-party service providers and vendors to create new and expensive solutions to accurately capture two associated trades executed on the same day and then transfer the differential onto a customer confirm. The complexity with MSRB's alternative proposal is based on the possible ambiguity of identifying contemporaneous cost with enough certainty to put the information on a customer confirmation. The common problem with the proposals is that they require dealers to create new systems, processes, and procedures to capture transaction data that is held already held and publicly disseminated by regulatory agencies.

In light of the unprecedented volume of new regulations impacting dealers in recent years, BDA believes that an overly complex, technologically intensive regulation must be avoided. Broker-dealers are required under FINRA and MSRB rules to abide by the highest standards of commercial honor. FINRA Rule 5310 and MSRB Rule G-18 require dealers to execute customer trades at prices that are “as favorable as possible under prevailing market conditions.” In addition, transactions must be executed for fair prices and commissions under FINRA Rule 2121 and MSRB Rule G-30.

In the past decade, mark ups in the fixed-income markets have been consistently narrowing. As FINRA notes in its proposal, the median mark up for a “retail-size” investment grade corporate bond transaction is 51 basis points. In 2012, the Securities and Exchange Commission’s reported that the average corporate bond mark up in 1999-2000 was 124 basis points. By contrast, according to the Investment Company Institute, the average annual bond fund expense fee was 70 basis points and the average front-load was 70 basis points in 2014.[1]

The premise of this regulation is to ensure that, despite all of the existing rules and the associated enforcement of those rules all of which ensure quality execution and the public reporting of every trade to EMMA and TRACE that retail investors could derive additional benefits if they better understood dealer transaction-based compensation. BDA does not disagree with that notion, but BDA does disagree with the solution that regulators have proposed because it requires dealers to devote massive amounts of resources to comply when a simpler, less costly alternative exists.

BDA believes the FINRA proposal is too complex and will be too costly.

FINRA’s reference price approach is problematic primarily because it is too complex and will be too costly from a technology, compliance, and operational standpoint. As BDA discussed in its 2014 comment letter, redesigning dealer systems to capture a reference price is operationally intensive and will require a full system re-build for many dealers. This will be a significant cost burden, especially for smaller dealers that have fewer compliance personnel and less revenue to divert from core operations to fund growing technology and compliance budgets.

The reference price solution is more complex and this fact reduces the value of the disclosure to retail investors. The proposed “alternative methodology” for complex trades is a particular element that BDA views as far too complex. Retail investors may not understand the reference price disclosure in its simplest form. BDA believes that the disclosure will be significantly less well understood if differing methodologies are allowed for “complex” trades. These types of exceptions, including the exception for

[1] Investment Company Institute Fact Book 2014: http://www.icifactbook.org/fb_ch5.html#fees

‘material change provision’, will conceivably allow for different retail confirmation disclosures for the same exact trades depending on the judgment and chosen procedure of different dealers all executing different, but similar, trades and what principal transactions that dealer has entered into during the trading day. This design means that retail investors across the marketplace will receive inconsistently computed confirmations, thus reducing the value, clarity, and comparability of the disclosure to transactions in the marketplace generally.

Furthermore, BDA does not believe that a reference price disclosure will give retail investors a valuable indicator with which they will be able to understand transaction costs and dealer compensation in the market. Dealers enter into principal trades at various prices and quantities throughout the trading day. Therefore, the reference is not going to consistently be a valuable indicator for transaction costs in comparison to other investors in the marketplace transacting at the same time in the same security. In fact, it will be a confusing indicator because, unlike the inter-dealer prevailing price, it is a reference to where the market was and not what the current market price is or what the inter-dealer price is at the time of the retail investor trade.

For example, as BDA stated in its previous comment letter, a dealer may purchase bonds at 99 in a principal capacity and then enter into a sale, possibly hours after the initial transaction, at a 102 in full compliance with the dealer’s best execution responsibilities. At that point, another dealer could be executing comparable retail sales at 102.5 or 103 with a cost-basis (for disclosure purposes) of 101. BDA notes that the disclosure—by definition—is based on where the market was rather than on the actual market conditions at the time of the executed trade. This creates the opportunity for a highly misleading disclosure. In this instance, the dealer that filled the customer order at the superior market price will be required to disclose a larger markup than the dealer that filled the customer order at the inferior price. The potential impact on the market, especially the impact on liquidity, that could be caused by providing this misleading information to investors is currently unknown and should be studied fully for the benefit of investors and the marketplace.

The premise for the proposed regulation is to allow retail investors to have greater information about transaction costs and to allow retail investors to approach their broker informed with greater information about their transaction costs. BDA does not believe the dealer-reference price approach is the optimal method for providing the information to retail customers to inform that discussion.

BDA believes the MSRB’s methodology introduces significant new risks due to its ambiguity.

Of the proposed disclosure methodologies, BDA believes the central element of MSRB’s methodology, which proposes a mark up disclosure relative to the prevailing inter-dealer price at the time of the retail trade, is a step in the right direction because it attempts to limit technology and operational costs. The inter-dealer price would be used to compute the required markup disclosure, in dollar terms and as a percentage, which would be displayed on retail confirmations.

BDA believes that the biggest uncertainty created by the MSRB's methodology would be with reliably and consistently ascertaining inter-dealer cost for computing and reporting the confirmation disclosure. MSRB's proposal contemplates a marketplace where inter-dealer price is readily observable and universally agreed upon. However, in certain instances, there may be a tightly distributed range of views amongst dealers for what inter-dealer cost is at a given point in time. This introduces the risk that an examiner could disagree with one trader's specific determination of the prevailing inter-dealer market price, which could lead to violations of MSRB and FINRA rules regarding accuracy of customer confirmations. This is a very serious concern with the MSRB approach.

BDA believes these risks could potentially be reduced, to a certain extent, through guidance. Specifically, dealers would benefit from guidance outlining what due diligence process and procedures would be required related to the documentation of the inter-dealer cost and how would those procedures fit within the existing due diligence and documentation requirements related to the best execution rules. Best execution rules allow for a range of acceptable trade prices to be considered if a thorough process for ascertaining market price is employed. BDA is concerned that differing views about prevailing market prices could give rise to serious and unnecessary violations of rules related to confirmation accuracy. Therefore, it would be useful to provide guidance that describes hypothetical transactions, in addition to what types of processes and documentation would be required.

If the premise of these rules is to foster greater understanding of dealer compensation and allow retail customers to understand execution quality versus other retail customers, the MSRB proposal may allow for that to take place with less complexity, and in a less costly way, than the FINRA proposal. BDA believes that the MSRB methodology would provide a more consistent and meaningful disclosure because retail investors would have the same reference element, the prevailing market price, and the disclosure would be more consistent for similar retail transactions executed at roughly the same time.

BDA strongly urges regulators to harmonize their rules.

Currently, the Notices outline two vastly different proposed rules. The worst possible outcome for dealers, especially smaller dealers, is two distinctly different final rules. Two different rules would mean a doubling of implementation and technology-cost burdens and would create a massive and unnecessary compliance burden for dealers on an ongoing basis. BDA understands that it is the intent of regulators to harmonize the proposals to the greatest degree possible. However, BDA wants to stress that a harmonized rule is absolutely essential, especially for smaller dealers who are already struggling with vastly higher compliance and technology costs as a result of new regulations.

FINRA's proposal notes that 70% of transactions in corporate credit are concentrated amongst 20 dealers. In light of the ongoing trend towards greater dealer consolidation, doubling the regulatory cost impact on dealers, especially smaller dealers, would likely accelerate the consolidation trend. Supporting greater consolidation of trading amongst the largest dealers at the expense of smaller dealers would be a perverse outcome for a rulemaking designed to allow retail investors to benefit from increased competition amongst dealers.

In addition to harmonization, BDA urges regulators to recognize that this is a significant rulemaking that will have a large impact on how dealers operate, from a trading, operations, and technology standpoint. Each time a proposal is put forth, dealers are required to assess the proposal as if it were a final rule. Dealers have to interact with operational, compliance, legal, trading, internal technology staff, and third-party vendors to assess the extent and cost of the potential systems upgrades, including the development costs of third-party vendor solutions. This is expensive and time consuming for firms with limited resources and limited staff. It is important for regulators to engage dealers and enter into robust discussions about the systems and technology impact and costs associated with this proposal in order for regulators to begin to understand the complexity and costs associated with the proposals. BDA previously recommended a feasibility study so that regulators could fully contemplate the costs associated with this proposal. BDA is disappointed that that study did not take place prior to these new proposals being published for comment.

BDA urges regulators to pursue the least complex, least-cost method by leveraging TRACE and EMMA data.

If regulators are determined to require a confirmation disclosure on a population of trades that is larger than purely "riskless principal" transactions, BDA recommends regulators develop a harmonized proposal based on the least complex, lowest cost proposal by using the centralized data that is already reported to TRACE and EMMA.

BDA recommends that regulators leverage the transaction data that they already hold to provide the type of retail confirmation disclosure the proposals are designed to create. Both the MSRB and FINRA have all the transaction data supplied to them throughout the trading day and are engaged in constant public price dissemination throughout the trading day. At a much lower cost to broker-dealers, and with much greater clarity, than the systems outlined in the Notices, FINRA and MSRB could compute the daily average inter-dealer price and require customer confirmations to include the differential (in dollar terms and as a mark up percentage) between the daily average inter-dealer cost price and the retail investor's transaction price. This would allow customers to better understand dealer compensation and would provide sufficient information for a customer to contact their dealer to discuss the execution of their trades.

Additionally, BDA would also like to note that, especially in the municipal securities market, the difference between a retail customer's cost and the inter-dealer contemporaneous cost, the dealer's reference price, and the average daily inter-dealer cost would, in most cases, be minimal.

This method represents a more efficient way of delivering a confirmation disclosure. BDA is ready to work with regulators to improve the proposals and to discuss alternatives that would be less costly and deliver pricing information that would allow retail investors to be more informed about the marketplace.

Thank you again for the opportunity to submit these comments.

Sincerely,

Michael Nicholas
Chief Executive Officer

December 11, 2015

BY ELECTRONIC MAIL

Marcia E. Asquith
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Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314-3412

Re: FINRA Regulatory Notice 15-36
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2015-16
Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers

Dear Ms. Asquith and Mr. Smith:

RW Smith & Associates, LLC strongly supports transparency efforts within the bond markets. In regard to these proposed rules, however, we continue to be concerned that they will not provide retail customers, the intended beneficiaries of transparency, with clear or useful information. To the contrary, especially with the FINRA proposal, we believe the rule as proposed would lead to widespread confusion, specifically within the retail market.

As we have stated in meetings time and again with both regulatory agencies, we remain extremely concerned that two peer organizations, FINRA and the MSRB, that have consistently expressed a desire to align their rule-making continue to issue such disparate proposals. The actions of both organizations have led members to reasonably conclude that neither regulator, nor their boards, is willing to concede their position on their proposal. This continues to trouble members because in the end neither FINRA nor the MSRB has the ability to force the other to capitulate, and the result from a regulatory stalemate between intractable counterparties would be operationally and financially disastrous for member firms.

RW Smith, along with every other member firm we spoke to in regard to these proposals, would like to once again encourage both FINRA and the MSRB to reconsider their proposals, and as a reasonable alternative turn their attention back to TRACE and EMMA. The industry has funded the creation and maintenance of both of these technology platforms to the tune of over $130 million and it is our position that the focus of both the regulators and the industry should now be on increasing visibility, familiarity and usage of the investor tools and market data available on TRACE and EMMA. There are a multitude of approaches to achieve the objective, such as implementing hyperlinks on electronic confirmations, and member firms are ready and willing to work with the regulators to move this approach forward.

We understand from some of the FINRA board members that there is a firmly-held belief that retail customers will benefit from the production of a “reference price” provided on their trade confirmations. While we applaud and are in alignment with the intention of the board, we would strongly encourage them to listen to members and member firms who have been in the retail market for decades, and speak from vast and deep experience. It is widely held by market participants that the construct of a reference price that can and will change from one firm and one confirmation to another on the same CUSIP number will without a doubt be confusing and, in the end, meaningless to retail customers. If so many of us who are in the business hold this as an absolute, why does our well-informed and well-intentioned feedback continue to fall on deaf ears at FINRA? As an alternative, we would suggest providing retail customers with a link to EMMA and/or TRACE so they could view date-specific or current market pricing. If the objective is to get market pricing information into retail customer hands, then let's do exactly that by connecting them into the very robust platforms of EMMA and TRACE. A "reference price" is meaningless to retail and we strongly oppose the adoption of any version of this proposal.

If, in the end, some version of either of these proposals move forward, it is imperative that both FINRA and the MSRB adopt a uniform rule. In no scenario should two differing rules be passed and implemented. Working in concert, determine the objective: is it transparency of pricing or markup disclosure or both? If it is transparency of pricing then move forward with a proposal regarding links to EMMA and/or TRACE, and if it is markup disclosure then go with riskless principal transactions only. The SEC has long held that "riskless principal" transactions are the economic equivalent of "as agent" transactions and, as we all know, member firms are required to disclose transactional commissions on customer confirmations of As Agent trades. We suggest that FINRA and the MSRB use the same approach to riskless principal transactions; there is no need to reinvent the wheel, just use the agency methodology as your baseline.

A brief comment on the subject of "gaming the system", FINRA has expressed a concern that the 2-hour window proposed by the MSRB would allow an opportunity for members/member firms to game the system in order to avoid complying with the disclosure rule. The statistics clearly show that the vast majority of riskless principal transactions occur within 15-minutes of one another, the regulators have access to firm and transaction-specific data, and the examination process inclusive of this data would clearly show if any "gaming" was taking place once the disclosure rule was implemented. Moreover, we would like to underscore with both regulators that the overwhelming majority of industry members are rule-abiding, honest, hard working individuals - and firms. Do not write rules for the half-percent that end up costing the rest of us millions of dollars to implement, write them for customer and market protection and the 99.50% of the rest of us, and then utilize Member and Market Reg in ferreting out the bad actors.

In closing, RW Smith continues to believe there are better, more efficient, and more effective ways of achieving the twin objectives of pricing disclosure and riskless principal markup disclosure for retail customers. We have included our suggestions in this comment letter and would like to encourage both regulators to continue to engage the industry on the best and most reasonable way to achieve these objectives.

Finally, we would like to note that RW Smith participated in the drafting of the SIFMA comment letter, and would like to officially represent our support of that submission.

Thank you for your consideration of our comments.

Sincerely,

Paige W. Pierce
President & CEO
RW Smith & Associates, LLC

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11 December 2015

Marcia E. Asquith
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FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: Pricing Disclosure in the Fixed Income Markets (Regulatory Notice 15-36)

Dear Ms. Asquith:

CFA Institute[1] is pleased to comment on FINRA's proposed rules requiring its member firms to disclose certain information on customer confirmations for transactions in debt securities. CFA Institute represents the views of those investment professionals who are its members before standard setters, regulatory authorities, and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues that affect the efficiency, integrity and accountability of global financial markets.

Executive Summary

Need for both pre- and post-trade transparency. CFA Institute strongly supports efforts to increase transparency in the fixed-income market, and believes that measures to provide additional pre-trade information are warranted, in addition to the post-trade transparency that this proposal seeks. We encourage FINRA to consider additional ways to increase this transparency, including providing *all* customers with links to Trade Reporting and Compliance Engine (TRACE) data, not just select customers, as proposed.

Required disclosure in complex trades. We recommend use of a uniform standard for determining the reference price to be disclosed, even in complex trades.

Disclosure when there are material changes to the price of a security. We do not agree with the proposal that would allow dealers the option to omit disclosure of the reference price in cases

[1] CFA Institute is a global, not-for-profit professional association of more than 133,700 investment analysts, advisers, portfolio managers, and other investment professionals in 145 countries, of whom more than 127,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 147 member societies in 73 countries and territories.

where a material event results in significant price swings. Instead, we believe a better option is to require dealers to provide that disclosure with clarifying language.

Discussion

We agree with FINRA's concern that "investors in fixed-income securities currently are limited in their ability to understand and compare transaction costs associated with their purchase and sales." This is particularly noteworthy, given FINRA's own research indicating that "some customers paid considerably more than others in similar trades." We thus strongly support FINRA's efforts through this proposal to shine more light into the fixed-income market and to provide customers with additional information about their specific transactions.

Price Disclosure for Similar Transactions

As proposed, all member firms acting in the capacity of principals in transactions involving corporate or agency debt securities would have to disclose on retail customer confirmations:

- The price the customer paid for the bond;
- The "reference price" of the security subject to the principal trading transaction;
- The differential between the price the customer paid and the reference price; and
- A reference — and hyperlink if the confirmation is electronic — to publicly available TRACE data.

This would be required when firms are acting as principal and sell to, and buy from, their customers the same securities during that same trading day. Transactions not involving firms trading as principal would not trigger any requirement to provide this link.

Difference and Similarities to Municipal Securities Rulemaking Board Proposal

FINRA notes that it has discussed with the Municipal Securities Rulemaking Board (MSRB) a coordinated approach to rulemaking in this area. Similar to the MSRB, FINRA hopes through this rulemaking to provide investors with information that will help them better evaluate the costs and services received from their firms relating to select transactions. By providing links to the TRACE data, FINRA also hopes customers will gain understanding about firms' pricing practices.

The two proposals differ, however, in several respects, and FINRA invites comment on the differences. To that end, we provide suggestions where we favor the MSRB approach or otherwise believe uniformity is in the interests of investors.

Criteria for Triggering Disclosure

In an earlier proposal, FINRA proposed using a “qualifying size” trigger for additional disclosure requirements. We support FINRA’s decision in this revised proposal to instead use a “retail customer account standard.” This approach is not only a clearer and more direct standard for firms to apply, but also is consistent with the approach proposed by the MSRB.

Alternative Methodologies for More Complex Trades

Under the proposal, firms would need to determine and disclose the “reference price” of the security subject to the principal trading transaction. FINRA has proposed two approaches for making this calculation. In a straightforward scenario where the retail and firm principal transactions do not have intervening principal trades during the same trading day, and the principal trade is the same size or greater than the retail trades, the reference price would be the price of the principal trade.

Where there are intervening trades of differing prices or the principal trade is not equal to, or greater than, that of the retail customer, FINRA proposes giving firms flexibility to determine the reference price. The proposal notes that in these cases, firms can employ a “reasonable alternative methodology,” including the average weighted price of firm trades that were equal to or more than their customers’ trades. They also could use prices for the last same-day trades the firm executed as principal to their customers’ trades. In all cases, firms would have to consistently apply whatever methodology chosen.

We agree with FINRA’s assessment that while this flexibility may be more cost-effective for firms, it also would reduce comparability and thus investors’ ability to evaluate transactions. We thus argue for adoption of one uniform standard to be applied in all scenarios. We also recommend that should FINRA elect to retain use of a reference price, that it consider requiring firms to disclose the percentage of the price differential. This, we believe, would provide customers with a better contextual basis for comparison.

Material Changes to the Price of the Security

In cases where a material event (such as credit downgrades or breaking news) affects market prices and results in significant swings in bond market prices between the times of customer and firm trades, firms would have flexibility whether or not to disclose the reference price. They could choose not to disclose or disclose with clarifying information. In providing firms this option, FINRA reasons that depending on the circumstances, investors could be confused about the differences in the prices resulting from the abnormal swings.[2]

We encourage eliminating the option of whether to provide the price in these circumstance. While we appreciate FINRA's concern for investor confusion that might stem from large market swings, we believe investors should be able to rely on receiving a reference price. To that end, we recommend that firms be required to provide that reference price with clarifying information.

Link to TRACE Data

Under the proposal, only customers who are receiving additional disclosure due to firm principal trades in the same security would receive a link from their firms to TRACE on their confirmations. While we agree this will help direct those affected to a source with more information, we believe more should be done to increase transparency in fixed-income markets.

We favor the approach taken in the MSRB proposal. Under that proposal, firms would provide links to the Board's EMMA reporting system for all retail customer confirmations, regardless of whether the transactions involve trading as principal. All retail customers deserve to receive direct links to sources where they can gain additional information about their investments and price differentials, and better educate themselves about this market, generally. To that end, we recommend that firms provide all customers with links to TRACE.

Fixed Price New Issues

We support FINRA's proposal to exempt from the proposed disclosure requirements those transactions that are sold on their first trading day at the fixed offering price, on the basis that sufficient information accompanies new issues. We agree that disclosure requirements should continue to apply to variable price offerings that are part of secondary trades.

Trades Occurring on Functionally Separate Desks

Similar to the approach proposed by the MSRB, FINRA is proposing that transactions occurring on "functionally separate" trading desks located within a firm be excluded from calculating a reference price for purposes of disclosures on customer confirmations. Specifically, firm-side transactions that are functionally separate from those conducted on the retail-desk side would be exempt from disclosure, provided that firms have policies and procedures in place that demonstrate to examiners the transactions for institutional customers are separate from the retail

[2] The proposal makes clear that swings in prices resulting from general market volatility or normal price fluctuations would not be a basis for allowing firms the option of whether or not to disclose the reference price.

desks and from retail customers. We believe this approach reasonably achieves the goal to provide investor protections while also recognizing the practical realities of firm operations.

Positions Acquired by an Affiliate on a Previous Trading Day

FINRA's proposed disclosure requirements apply to relevant transactions occurring within the same trading day. Thus, the proposal would not apply when firms acting as principals execute trades with their affiliates whose position satisfies the trade, but the trade was not acquired on the same trading day. While we agree that this approach is reasonable when focusing on the same trading day as the pivotal time-frame for triggering disclosure requirements, we favor the alternative "look-through" approach proposed by the MSRB, and suggest adoption of this approach for consistency.

Conclusion

We strongly FINRA's efforts to increase the transparency in the fixed-income market by providing customers with new disclosures relating to their trades, and about the market We encourage FINRA and the MSRB to work together to better coordinate their approaches where the end goals are the same. This will increase consistency while also reducing investor confusion. Should you have any questions about our position, please do not hesitate to contact Kurt N. Schacht, CFA at kurt.schacht@cfainstitute.org, 212.756.7728 or Linda Rittenhouse at linda.rittenhouse@cfainstitute.org, 434.951.5333.

Sincerely,

/s/ Kurt N. Schacht

Kurt N. Schacht, CFA
Managing Director, Standards and
Financial Market Integrity
CFA Institute

/s/ Linda L. Rittenhouse

Linda L. Rittenhouse
Director, Capital Markets Policy
CFA Institute

TMC Bonds | TMCBONDS.COM FIXED INCOME MARKETPLACE

December 11, 2015

Electronic Mail

Attn. Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Request for Comment on Pricing Disclosure in the Fixed Income Markets 15-36

Dear Ms. Asquith:

TMC Bonds, L.L.C. ("TMC") welcomes the opportunity to respond to FINRA's Request for Comment #15-36. For efficiency, we have filed this response with the MSRB as well, as TMC seeks similar guidance in both markets.

TMC is an electronic exchange for trading fixed income securities and a registered Alternative Trading System ("ATS") with the Securities and Exchange Commission. Started in May 2000, TMC has become a leader in facilitating electronic trading for both taxable and tax-exempts bonds over its open and anonymous platform. As counter-party to each side of a trade, TMC reports approximately 4,500 municipal trades daily to the MSRB as riskless principal. TMC also has a significant and growing presence in the taxable market. In October, TMC accounted for approximately 16% of the corporate transaction volume for transactions with trade size under 250 bonds. As with municipals, TMC is the counter-party to the trade and reports its riskless principal trades to TRACE.

While the MSRB has filed a similar request for comment in Regulatory Notice 2015-16, we would like to emphasize support for FINRA and the MSRB to have a fully harmonized ruling. The cost of compliance for one proposal is already significant, and the possibility of adding multiple scenarios for different products greatly increases the programming complexity and cost. While there are differences in form for each market, we believe that the base methodology from either proposal does not present any issues that would negate uniform reporting.

Technology challenges aside, we are greatly concerned that the current Draft Rule has inconsistent goals and deviates from the Securities and Exchange Commission's 2012 Report recommendation to "consider requiring municipal bond dealers to disclose to customers, on confirmations for riskless principal transactions, the amount of any markup or markdown" by virtue of using an arbitrary time parameter as a means to identify riskless trades. While we believe the MSRB's shorter time frame is more meaningful than FINRA's "same-day" requirement to capture an estimated mark-up, its weakness is that it does not truly capture the spirit of disclosing "riskless-principal" mark-ups but instead discloses all matched trades executed within the set time. A time-based methodology, unless measured in much smaller increments, is including the baby with the bath water, as the true at-risk trades will be included with the riskless trades. This conflation of mixing the accurate with the misleading becomes more problematic as the time parameter is widened, as suggested in the FINRA proposal. Any trade committed without an order in-hand is an "at-risk" trade.

The time parameter obfuscates the potential risk that a trader takes and prices into a trading decision and blurs its meaning when a positioned bond is moved quickly out of inventory.

The time dilemma highlights the difficulty of trying to capture an idea that is difficult to define. If one is truly interested in disclosing any principal trade mark-up, then the only meaningful calculation is from the prevailing market price. As in most instances for illiquid bonds (using TMC's municipal experience as a barometer), 85% of the transacted bonds have no market depth, meaning it would be the owner of the security estimating the prevailing market price. Likewise, for disclosing any riskless principal trade mark-up, then the dealers contemporaneous cost would be appropriate.

Therefore, we believe that the only appropriate mark-up available for disclosure would be for true riskless principal trades, in which a matched trade is executed contemporaneously. We would support the regulators explicitly defining a riskless-trade and modeling language similar to FINRA's NTM-99-65 for equities, which defines a riskless-principal transaction as "a transaction in which a member, after having received an order to buy (sell) a security, purchases (sells) the security as principal and satisfies the original order by selling (buying) as principal at the same price (the offsetting "riskless" leg). Generally, a riskless principal transaction involves two orders, the execution of one being dependent upon the receipt or execution of the other; hence, there is no "risk" in the interdependent transactions when completed." We would also seek further transparency on current market data where a shorter time window can be used than the "same-day" recommendation. How does this change for a 2 second window? In a study conducted by Larry Harris, Chair in Finance USC Marshall School of Business, entitled "Transaction Costs, Trade Throughs, and Riskless Principal Trading in Corporate Bond Markets", corporate bond trades that occurred with a matched side within 2 seconds represented 41.7%

of all trades. As corporates can be sold short, this number suggest that for municipals a matched trade number should be higher, and therefore the suggested MSRB 2 hour time window may be an effort to prevent firms from engaging in manipulative behavior as opposed to truly identifying matched trades. Thus, we would support defining a riskless transaction for purposes of mark-up disclosure and adding language similar to the MSRB's Rule G-14 that prohibits positioning bonds in a fictitious manner or in furtherance of any fraudulent, deceptive or manipulative purpose.

We further support this methodology as, under the current proposal, the integration of systems to calculate the reference price will be expensive and, for some firms, nearly impossible to effect with current infrastructure. For example, TMC has clients who use a principal trading account to facilitate buying and selling bonds. There is no cost system for tracking P&L on the individual trades with this type of account; only the remaining cash balance in the account defines the theoretical P&L for the day. While the MSRB stated that most firms already know their cost due to regulatory requirements, many firms use a defined matrix that determines the mark-up to insure that the advisor works for a reasonable profit and thus track the mark-up, not the cost. This proposal would require these types of firm to build out a new system to track costs on an individual trade basis. Furthermore, in an environment that is encouraging firms to report, settle, and transact at faster times, the extra point of friction to calculate a reference price hours after a trade has occurred, will require a batch process whereby most firms will be sending an end-of-day reference price file to their clearing partners for producing customer confirmations. The concept of true straight-through-processing, a long standing industry goal, dies here. Additionally, the clearing firms themselves may have their own challenges, as they will now have to accept an end-of-day file that will need to be batch processed prior to the creation of the confirmation.

TMC's clearing firm has already expressed its inability to perform this task, based on its current system architecture.

If the regulators are seeking to disclose mark-ups based on a defined set of variables, then the data already resides with both the MSRB and FINRA. Why would it be appropriate to delegate the calculation to each firm when one central party already has all the data and can readily calculate the value? By having the regulators add the tag to its existing pricing feed, thousands of firms would be spared the burden of attempting to integrate systems and independently calculate a reference price. As the price could be disseminated in near real-time, assuming an appropriate time parameter, this would eliminate the complexity of adding batch processing to the clearing process. Furthermore, as the regulator mines the data, the algorithm could be adjusted to changing markets without tasking thousands of firm to coordinate systems. Similarly, if the trades were truly riskless, the cost basis of each trade would be known at the time of execution and could be easily added to a trade report or clearing ticket and thus promote the benefits of straight-through-processing.

While the goal of disclosing riskless principal mark-ups is laudable, the current proposal's attempt to define this type of transaction is too general. By inadvertently including risk trades, using a broad time frame definition, a customer will never have an apples to apples comparison when reviewing a trade confirm. We believe greater examination of definitions, surrounding transaction types such as bids wanted and true matched trades when buying for customers, will provide a more reasonable basis for defining a riskless trade. Furthermore, the economics of having a decentralized process whereby each dealer is responsible for determining either a reference trade price or mark-up value, would be costly, complex, and cause friction for the efficient settlement of trades.

We greatly appreciate the opportunity to respond and are available for any further conversations.

Sincerely,

Thomas S. Vales
Chief Executive Officer

FINANCIAL INFORMATION FORUM
5 Hanover Square
New York, New York 10004
____
212-422-8568

Via Electronic Delivery

December 11, 2015

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: MSRB Notice 2015-16 - Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers; FINRA Notice 15-36 - FINRA Requests Comment on a Revised Proposal Requiring Confirmation Disclosure of Pricing Information in Corporate and Agency Debt Securities Transactions.

Dear Mr. Smith and Ms. Asquith,

The Financial Information Forum (FIF)[1] would like to take this opportunity to comment on MSRB Notice 2015-16 and FINRA Notice 15-36 ("Proposals"). The FIF Back Office Committee ("FIF") has reviewed the proposals from an implementation perspective. We understand the intent of the proposals is to provide retail investors with insight and transparency into transaction costs and dealer compensation associated with their trades. We believe these proposals create significant implementation challenges to all dealers of municipal, corporate and agency debt securities, and may cause unintended consequences. FIF's comments on both proposals are limited to considerations related to implementation of the alternatives outlined in each of the proposals, and do not address policy issues. *This letter should not be interpreted as an endorsement or recommendation for either a mark-up or reference price on retail customer confirmations.*

Alignment of MSRB and FINRA is Imperative

As noted in our previous Comment Letter[2], FIF members reiterate the request for MSRB and FINRA to take a coordinated approach in their rule making and requirements on this initiative. While the intent of

[1] FIF (www.fif.com) was formed in 1996 to provide a centralized source of information on the implementation issues that impact the securities industry across the order lifecycle. Our participants include trading and back office service bureaus, broker-dealers, market data vendors and exchanges. Through topic-oriented working groups, FIF participants focus on critical issues and productive solutions to technology developments, regulatory initiatives, and other industry changes.

[2] FIF Comment Letter on MSRB Notice 2014-20 and FINRA Notice 14-52; submitted January 20, 2015.

these new proposals is similar, to provide added transparency to retail[3] customers through additional disclosure on the customer confirmation, there are significant differences between the most recent MSRB proposal to require mark-up information and the FINRA proposal to require dealers to provide reference pricing. The obvious differences include: the timeframe for triggering disclosure (MSRB's two hour window vs. FINRA's same trading day), data required to be disclosed on the confirmation (dealer mark-up on prevailing market price expressed as a percentage vs. differential between price to the customer and the member's reference price.) Each of these approaches will vary in implementation costs and ongoing operational costs.

Additionally, while we prefer to limit the scope of this disclosure to address only "riskless" principal trades, if the regulators intend to broaden the scope of the requirements in the future (for example, expand the focus from riskless principal to include all principal trades), FIF members wish to avoid a double build-out and would prefer that all requirements be addressed within the same initiative. From an implementation perspective, incremental steps result in increased costs.

FIF members urge MSRB and FINRA to be fully harmonized in any resulting regulations, as we expect that costs would increase exponentially if there are significant variations between MSRB and FINRA rules, as well as extended lead times for implementation.

Limited Resources

It is important to understand that in most cases, the same resources within a firm are responsible to effect the necessary changes in both the TRACE and the MSRB data capture and confirmation processes. Implementation of T+2 for corporate and municipal bonds will rely largely on the same skilled and knowledgeable subject matter experts to conduct the analysis, and make and test the operational and technical changes. We urge the regulators to consider the burden placed on these finite resources, given the array of regulatory initiatives planned for 2016 and 2017.[4]

While neither FINRA nor the MSRB have provided timeframes for implementation of these new disclosure requirements, overlapping timeframes with the industry's preparations for T+2 settlement must be avoided. Chair White has registered her strong support for T+2 requesting that SROs finalize schedules of rule changes such that the industry could complete its work no later than the third quarter of 2017. Accordingly, MSRB has committed to adopt rule changes by Q2 2016 to meet the targeted completion date. The many initiatives involved to reach T+2 will be resource intensive and costly. Whatever approach is agreed by the regulators to address confirmation disclosure, we request that the effective dates be scheduled to allow sufficient time for implementation after T+2 has been completed.

Significant Implementation Challenges

In addition to urging that regulators develop an implementation timeline with due consideration being given to T+2 and other regulatory initiatives that will draw upon the same finite resources, FIF has identified the following implementation challenges with the FINRA and MSRB proposals that it believes should be addressed in any final proposal submitted to the Commission for approval.

[3] FIF members appreciate the consistent approach proposed by both MSRB and FINRA to identify retail customers as those that are "not institutional" as defined by MSRB G-8 or FINRA 4512(c), or not a proprietary account. Inclusion of institutional accounts under these proposals would cause serious disruption to the automated confirmation process (e.g. Omgeo).

[4] Several TRACE and MSRB changes are in progress and must be completed by May 23, 2016. Most recently, additional changes to TRACE have been proposed by FINRA for implementation July 18, 2016. Pending adoption of T+2 rule changes in Q2 2016, work must start immediately following current initiatives to meet a Q3 2017 target for T+2.

Straight Through Processing Disruptions

Using the full trading day window to determine if a trade was done risklessly will negatively impact straight-through processing in those firms that currently produce customer confirmations at the time of the trade. There has been a concerted effort in recent years to streamline and automate, and this requirement will break the process that has taken years to achieve.

- Dealers will need to hold up generating a retail trade confirmation to identify any possible related principal (inter-dealer) trades in the same security, on the same side. Principal transactions may have been executed either before or after the customer trade, or both. In any case, a process must be developed to capture trades that are potentially related and to identify specifically which trades should be applied to the calculation to be included on the confirmation. Manual intervention may be required to ensure the appropriate trades are selected; that is, that the principal trades identified are those most closely aligned to the riskless trade and representative of the prevailing market.
- If the same-day trading window is ultimately used in any resulting requirements, limiting the search to principal trades that *preceded* the customer trade would be preferable. Although this does not eliminate the potential need for manual intervention, it would not require the confirmation process to be deferred until end-of-day.
- There are firms that generally use a batch cycle to produce “retail” confirms, but leverage the real-time “institutional ID” process[5] to generate confirms for their high net worth clients who utilize third party custodians, for example. The need to place the added information on the ID confirmation for these clients would seriously disrupt the process and cause widespread consequences. While a follow-up paper confirmation could be produced for these high net worth individuals, in all likelihood, neither the investor nor the custodian wants to manage the paperwork.

Leveraging TRACE/MSRB Reference Prices

There are pros and cons to utilizing a reference price made available by FINRA or MSRB, as discussed in the proposals. Some uniform set of business rules would need to be established to determine exactly the criteria for identifying which trades should be included in the reference price calculations.

- Pros
    - For firms utilizing a batch process, this would be straightforward to implement; assuming an end-of-day feed were made available by MSRB and FINRA prior to 6PM (ET), this would allow most firms time to include the information in their confirmation processes.
    - This would eliminate the need for each firm to build the “matching engine” required to identify transactions representing contemporaneous cost or related principal transaction(s).
    - This would reduce the significant burden and expense on smaller firms, particularly those that rely on third-parties for clearing and/or transaction processing.[6]
    - This approach would provide consistent reference pricing across the industry.
    - Customers would have confidence in market transparency if the prevailing market or reference prices were obtained from FINRA or MSRB.

[5] See Footnote 3.

[6] Some third-party firms such as clearing firms and other service providers have indicated they will not take responsibility, for both operational and legal reasons, to identify which trade(s) represent the principal trade(s) related to a riskless transaction; therefore, introducing brokers and client firms would need to provide their clearing firm or service provider with the appropriate reference price or contemporaneous cost, which may require matching principal transaction(s) to the riskless trade. Leveraging a feed made available by MSRB and TRACE was described by one clearing firm as the optimal approach, as it would be seamless to the introducing brokers, with an implementation cost less than half of the $500,000 estimated to capture contemporaneous cost or other reference price from the introducing broker. This estimate of $500K does not include the cost that would be imposed on the many introducing brokers, which are primarily smaller regional firms, to identify the matching trades.

- Cons
    - FINRA or MSRB reference prices would not reflect the circumstances of that particular customer trade.
    - Retail customers will not understand the nuanced-differences between their trade and the time-weighted average price of others in the market. The onus would be on the investment advisor to explain the differences, with the facts and circumstances of the other trades unknown to him/her.
    - For those utilizing a real-time confirmation process, dealers do not want to hold up the confirmation to obtain the TRACE or MSRB end-of-day reference price. Similar to the issues with delaying the confirmation until end-of-day to capture potential principal trades, firms would want to expedite the process by capturing the most recent price or set of prices available in real-time from TRACE or MSRB. However, in this real-time scenario, a same day "look-back" may not produce any trades in that security, particularly if the transaction were to occur early in the day. In that case, some other methodology must be agreed upon.

Calculating Mark-Up/Mark-Down for Purposes of Disclosure
The MSRB proposal would require dealers to include the dealer's mark-up or mark-down from the contemporaneous cost or the prevailing market price for the security on the customer confirmation. Dealers are required by MSRB G-30 fair pricing standards to perform diligence in determining the market value and reasonable compensation on any security at the time of proposing a bid or offer price. Following are the considerations regarding use of the "Prevailing Market Price" as the reference price from which the mark-up or mark-down would be calculated.

- Pro
    - A significant challenge is rooted in the fact that the large majority of municipal bonds trade infrequently. In most circumstances where there is no previous street-side trade execution or other transaction that may determine "contemporaneous cost" and no clearly identifiable "reference" trades, establishing a reasonable price and a fair mark-up is accomplished using many other inputs including: evaluated pricing, similar credits, market sector, transaction size, supply and demand considerations, and other relevant factors. However, because a reasonable method to determine the prevailing market price is required as part of the current business process, the prevailing market price and inputs to derive it should be readily available.
- Con
    - Despite the availability of a prevailing market price, FIF does not believe this price will be a clear metric for retail customers to understand. The inputs used to calculate the prevailing market price will not be disclosed on the confirmation, leading to a mark-up or mark-down based on a price with no context, which may confuse customers.

While the dealer's contemporaneous cost is perhaps more relevant for establishing the mark-up/mark-down in a *riskless trade*, for reasons discussed previously, it is significantly more difficult and more costly to capture. However, for purposes of establishing the mark-up/mark-down in a *principal trade*, the issues are far more complex. The mark-up on a bond includes profit along with the cost of doing business. Dealers are hedging positions to reduce their amount of risk. Disclosing the mark-up to the customer will not factor in any potential loss incurred on the hedge. The costs of operating the business and maintaining an inventory should also factor into the mark-up. These factors will not be clearly identifiable to the customer on the confirmation which misleads the customer to believe that the mark-up is full profit for the dealer. Because a mark-up may include multiple components such as sales credit, desk credit, and compensation for risk in the case of a principal trade, FIF members believe presenting a percentage of the price differential on the confirmation will confuse retail investors.[7]

As we've stated previously in this letter, we are not endorsing either a mark-up or reference price to be disclosed on customer confirmations. There appears to be no clear consensus amongst FIF members or the industry as to which proposal is preferred. Regardless of which methodology is ultimately selected by the regulators for the purposes of disclosure, FIF members believe that only the dollar amount differential should be displayed, and should only be applied in cases where the dealer firms themselves establish the "reference price" being used (e.g. contemporaneous cost). In cases where a third-party price (TRACE, MSRB or some other form of derived price that is not directly linked to the customer trade) is displayed, a difference expressed in terms of percentage and/or dollar amount is meaningless and misleading, as it does not accurately reflect the mark-up or how the bond was priced to the customer.

MSRB and FINRA should consider that customers do not currently receive a similar percentage of price differential on their confirmations, as no other asset class requires the percentage to be disclosed. Additionally, including the percentage spreads on the confirmation will require significant programming, as market data and other information not normally passed from front office systems to back office systems will need to be accommodated. This will lead to increased costs and time to implement.

Other Concerns

Impact on Liquidity

One potential "unintended consequence" of this initiative is firms may be driven away from carrying inventory and toward conducting agency-only business. While FIF comments are typically limited to implementation issues, FIF is mentioning this risk due to the anticipated difficulty and cost of implementing the mark-up or reference price disclosure requirements, which could contribute, in part, to a firm's decision to limit its principal trading and market making activities. Retail investors may be negatively impacted, as investment advisors look to external markets, rather than internally, to buy and sell bonds for their clients.

Inability to "Look Through"

In many firms there will not be an ability to "look through" to principal trades on the other trading desks that may supply offerings or bids for retail investors. With separate P&Ls, and most often conducting inter-dealer business on completely separate platforms, the opportunity to identify the principal leg of trade may not be obtainable until late in the transaction life-cycle after all trades have been processed.

Time of Execution

FIF members expressed concern in placing the Time of Execution on the confirmation for two primary reasons: 1) it will be an additional expense to parse that information from trading platforms, as this is not typically carried through to the back office systems that generate the confirmations; and, 2) it will not be possible to adjust the Time of Execution properly in conjunction with any trade modifications, cancelations or corrections. While we understand MSRB's intent in requesting the Time of Execution on

[7] While FIF members fully understand the intent of this initiative is to disclose the full difference between the dealer's cost and the dealer's price to the customer, a simple and straightforward alternative would be to limit the disclosure on all retail customer confirmations to display only sales credit. This would provide increased transparency to retail customers in terms that are easily understood by the retail investor. The sales credit is known at time of the trade, it can be applied to any retail customer transaction regardless of a corresponding principal transaction, and is already passed on to the back office which would easily allow for the sales credit to be included on the customer confirmation with minor additional programming.

the trade confirmation is to support the investors' ability to look up the prices of similar trades on EMMA, the number of trades in each CUSIP listed on EMMA are so limited that investors will not have difficulty in ascertaining the prevailing market prices at or around the time of their trade. FIF members believe the Time of Execution is unnecessary information on a municipal bond confirmation, and it is not required on a confirmation for other security types.

Retail Confusion

In addition to the examples that have already been described, retail confusion may also be caused by the fact that these disclosures will only occasionally be provided; that is, they will apply to only certain "riskless" transactions. Furthermore, in response to the question regarding the form and format of the additional disclosure, FIF members believe that placing added information on a document separate from the confirmation will present additional challenges in bringing together documents that would be produced by separate systems. It would only add to customer confusion if the information was not delivered to the retail investor as one unit.

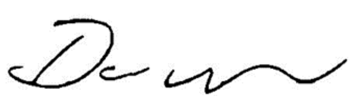
Summary

FIF believes this is a policy decision best left to the dealer firms to voice their opinions regarding trading and market making activities, and their positions and preferences with respect to additional disclosure on retail customer confirmations. Unfortunately, there appears to be no single solution that would accomplish the goals of full transparency, be easy for the retail investor to understand and straightforward to implement. Therefore, *FIF does not advocate or recommend the use of any particular method, but merely points out the implementation impacts of each approach.*

Again, we request that the implementation solutions for FINRA 15-36 and MSRB 2015-16 be consistent and realistic in terms of delivering information that is readily available, requiring limited or no manual intervention, and allowing the confirmation process to remain as automated as possible and processed in a timely fashion.

In conclusion, FIF would like to thank the MSRB and FINRA for providing the opportunity to comment on the proposed changes, and we support these efforts to establish a consistent, harmonized approach to transparency and disclosure.

Regards,



Darren Wasney
Program Manager
Financial Information Forum