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Page 1 of * 546

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

File No.* SR - 2016 - * 12

Amendment No. (req. for Amendments *)

Filing by Municipal Securities Rulemaking Board

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

Initial * ☑ Amendment * ☐ Withdrawal ☐

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

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

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

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

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

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

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document ☐ Exhibit 3 Sent As Paper Document ☐

Description

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

Proposed Rule Change to MSRB Rules G-15 and G-30 to Require Disclosure of Mark-Ups and Mark-Downs to Retail Customers on Certain Principal Transactions and to Provide Guidance on Prevailing Market Price

Contact Information

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

First Name * Michael Last Name * Post

Title * General Counsel -- Regulatory Affairs

E-mail * mpost@msrb.org

Telephone * (202) 838-1500 Fax

Signature

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

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

Date 09/01/2016

By Ronald W. Smith

(Name *)

(Title *)

Corporate Secretary

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

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

Form 19b-4 Information *

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

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Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act" or "Exchange Act"),[1] and Rule 19b-4 thereunder,[2] the Municipal Securities Rulemaking Board ("MSRB" or "Board") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change to amend MSRB Rule G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to customer transactions, and MSRB Rule G-30, on prices and commissions, (the "proposed rule change") to require brokers, dealers and municipal securities dealers (collectively, "dealers") to disclose mark-ups and mark-downs to retail customers on certain principal transactions and to provide dealers guidance on prevailing market price for the purpose of calculating mark-ups and mark-downs and other Rule G-30 determinations.

(a) The text of the proposed rule change is attached as Exhibit 5. Text proposed to be added is underlined, and text proposed to be deleted is enclosed in brackets.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

The Board approved the proposed rule change at its July 27-28, 2016 meeting. Questions concerning this filing may be directed to Michael L. Post, General Counsel – Regulatory Affairs, or Saliha Olgun, Assistant General Counsel, at 202-838-1500.

If the Commission approves the proposed rule change, the MSRB will announce the effective date of the proposed rule change no later than 90 days following Commission approval. The effective date will be no later than 365 days following Commission approval.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Proposed Amendments to Rule G-15

The MSRB is proposing to amend Rule G-15 to require dealers to provide additional pricing information on customer confirmations in connection with specified

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

municipal securities transactions with retail customers. Specifically, if a dealer trades as principal with a retail (i.e., non-institutional) customer in a municipal security, the dealer must disclose the dealer's mark-up or mark-down (collectively, "mark-up," unless the context requires otherwise) from the prevailing market price for the security on the customer confirmation, if the dealer also executes one or more offsetting principal transaction(s) on the same trading day as the customer, on the same side of the market as the customer, in an aggregate size that meets or exceeds the size of the customer trade.

Many dealers already are required to disclose additional pricing information to customers for certain types of transactions under certain circumstances. Pursuant to Exchange Act Rule 10b-10, dealers effecting equity transactions in which they act in a riskless principal capacity must disclose on the customer confirmation the difference between the price to the customer and the dealer's contemporaneous purchase or sale price.[3] Pursuant to Rule G-15, dealers effecting municipal securities transactions in which they act in an agent capacity must disclose on the customer confirmation the amount of remuneration received from the customer in connection with the transaction (i.e., the commission).

The MSRB has conducted analyses of various data reported to its Electronic Municipal Market Access (EMMA®) system[4] in order to evaluate the potential need for the proposed mark-up disclosure rule. Over the period from July 1, 2015 through September 30, 2015 (Q3 2015),[5] the average daily number of retail-size[6] customer

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3 See 17 CFR 240.10b-10. Under Rule 10b-10, where a broker or dealer is acting as principal for its own account and is not a market maker in an equity security, and receives a customer order in that equity security that it executes by means of a principal trade to offset the contemporaneous trade with the customer, the rule requires the broker or dealer to disclose the difference between the price to the customer and the dealer's contemporaneous purchase (for customer purchases) or sale price (for customer sales). See Rule 10b-10(a)(2)(ii)(A). Where the broker or dealer acts as principal for any other transaction in a defined National Market System stock, or an equity security that is listed on a national securities exchange and is subject to last sale reporting, the rule requires the broker or dealer to report the reported trade price, the price to the customer in the transaction, and the difference, if any, between the reported trade price and the price to the customer. See Rule 10b-10(a)(2)(ii)(B).

4 EMMA is a registered trademark of the MSRB.

5 Q3 2015 trading activity was substantially similar to trading activity in the preceding two and following one quarter. For example, the total number of trades reported to EMMA in Q3 2015 was 2,319,070 while the average number of trades reported to EMMA per quarter in 2015 was 2,305,705. Similarly, the number of retail-size, customer transactions in the secondary market in which the dealer acted in a principal capacity in Q3 2015 was 994,409 while the average number of trades per quarter with the same characteristics during 2015 was 980,809.

transactions in the secondary market for municipal securities in which the dealer acted in a principal capacity was 15,538. The transactions were mainly concentrated among large firms. These trades were reported by approximately 700 dealers, however, the top 20 dealers with the highest volumes accounted for approximately 73 percent of the transactions in municipal securities. Of those retail-size customer transactions in the secondary market in which the dealer acted in a principal capacity, approximately 55 percent would have likely received a disclosure if the proposed rule had been in place.[7]

Of those trades which likely would have received disclosure, 38 percent of the offsetting trade(s) that would have triggered the disclosure occurred simultaneously (the reported times of both the customer trade and the offsetting trade(s) were identical), 50 percent of the offsetting trade(s) occurred within 19 seconds of the customer trade, and 83 percent of the offsetting trades occurred within 30 minutes.

For those trades that likely would have received disclosure, the median value of the estimated mark-up for customer purchases was approximately 1.20 percent and the median value of the estimated mark-down was approximately 0.50 percent.[8] For both mark-ups on customer purchases and mark-downs on customer sales, many customers paid considerably more than the median value. For example, five percent of customer

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6 The data reported to the MSRB do not indicate whether the customer purchasing or selling a security has an "institutional" account as defined in Rule G-8(a)(xi). Therefore, for the purposes of the analysis included here, the MSRB has defined a "retail-size" transaction as any customer transaction with a reported trade amount of 100 bonds or fewer or a face value of $100,000 or less. The MSRB recognizes that this proxy for retail customers may, in some cases, include transactions with institutional account holders and may also fail to include transactions with some retail customers.

7 That is, the customer's trade with a dealer was preceded or followed, on the same trading day, by one or more trades equal to the customer trade, by the dealer on the other side of the market in the same security. The percentage of customer trades that would have received a disclosure may be overestimated because in some cases, the dealer trade on the other side of the market may have been with an affiliate and the "look through" provision of the proposed rule may not have identified another trade that would have required disclosure.

8 The mark-up and mark-down calculations involved matching customer trades to one or more offsetting same-day principal trades by the same dealer in the same CUSIP. This included matching same-size trades as well as trades of different sizes where there was no same-size match (e.g., a dealer purchase of 100 bonds matched to two sales to customers of 50 bonds each). The mark-ups (mark-downs) on customer buys (sells) correspond to the percentage difference in price in customer trades and the offsetting principal trade.

purchases that would have been eligible for disclosure (representing approximately 14,900 trades) had estimated mark-ups higher than 2.25 percent while five percent of customer sales (representing approximately 6,500 trades) had estimated mark-downs higher than 1.51 percent.

The MSRB believes that retail investors are currently limited in their ability to assess and compare transaction costs associated with the purchase or sale of municipal securities. Joint investor testing conducted by the Financial Industry Regulatory Authority ("FINRA") and the MSRB ("joint investor survey") revealed that investors lack a clear understanding of how dealers are compensated when dealers act in a principal capacity and that investors have a desire for more information on this topic. Retail investors transacting with dealers acting in a principal capacity may, therefore, participate in the municipal securities market with less information than other market participants and be less able to foster price competition.[9] This information asymmetry may be observable, in part, in the large differences between estimated median mark-ups and the highest mark-ups paid by retail customers. As noted above, the five percent of customer trades with the highest mark-ups have mark-ups that are more than twice as large as the median mark-up.

Some market participants have asserted that the observed dispersion in mark-ups might be explained by bond- or execution-specific characteristics (e.g., that higher mark-ups can be explained by the additional dealer costs associated with transacting in relatively small quantities). The data do not support this conclusion. An analysis of the transactions that took place during Q3 2015 and that likely would have received disclosures if the proposed rule had been in place indicates that not only are the large dispersions in mark-ups not fully explained by bond- or execution-specific characteristics, but also that, in some cases, factors that might be expected to result in lower mark-ups appear to be associated with higher mark-ups. For example, the median quantity of bonds traded in transactions with the highest mark-ups was either the same or similar to the median quantity of bonds traded in transactions with significantly lower mark-ups and bonds with higher trading frequencies in Q3 2015, and presumably higher liquidity, actually had higher estimated mark-ups than bonds that traded less frequently. The MSRB believes that requiring dealers to disclose their mark-ups on retail customer confirmations would provide meaningful and useful pricing information and may lower transaction costs for retail transactions.

As described in greater detail in the section on comments received on the proposed rule change, the MSRB initially solicited comment on a related proposal in MSRB Notice 2014-20 (the "initial confirmation disclosure proposal"),[10] and

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9 The SEC's 2012 Report on the Municipal Securities Market reached similar conclusions based on multiple studies. See U.S. Securities and Exchange Commission, Report on the Municipal Securities Market (July 31, 2012).

10 See MSRB Notice 2014-20 (November 17, 2014).

subsequently on a revised proposal in MSRB Notice 2015-16 (the "revised confirmation disclosure proposal").[11] The MSRB also has been coordinating with FINRA regarding the development of similar proposals, as appropriate, to foster generally consistent potential disclosures to customers across debt securities and to reduce the operational burdens for firms that trade multiple fixed income securities. The MSRB and FINRA published their initial and revised confirmation disclosure proposals on similar timelines,[12] and FINRA filed with the Commission a substantially similar proposed rule change to the proposed amendments to Rule G-15 on August 12, 2016.[13]

Provided below is a more detailed description of each significant aspect of the proposed amendments to Rule G-15.

Scope of the Disclosure Requirement

The proposed mark-up disclosure requirement would apply where the dealer buys (or sells) a municipal security on a principal basis from (or to) a non-institutional customer and engages in one or more offsetting principal trade(s) on the same trading day in the same security, where the size of the dealer's offsetting principal trade(s), in the aggregate, equals or exceeds the size of the customer trade. A non-institutional customer would be a customer with an account that is not an institutional account, as defined in Rule G-8(a)(xi), (i.e., a retail customer account).[14] The proposed rule change would apply to transactions in municipal securities, other than municipal fund securities.[15]

The MSRB believes that the proposed amendments would provide meaningful pricing information to retail investors, which would most benefit from such disclosure, while not imposing unduly burdensome disclosure requirements on dealers. The MSRB

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11 See MSRB Notice 2015-16 (September 24, 2015).

12 See FINRA Regulatory Notice 14-52 (November 2014) and FINRA Regulatory Notice 15-36 (October 2015).

13 See SR-FINRA-2016-032 (Aug. 12, 2016).

14 Rule G-8(a)(xi) defines an institutional account as

> the account of (i) a bank, savings and loan association, insurance company, or registered investment company; (ii) an investment adviser registered 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.

15 See discussion infra, Exceptions for Functionally Separate Trading Desks, List Offering Price Transactions and Municipal Fund Securities.

believes that requiring disclosure for retail customers, i.e., those with accounts that are not institutional accounts, would be appropriate because retail customers typically have less ready access to market and pricing information than institutional customers. The MSRB believes that using the definition of an institutional account as set forth in Rule G-8(a)(xi) to define the scope of the disclosure requirement would be appropriate because reliance on an existing standard would simplify implementation and thereby reduce costs associated with the requirement.[16]

Same-Day Triggering Timeframe

The MSRB believes that it would be appropriate to require disclosure of the mark-up where the dealer's offsetting principal trade(s) equaled or exceeded the size of the customer trade on the same trading day. To the extent that a dealer will often refer to its contemporaneous cost or proceeds, e.g., the price it paid or received for the bond, in determining the prevailing market price for purposes of calculating the mark-up or mark-down, the MSRB believes that limiting the disclosure requirement to those instances where there is an offsetting trade in the same trading day would generally make determination of the prevailing market price easier.

As is discussed in greater detail below, a number of commenters stated that the window for triggering disclosure should be limited to two hours. Among other things, commenters argued that a two-hour window would be easier to implement, and would more closely capture riskless principal trades, which would align the proposed disclosure to the riskless principal disclosure requirements for equity securities under Exchange Act Rule 10b-10.[17]

The MSRB believes that there are added benefits to requiring disclosure for trades that occur within the same trading day, rather than only trades that occur within two hours. First, the full-day window would ensure that more investors receive mark-up disclosure. Second, the full-day window may make dealers less likely to alter their trading patterns in response to the proposed requirement, as dealers would need to hold positions overnight to avoid the proposed disclosure.[18]

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16 As discussed in greater detail below, the MSRB initially proposed that the disclosure requirement would apply to customer trades involving 100 bonds or fewer or bonds in a par amount of $100,000 or less. In response to comments that the proposed size-based standard could either exclude retail customer transactions above that amount from the proposed disclosure, or subject institutional transactions below that amount to the proposed disclosure, the MSRB revised the proposal to incorporate the Rule G-8(a)(xi) definition of an institutional account.

17 See 17 CFR 240.10b-10.

18 It is important to note that, under Rule G-18, on best execution, dealers must use reasonable diligence to ascertain the best market for the security and buy or sell in that market so that the resultant price to the customer is as favorable as possible

Some commenters recommended that the proposed disclosure obligation be limited to riskless principal transactions involving retail investors, which, in their view, would more accurately reflect dealer compensation and transaction costs and be more consistent with the stated objectives of the SEC in this area. These commenters would apply the requirement to riskless principal transactions as previously defined in the equity context by the Commission, where the dealer has an "order in hand" at the time of execution. However, the MSRB believes that it may be difficult to objectively define, implement and monitor a riskless principal trigger standard for municipal securities. The MSRB also believes that customers would benefit from the disclosure irrespective of whether the dealer's capacity on the transaction was riskless principal and believes, at this juncture, that using the riskless principal standard ultimately would be too narrow.

Non-Arms-Length Affiliate Transactions

With respect to the offsetting principal trade(s), where a dealer buys from, or sells to, certain affiliates, the proposal would require the dealer to "look through" the dealer's transaction with the affiliate to the affiliate's transaction(s) with third parties in determining when the security was acquired and whether the "same trading day" requirement has been triggered. Specifically, the MSRB proposes to require dealers to apply the "look through" where a dealer's transaction with its affiliate was not at arms-length. For purposes of the proposed rule change, an "arms-length transaction" would be considered a transaction that was conducted through a competitive process in which non-affiliate dealers could also participate -- e.g., pricing sought from multiple dealers, or the posting of multiple bids and offers -- and where the affiliate relationship did not influence the price paid or proceeds received by the dealer. As a general matter, the MSRB would expect that the competitive process used in an "arms-length" transaction, e.g., the request for pricing or platform for posting bids and offers, is one in which non-affiliates have frequently participated. The MSRB believes that, for example, sourcing liquidity through a non-arms-length transaction with an affiliate is functionally equivalent to selling out of a dealer's own inventory for purposes of the proposed disclosure trigger. The MSRB therefore believes it would be appropriate in those circumstances to require a dealer to "look through" its transaction in a security with its affiliate to the affiliate's transactions

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under prevailing market conditions. Rule G-18, Supplementary Material .03 emphasizes that a dealer must make every effort to execute a customer transaction promptly, taking into account prevailing market conditions. Any intentional delay of a customer execution to avoid the proposed disclosure requirement or otherwise would be contrary to these duties to customers. A dealer that purposefully delayed the execution of a customer order to avoid the proposed disclosure also may be in violation of the MSRB's fundamental fair-dealing rule, Rule G-17, on conduct of municipal securities and municipal advisory activities.

in the security with third parties to determine whether the proposed mark-up disclosure requirement applies in these circumstances.[19]

Exceptions for Functionally Separate Trading Desks, List Offering Price Transactions and Municipal Fund Securities

Functionally Separate Trading Desks. The proposed amendments contain a number of exceptions from the mark-up disclosure requirement. First, if the offsetting same-day dealer principal trade was executed by a trading desk that is functionally separate from the dealer's trading desk that executed the transaction with the customer, the principal trade by that separate trading desk would not trigger the disclosure requirement. Dealers must have in place policies and procedures reasonably designed to ensure that the functionally separate principal trading desk through which the dealer purchase or dealer sale was executed had no knowledge of the customer transaction. The MSRB believes that this exception is appropriate because it recognizes the operational cost and complexity that may result from using a dealer principal trade executed by a separate, unrelated trading desk as the basis for determining whether a mark-up disclosure is triggered on the customer confirmation. For example, the exception would allow an institutional desk within a dealer to service an institutional customer without triggering the disclosure requirement for an unrelated trade performed by a separate retail desk within the dealer. At the same time, in requiring that the dealer have policies and procedures in place that are reasonably designed to ensure that the other trading desk had no knowledge of the customer transaction,[20] the MSRB believes that the safeguards surrounding the exception are sufficiently rigorous to minimize concerns about the potential misuse of the exception. In other words, in the example above, the dealer could not use the functionally separate trading desk exception to avoid the proposed disclosure

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19 Similarly, as explained in greater detail, infra, in the discussion of the proposed prevailing market price guidance, in the case of a non-arms-length transaction with an affiliate, the dealer also would be required to "look through" to the affiliate's transaction(s) with third parties in the security and the time of trade and related cost or proceeds of the affiliate in determining the dealer's calculation of the mark-up pursuant to Rule G-30.

20 This provision is distinguished from the "look through" provision noted above, whereby the customer transaction is being sourced through a non-arms-length transaction with the affiliate. Under the separate trading desk exception, functionally separate trading desks are required to have policies and procedures in place that are reasonably designed to ensure that trades occurring on the functionally separate trading desks are executed with no knowledge of each other and reflect unrelated trading decisions. Additionally, the MSRB notes that this exception would only apply to determine whether or not the proposed disclosure requirement has been triggered; it does not change the dealer's requirements relating to the calculation of its mark-up or mark-down under Rule G-30.

requirement if trades at the institutional desk were used to source securities for transactions at the retail desk.

The MSRB also believes that this exception is appropriate and consistent with the concept of functional and legal separation that exists in connection with other regulatory requirements, such as SEC Regulation SHO, and notes that some dealers may already have experience maintaining functionally separate trading desks to comply with these requirements, depending upon their particular mix of business.

List Offering Price Transactions. Second, the mark-up would not be required to be disclosed if the customer transaction is a list offering price transaction, as defined in paragraph (d)(vii)(A) of Rule G-14 RTRS Procedures.[21] For such transactions, bonds are sold at the same published list offering price to all investors, and the compensation paid to the dealer, such as the underwriting fee, is paid for by the issuer and typically is described in the official statement.[22] Given the availability of information in connection with such transactions, the MSRB believes that the proposed mark-up disclosure would not be warranted for list offering price transactions.

Municipal Fund Securities. Lastly, disclosure of mark-ups would not be required for transactions in municipal fund securities. Because dealer compensation for municipal fund securities transactions is typically not in the form of a mark-up, the MSRB believes that the proposed mark-up disclosure would not have application for transactions in municipal fund securities. Additionally, the proposed requirement to disclose the time of execution and a reference and hyperlink to the Security Details page for the customer's security on EMMA (both discussed below) also would not be established for transactions in such securities.

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21 The term "list offering price transaction" is defined as a primary market sale transaction executed on the first day of trading of a new issue "by a sole underwriter, syndicate manager, syndicate member, selling group member, or distribution participant [to a customer] at the published list offering price for the security." Rule G-14 RTRS Procedures (d)(vii)(A).

22 Under Rule G-32, on disclosures in connection with primary offerings, a dealer selling offered municipal securities generally must deliver to its customers a copy of the official statement by no later than the settlement of the transaction. Under Rule G-32(a)(iii), any dealer that satisfies the official statement delivery obligation by making certain submissions to EMMA in compliance with Rule G-32(a)(ii) must also provide to the customer, in connection with offered municipal securities sold by the issuer on a negotiated basis to the extent not included in the official statement, among other things, certain specified information about the underwriting arrangements, including the underwriting spread.

Proposed Information to be Disclosed on the Customer Confirmation

If the transaction meets the criteria described above, the dealer would be required to disclose on the customer confirmation the dealer's mark-up from the prevailing market price for the security. The mark-up would be required to be calculated in compliance with Rule G-30 and the supplementary material thereunder, including proposed Supplementary Material .06 (discussed below), and expressed as a total dollar amount and as a percentage of the prevailing market price of the municipal security.[23] The MSRB believes that it would be appropriate to require dealers to calculate the mark-up in compliance with Rule G-30, as new Supplementary Material .06 would provide extensive guidance on how to calculate the mark-up for transactions in municipal securities, including transactions for which disclosure would be required under the proposed rule change, and incorporates a presumption that prevailing market price is established by reference to contemporaneous cost or proceeds. While some commenters noted the operational cost and complexity of implementing a mark-up disclosure requirement, the MSRB notes that dealers are currently subject to Rule G-30, on prices and commissions, and already are required to evaluate the mark-ups that they charge to ensure that they are fair and reasonable.[24]

The MSRB recognizes that the determination of the prevailing market price of a particular security may not be identical across dealers.[25] Existing Rule G-30, however, requires dealers to exercise reasonable diligence in establishing the prevailing market price.[26] The MSRB, therefore, would expect that dealers have reasonable policies and

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23 Some commenters stated that the mark-up should be expressed as a total dollar amount, while others suggested that disclosure as a total dollar amount should not be required. Others still stated that the mark-up should be required to be disclosed as both a percentage and a total dollar amount. While commenters did not uniformly favor any particular format of disclosure, results of the joint investor survey indicated that investors found that disclosing the mark-up or mark-down both as a dollar amount and as a percentage of the prevailing market price would be more useful than only disclosing it in one of those forms.

24 Rule G-30, Supplementary Material .01(d).

25 For example, because the prevailing market price of a security is presumptively established by reference to the dealer's contemporaneous cost or proceeds, different dealers may arrive at different prevailing market prices for the same security depending on the price at which they contemporaneously acquired or sold such security. However, even where dealers may reasonably arrive at different prevailing market prices for the same security, the MSRB believes that the difference between such prevailing market price determinations would typically be small.

26 Rule G-30, Supplementary Material .04(b).

procedures in place to establish the prevailing market price and that such policies and procedures are applied consistently across customers.

The MSRB understands that some dealers provide confirmations on an intra-day basis. As explained in detail below in the context of the proposed amendments to Rule G-30, the proposed requirement to disclose a mark-up calculated "in compliance with" Rule G-30 (including the proposed prevailing market price guidance) need not delay the confirmation process. A dealer may determine, as a final matter for disclosure purposes, the prevailing market price based on the information the dealer has, based on the use of reasonable diligence as required by proposed amended Rule G-30, at the time of the dealer's generation of the disclosure.

The proposed rule change also would require the dealer to provide a reference and hyperlink to the Security Details page for a customer's security on EMMA, along with a brief description of the type of information available on that page. This disclosure requirement would be limited to transactions with retail (i.e., non-institutional) customers, but would apply for all such transactions regardless of whether a mark-up disclosure is required for the transaction.[27] The MSRB believes that such a link would provide retail investors with a broad picture of the market for a security on a given day and believes that requiring a link to EMMA would increase investors' awareness of, and ability to access, this information. Additionally, results from the joint investor survey support the value to investors of a security-specific link to EMMA, rather than a link to the EMMA homepage.[28] The MSRB believes that a link to EMMA or such other enhancements would not be sufficient, as customers are not always able to identify with certainty a principal trade in the same security that was made by that customer's dealer. As a result, the customer would not always be able to ascertain the exact amount of the price differential between the dealer and customer trade or to determine whether such a trade accurately reflects the "prevailing market price" for purposes of calculating the dealer's compensation.

The proposed rule change also would require the dealer to disclose on all customer confirmations, other than those for transactions in municipal fund securities, the time of execution. Dealers are already under an obligation to either disclose such information on the customer confirmation or to include a statement that the time of

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27 Because institutional customers typically have more ready access to the type of information available on EMMA, the MSRB is not proposing to require this disclosure for transactions with institutional customers. Of course, dealers are free to voluntarily provide such a disclosure on all customer confirmations, including those for institutional customers.

28 Some commenters stated that EMMA already contains sufficient pricing information for municipal securities, such as the last trade price for a security, and recommended that the MSRB focus solely on enhancing access to EMMA instead of requiring additional pricing disclosure.

execution will be furnished upon written request.[29] The proposed amendments to Rule G-15 would essentially delete the option to provide this information upon request. The MSRB believes that the provision of a security-specific link to EMMA on retail customer confirmations, together with the time of execution would provide retail customers a comprehensive view of the market for their security, including the market as of the time of their trade. This combined disclosure also would reduce the risk that a customer may overly focus on dealer compensation and not appropriately consider other factors relevant to the investment decision. Even in instances in which the mark-up would not be required to be disclosed to customers, the MSRB believes that the inclusion of the time of execution on all customer confirmations (retail and institutional) would increase market transparency at relatively low cost. Results from the joint investor survey support the MSRB's view that time of execution disclosure is valued by investors.

As noted above, if the Commission approves the proposed rule change, the MSRB will announce the effective date of the proposed rule change no later than 90 days following Commission approval. The effective date will be no later than 365 days following Commission approval.

Proposed Amendments to Rule G-30

The MSRB is proposing to add new supplementary material (paragraph .06 entitled "Mark-Up Policy") and amend existing supplementary material under MSRB Rule G-30, on prices and commissions, to provide guidance on establishing the prevailing market price and calculating mark-ups and mark-downs for principal transactions in municipal securities (the "proposed guidance" or "proposed prevailing market price guidance"). The MSRB believes additional guidance on these subjects would promote consistent compliance by dealers with their existing fair-pricing obligations under MSRB rules, in a manner that would be generally harmonized with the approach taken in other fixed income markets. The MSRB also believes that such guidance would support effective compliance with the proposed amendments to Rule G-15, discussed above. In addition, commenters indicated that compliance with the proposed amendments to MSRB Rule G-15 would be less burdensome if the MSRB were to provide guidance on establishing the prevailing market price. Significantly, municipal securities dealers that also transact in corporate or agency debt securities must comply with FINRA Rule 2121,

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[29] Dealers have an existing obligation to report "time of trade" to the Real-Time Transaction Reporting System pursuant to Rule G-14, on reports of sales or purchases. In addition, dealers have an existing obligation to make and keep records of the time of execution of principal transactions under Rule G-8(a)(vii). The time of execution for proposed confirmation disclosure purposes is the same as the time of trade for Rule G-14 reporting purposes and the time of execution for purposes of Rule G-8(a)(vii), except that dealers should omit all seconds from the disclosure because the trade data displayed on EMMA does not include seconds (e.g., dealers should disclose a time of trade of 10:00:59 as 10:00).

including Supplementary Material .02 ("FINRA guidance") for transactions in those securities.[30]

The proposed rule change also includes amendments to the Supplementary Material to Rule G-30. For example, the MSRB proposes to clarify in Supplementary Material .01(a) that a dealer must exercise "reasonable" diligence in establishing the market value of a security and the reasonableness of the compensation received. This requirement is consistent with existing Supplementary Material .04(b) ("[D]ealers must establish market value as accurately as possible using reasonable diligence under the facts and circumstances") and clarifies that the same standard applies under the Supplementary Material .01(a). Similarly, the proposed amendments to Supplementary Material .01(d) to Rule G-30 will clarify the relationship between that provision and the new proposed Supplementary Material .06 containing the proposed prevailing market price guidance. In addition, this provision will assist in understanding of the overall rule.

When a dealer acts in a principal capacity and sells a municipal security to a customer, the dealer generally "marks up" the security, increasing the total price the customer pays. Conversely, when buying a security from a customer, a dealer that is acting as a principal generally "marks down" the security, reducing the total proceeds the customer receives. Rule G-30(a) prohibits a dealer from engaging in a principal transaction with customers except at an aggregate price (including any mark-up or mark-down) that is fair and reasonable. The Supplementary Material to Rule G-30, among other things, provides that as part of the aggregate price to the customer, the mark-up or mark-down also must be a fair and reasonable amount, taking into account all relevant factors.[31]

A critical step in determining whether the mark-up or mark-down on a principal transaction with a customer and the aggregate price to such customer is fair and reasonable is correctly identifying the prevailing market price of the security. Currently, under Rule G-30, the total transaction price to the customer must bear a reasonable relationship to the prevailing market price of the security, and, in a principal transaction, the dealer's compensation must be computed from the inter-dealer market price prevailing at the time of the customer transaction.[32] Moreover, existing Rule G-30 requires dealers to exercise diligence in establishing the market value of the security and the reasonableness of their compensation.[33]

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30 See FINRA Rule 2121, Fair Prices and Commissions, Supplementary Material .02, Additional Mark-Up Policy For Transactions in Debt Securities, Except Municipal Securities.

31 Rule G-30, Supplementary Material .01(d).

32 Rule G-30, Supplementary Material .01(c), (d).

33 Rule G-30, Supplementary Material .01(a).

Under the proposed guidance, the prevailing market price of a municipal security generally would be presumptively established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained. This presumption could be overcome in limited circumstances. If the presumption is overcome, or if it is not applicable because the dealer's cost is (or proceeds are) not contemporaneous, various factors discussed below would be either required or permitted to be considered, in successive order, to determine the prevailing market price. Generally, a subsequent factor or series of factors could be considered only if previous factors in the hierarchy, or "waterfall," are inapplicable.

As described in greater detail below, the MSRB solicited comment on draft prevailing market price guidance in MSRB Notice 2016-07 (the "draft guidance"). The draft guidance was substantially similar to and generally harmonized with the FINRA guidance for non-municipal fixed income securities. As discussed below, the proposed guidance is substantially in the form of the draft guidance on which public comment was sought, with some minor changes. In addition, the MSRB provides additional explanation of the proposed guidance herein in response to commenters and to clearly express the MSRB's intended meaning of the proposed guidance. Moreover, the MSRB will continue to engage with FINRA with the goal of promoting generally harmonized interpretations of the proposed guidance, if approved, and the FINRA guidance, as applicable and to the extent appropriate in light of the differences between the markets.

Provided below is a more detailed description of each significant aspect of the proposed amendments to Rule G-30.

Rebuttable Presumption Based on Contemporaneous Costs or Proceeds

The proposed guidance builds on the standard in existing Supplementary Material to Rule G-30 that the prevailing market price of a security is generally the price at which dealers trade with one another (i.e., the inter-dealer price).[34] The proposed guidance provides that the best measure of prevailing market price is presumptively established by referring to the dealer's contemporaneous cost (proceeds), as consistent with other MSRB pricing rules, such as the best-execution rule (Rule G-18). Under the proposed guidance, a dealer's cost is (or proceeds are) considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the municipal security. The reference to dealer contemporaneous cost or proceeds in determining the prevailing market price reflects a recognition of the principle that the prices paid or received for a security by a dealer in actual transactions closely related in time are normally a highly reliable indication of the

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[34] See Rule G-30, Supplementary Material .01(d) ("Dealer 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.").

prevailing market price and that the burden is appropriately on the dealer to establish the contrary.

A dealer may look to other evidence of the prevailing market price (other than contemporaneous cost) only where the dealer, when selling the security, made no contemporaneous purchases in the municipal security or can show that in the particular circumstances the dealer's contemporaneous cost is not indicative of the prevailing market price. When buying a municipal security from a customer, the dealer may look to other evidence of the prevailing market price (other than contemporaneous proceeds) only where the dealer made no contemporaneous sales in the municipal security or can show that in the particular circumstances the dealer's contemporaneous proceeds are not indicative of the prevailing market price.

A dealer may be able to show that its contemporaneous cost (when it is making a sale to a customer) or proceeds (when it is making a purchase from a customer) are not indicative of the prevailing market price, and thus overcome the presumption, in instances where: (i) interest rates changed to a degree that such change would reasonably cause a change in municipal securities pricing; (ii) the credit quality of the municipal security changed significantly;[35] or (iii) news was issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the municipal security.[36]

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35 Consistent with FINRA statements with respect to other fixed income securities, although an announcement by a nationally recognized statistical rating organization ("NRSRO") that it has reviewed the issuer's credit and has changed the issuer's credit rating is an easily identifiable incidence of a change of credit quality, the category is not limited to such announcements. It may be possible for a dealer to establish that the issuer's credit quality changed in the absence of such an announcement; conversely, a relevant regulator may determine that the issuer's credit quality had changed and such change was known to the market and factored into the price of the municipal security before the dealer's transaction (the transaction used to measure the dealer's contemporaneous cost) occurred. See Exchange Act Release No. 54799 (Nov. 21, 2006); 71 FR 68856 (Nov. 28, 2006) (FINRA Notice of Filing of Amendments Related to Mark-Up Policy).

36 Consistent with FINRA statements with respect to other fixed income securities, certain news affecting an issuer, such as news of legislation, may affect either a particular issuer or a group or sector of issuers and may not clearly fit within the two previously identified categories – interest rate changes and credit quality changes. Such news may cause price shifts in a municipal security, and could, depending on the facts and circumstances, invalidate the use of the dealer's own contemporaneous cost as a reliable and accurate measure of prevailing market price. See id.

Hierarchy of Pricing Factors. Under the proposed guidance, if the dealer has established that the dealer's cost is (or proceeds are) not contemporaneous or if the dealer has overcome the presumption that its contemporaneous cost or amount of proceeds provides the best measure of the prevailing market price, the dealer must consider, in the order listed (subject to Supplementary Material .06(a)(viii), on isolated transactions and quotations), a hierarchy of three additional types of pricing information, referred to here as the hierarchy of pricing factors: (i) prices of any contemporaneous inter-dealer transactions in the municipal security; (ii) prices of contemporaneous dealer purchases (or sales) in the municipal security from (or to) institutional accounts with which any dealer regularly effects transactions in the same municipal security; or (iii) if an actively traded security, contemporaneous bid (or offer) quotations for the municipal security made through an inter-dealer mechanism, through which transactions generally occur at the displayed quotations. Pricing information of a succeeding type may only be considered where the prior type does not generate relevant pricing information. In reviewing the available pricing information of each type, the relative weight of the information depends on the facts and circumstances of the comparison transaction or quotation. The proposed guidance also makes clear the expectation that, because of the lack of active trading in many municipal securities, these factors may frequently not be available in the municipal market. Accordingly, dealers may often need to consult factors further down the waterfall, such as "similar" securities and economic models, to identify sufficient relevant and probative pricing information to establish the prevailing market price of a municipal security.

Similar Securities. If the above factors are not available, the proposed guidance provides that the dealer may take into consideration a non-exclusive list of factors that are generally analogous to those set forth under the hierarchy of pricing factors, but applied here to prices and yields of specifically defined "similar" securities. However, unlike the factors set forth in the hierarchy of pricing factors, which must be considered in the specified order, the factors related to similar securities are not required to be considered in a particular order or particular combination. The non-exclusive factors specifically listed are:

- Prices, or yields calculated from prices, of contemporaneous inter-dealer transactions in a specifically defined "similar" municipal security;

- Prices, or yields calculated from prices, of contemporaneous dealer purchase (sale) transactions in a "similar" municipal security with institutional accounts with which any dealer regularly effects transactions in the "similar" municipal security with respect to customer mark-ups (mark-downs); and

- Yields calculated from validated contemporaneous inter-dealer bid (offer) quotations in "similar" municipal securities for customer mark-ups (mark-downs").

When applying one or more of the factors, a dealer would be required to consider that the ultimate evidentiary issue is whether the prevailing market price of the

municipal security will be correctly identified. As stated in the proposed guidance, the relative weight of the pricing information obtained from the factors depends on the facts and circumstances surrounding the comparison transaction, such as whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction, the timeliness of the information and, with respect to the final bulleted factor above, the relative spread of the quotations in the "similar" municipal security to the quotations in the subject security. As noted below, regarding isolated transactions generally, in considering yields of "similar" securities, except in extraordinary circumstances, dealers may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" municipal securities taken as a whole.

The proposed guidance provides that a "similar" municipal security should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor. At a minimum, the municipal security or securities should be sufficiently similar that a market yield for the subject security can be fairly estimated from the yields of the "similar" security or securities. Where a municipal security has several components, appropriate consideration may also be given to the prices or yields of the various components of the security. The proposed guidance also sets forth a number of non-exclusive factors that may be used in determining the degree to which a security is "similar." These include: (i) credit quality considerations;[37] (ii) the extent to which the spread at which the "similar" municipal security trades is comparable to the spread at which the subject security trades; (iii) general structural characteristics and provisions of the issue;[38] (iv) technical factors such as the size of the issue, the float and recent turnover of the issue, and legal restrictions on transferability as compared with the subject security; and (v) the extent to which the federal and/or state tax treatment of the "similar" municipal security is comparable to such tax treatment of the subject security.

Because of the unique characteristics of the municipal securities market, including the large number of vastly different issuers and the highly diverse nature of most outstanding securities, the MSRB expects that, in order for a security to qualify as sufficiently "similar" to the subject security, such security will be at least highly similar

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37 Credit quality considerations include, but are not limited to, whether the municipal security is issued by the same or similar entity, bears the same or similar credit rating, or is supported by a similarly strong guarantee or collateral as the subject security (to the extent securities of other issuers are designated as "similar" securities, significant recent information concerning either the "similar" security's issuer or subject security's issuer that is not yet incorporated in credit ratings should be considered (e.g., changes to ratings outlooks)).

38 General structural characteristics and provisions of the issue include, but are not limited to, coupon, maturity, duration, complexity or uniqueness of the structure, callability, the likelihood that the municipal security will be called, tendered or exchanged, and other embedded options, as compared with the characteristics of the subject security.

to the subject security with respect to nearly all of the listed "similar" security factors that are relevant to the subject security at issue. The MSRB believes that this recognition of a practical aspect of the municipal securities market supports a more rational comparison of a municipal security to only those that are likely to produce relevant and probative pricing information in determining the prevailing market price of the subject security. Pricing information, for example, for a taxable security will not be useful in evaluating a tax-exempt security without making some price adjustment for that difference, which would constitute a form of economic modeling that is not permitted except at the next level of the waterfall analysis. The same is true, just as additional examples, of a bond versus another with a different credit rating, a general obligation bond versus a revenue bond, a bond with bond insurance versus one without, a bond with a sinking fund versus one without, and a bond with a call provision versus one without. As a result of these practical aspects, and due also in part to the lack of active trading in many municipal securities, dealers in the municipal securities market likely may not often find pricing information from sufficiently similar securities and may frequently need to then consider economic models at the next level of the waterfall analysis.

When a security's value and pricing is based substantially on, and is highly dependent on, the particular circumstances of the issuer, including creditworthiness and the ability and willingness of the issuer to meet the specific obligations of the security (often referred to as "story bonds"), in most cases other securities would not be sufficiently similar, and therefore, other securities may not be used to establish the prevailing market price.

Economic Models. If information concerning the prevailing market price of a security cannot be obtained by applying any of the factors at the higher levels of the waterfall, dealers may consider as a factor in assessing the prevailing market price of a security the prices or yields derived from economic models. Such economic models may take into account measures such as reported trade prices, credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value, and may consider all applicable pricing terms and conventions used.[39]

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[39] Consistent with FINRA's commentary with respect to other fixed income securities, when a dealer seeks to identify prevailing market price using other than the dealer's contemporaneous cost or contemporaneous proceeds, the dealer must be prepared to provide evidence that would establish the dealer's basis for not using contemporaneous cost (proceeds), and information about the other values reviewed (e.g., the specific prices and/or yields of securities that were identified as similar securities) in order to determine the prevailing market price of the subject security. If a dealer relies upon pricing information from a model the dealer uses or has developed, the dealer must be able to provide information that was used on the day of the transaction to develop the pricing information (i.e., the data that was input and the data that the model generated and the dealer used to arrive at prevailing market price). See supra n. 35, FINRA Notice of Filing of Amendments Related to Mark-Up Policy.

Isolated Transactions and Quotations. The ultimate issue the proposed guidance is intended to address is the prevailing market price of the security; therefore, isolated transactions or isolated quotations generally would have little or no weight or relevance in establishing the prevailing market price. Due to the unique nature of the municipal securities market, including the large number of issuers and outstanding securities and the infrequent trading of many securities in the secondary market, the proposed guidance recognizes that isolated transactions and quotations may be more prevalent in the municipal securities market than other fixed income markets and explicitly recognizes that an off-market transaction may qualify as an "isolated transaction" under the proposed guidance.

The proposed guidance also addresses the application of the "isolated" transactions and quotations provision. The proposed guidance explains that, for example, in considering the factors in the hierarchy of pricing factors, a dealer may give little or no weight to pricing information derived from an isolated transaction or quotation. The proposed guidance also provides that, in considering yields of "similar" securities, except in extraordinary circumstances, dealers may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" municipal securities taken as a whole.

Contemporaneous Customer Transactions

Because the proposed guidance ultimately seeks to identify the prevailing inter-dealer market price, a dealer's contemporaneous cost (for customer sales) or proceeds (for customer purchases) in an *inter-dealer* transaction is presumptively the prevailing market price of the security. Where the dealer has no contemporaneous cost or proceeds, as applicable, from an inter-dealer transaction, the dealer must then consider whether it has contemporaneous cost or proceeds, as applicable, from a *customer* transaction. In establishing the presumptive prevailing market price, in such instances, the dealer should refer to such contemporaneous cost or proceeds and make an adjustment for any mark-up or mark-down charged in that customer transaction. This methodology for establishing the presumptive prevailing market price is appropriate because, as explained in the relevant case law, it reflects the fact that the price at which a dealer, for example, purchases securities from customers generally is less than the amount that the dealer would have paid for the security in the inter-dealer market. To identify the prevailing market price for the purpose of calculating the mark-up or mark-down in the contemporaneous customer transaction, the dealer should proceed down the waterfall, according to its terms, identifying the most relevant and probative evidence of the prevailing inter-dealer market price.

This approach is supported by the relevant case law, in which the prevailing market price has been established by reference to a customer price by adjusting the

customer price based on an "imputed" mark-up or mark-down.[40] This approach is also consistent with the text of the proposed guidance because the presumptive prevailing market price is, through this methodology, established "by referring to" the dealer's contemporaneous cost or proceeds, as required by proposed Supplementary Material .06(a)(i).[41] Moreover, this approach is consistent with the fundamental principle underlying the proposed guidance, because it results in a reasonable proxy for what the dealer's contemporaneous cost or proceeds would have been in an inter-dealer transaction. Indeed, because this adjustment methodology occurs at the first step of the waterfall analysis (proposed Supplementary Material .06(a)(i)), the resulting price from this methodology is presumed to be the prevailing market price for any contemporaneous transactions with the same strength of the presumption that applies to prices from inter-dealer transactions.

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[40] In a number of instances, where a dealer lacked contemporaneous inter-dealer transactions, the prevailing market price in connection with a sale to a customer was calculated by identifying contemporaneous cost from a transaction with another customer and then making an upward adjustment. The adjustment, referred to in the cases as an "imputed markdown," was then added to the dealer's purchase price from the customer to establish pricing at the level at which an inter-dealer trade might have occurred. Similarly, in determining the prevailing market price of a municipal security in connection with a purchase from a customer, the prevailing market price was determined by identifying the dealer's contemporaneous proceeds in a transaction with another customer, and then making a downward adjustment by deducting an "imputed mark-up" from such contemporaneous proceeds.

[41] For example, assume that Dealer A sells municipal security X to Dealer B at a price of 98.5. Then, assume that Dealer C purchases municipal security X from a customer at a price of 98 and contemporaneously sells the security to a customer at a price of 100. Because Dealer C itself has no other contemporaneous transactions in the security, it would proceed down the waterfall to the hierarchy of pricing factors, discussed supra. A dealer at that level of the waterfall analysis must first consider prices of any contemporaneous inter-dealer transaction in establishing the prevailing market price. Accordingly, Dealer C would consider the contemporaneous inter-dealer transaction between Dealer A and Dealer B at 98.5 in determining the amount of the mark-down, and deduct its contemporaneous cost of 98 from 98.5 to arrive at a mark-down of 0.5. Then, Dealer C would add the amount of the mark-down to the dealer's contemporaneous cost for a presumptive prevailing market price (or adjusted contemporaneous cost) of 98.5. In the absence of evidence to rebut the presumption, when disclosing the mark-up to the customer to whom Dealer C sold municipal security X, Dealer C would then disclose the difference between Dealer C's adjusted contemporaneous cost (98.5) and the price paid by the customer to whom Dealer C sold municipal security X (100) for a mark-up of 1.5 (1.02% of the prevailing market price).

This interpretation of the proposed prevailing market price guidance takes on special significance in the context of a mark-up disclosure requirement, such as contained in the proposed amendments to Rule G-15. Where, for example, a dealer purchases a security from one retail customer and contemporaneously sells it to another retail customer, with no relevant market changes in the interim, the total difference between the two prices may be attributed to dealer compensation, but each customer pays only a portion of this difference (as either a mark-up or a mark-down). Without adjustments to the contemporaneous cost and proceeds based on the mark-down and mark-up, respectively, the confirmation disclosures to both customers would reflect "double counting." By contrast, under the adjustment approach, where there are no relevant market changes in the interim that would rebut the presumption, there is a complete apportionment of the total difference in price (i.e., no double counting and no part of the total difference in price left undisclosed to either customer).

Non-Arms-Length Affiliate Transactions. The ultimate issue the proposed guidance is intended to address is the prevailing market price of the security, using the most relevant and probative evidence of the market price in the inter-dealer market. Therefore, as noted in the discussion above of the mark-up disclosure requirement, a non-arms-length transaction in a security (as defined in that context) with an affiliate should not be used to identify a dealer's contemporaneous cost or proceeds and presumptively the prevailing market price of the security. The MSRB believes that, for example, sourcing liquidity through a non-arms-length transaction with an affiliate is functionally equivalent to selling out of a dealer's own inventory for purposes of the calculation of the mark-up. The MSRB therefore believes it would be appropriate in those circumstances to require a dealer to "look through" its transaction in a security with its affiliate to the affiliate's transaction(s) in the security with third parties and the related time of trade and cost or proceeds of the affiliate in determining the dealer's calculation of the mark-up pursuant to Rule G-30. This is the case not only for transactions for which mark-up disclosure would be required under the proposed amendments to Rule G-15, but for the application of proposed amended Rule G-30 generally, including the proposed prevailing market price guidance, for purposes of evaluating the fairness and reasonableness of mark-ups and mark-downs.[42]

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[42] For example, assume Dealer A1, a market-facing dealer, and Dealer A2, a retail customer-facing dealer, are affiliates both owned by Company A. On the same trading day, Dealer A1 purchases municipal security X from an unaffiliated dealer at $90 ("Transaction 1"). Dealer A1 displays municipal security X for sale at $93 on Dealer A2's customer-facing platform, on which other dealers have not frequently participated. A retail customer places an order to purchase municipal security X from Dealer A2 at the displayed price of $93. Dealer A2 purchases municipal security X from Dealer A1 at $93 in a non-arms-length transaction within the meaning of proposed amended Rule G-15 ("Transaction 2"). Dealer A2 then sells municipal security X to the retail customer at $93, plus $1 trading fee ("Transaction 3"). During the day, there are no other transactions in municipal security X and no other dealers display any price for municipal security X. In this

Compliance at the Time of Generation of Disclosure. As noted, the MSRB understands that some dealers provide confirmations on an intra-day basis. The requirement under the proposed amendments to Rule G-15 to disclose a mark-up or mark-down calculated "in compliance with" Rule G-30 (including the proposed prevailing market price guidance) need not delay the confirmation process. A dealer may determine, as a final matter for disclosure purposes, the prevailing market price based on the information the dealer has, based on the use of reasonable diligence as required by proposed amended Rule G-30, at the time the dealer inputs the information into its systems to generate the mark-up disclosure.[43] Such timing of the determination of prevailing market price would avoid potentially open-ended delays that could otherwise result if dealers were required to wait to generate a disclosure until they could determine, for example, that they do not have any "contemporaneous" proceeds for a particular transaction. Such timing would also permit dealers who, on a voluntary basis, choose to disclose mark-ups and mark-downs on all principal transactions to generate customer confirmations at the time of trade, should they choose to do so. To clarify, a dealer would not be expected to cancel and resend a confirmation to revise the mark-up or mark-down disclosure solely based on the occurrence of a subsequent transaction or event that would otherwise be relevant to the calculation of the mark-up or mark-down under the proposed guidance. Where, however, a dealer has contemporaneous proceeds by the time of

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example, Transaction 2 should not be used to indicate Dealer A2's contemporaneous cost. Instead, Dealer A2 would be required to "look through" Transaction 2, a non-arm's length transaction with affiliated Dealer A1, and use Transaction 1 and the time of that trade and the related cost to Dealer A1 in determining the prevailing market price.

43 For example, assume Dealer A systematically inputs the mark-up-related information into its sytems intra-day for the generation of confirmations. At 9:00 AM, Dealer A purchases municipal security X from a customer at a price of 98. At 1:00 PM, Dealer A sells such security to another dealer at a price of 100. Dealer A does not sell municipal security X at any other time before 1:00 PM. At the time of the 9:00 AM transaction, Dealer A does not have any contemporaneous proceeds for municipal security X. Therefore, to determine the prevailing market price for municipal security X, Dealer A would proceed down the waterfall to the next category of factors—in this case, the hierarchy of pricing factors, as discussed supra. Dealer A would not be required to consider the price of 100, which the dealer would only know at 1:00 PM. In contrast, assuming instead that Dealer A systematically inputs the mark-up-related information into its sytems for confirmation generation at the end of the day, under the same facts as above, it would be required to consider, to the extent required by the prevailing market price guidance, the 1:00 PM inter-dealer trade price in determining the prevailing market price and the related mark-down to be disclosed for the 9:00 AM purchase.

generation of the disclosure, the dealer presumptively must establish the prevailing market price of the municipal security by reference to such contemporaneous proceeds.[44]

Consideration of Benefits and Costs

The MSRB believes that requiring dealers to disclose their mark-ups on retail customer confirmations based on the proposed amendments to Rule G-30 would provide meaningful and useful pricing information to a significant number of retail investors and may lower transaction costs for retail transactions. The MSRB also believes that the proposed amendments would provide retail customers engaged in municipal securities transactions covered by the rule with information more comparable to that currently received by retail customers in equity securities transactions and municipal securities transactions in which the dealer acts in an agent capacity. In addition, the disclosure may improve investor confidence, better enable customers to evaluate the costs and quality of the execution service that dealers provide, promote transparency into dealers' pricing practices, improve communication between dealers and their customers, and make the enforcement of Rule G-30 more efficient.

The MSRB believes that the proposed amendments to Rule G-30 reflect an appropriate balance between consistency with existing FINRA guidance for determining prevailing market price in other fixed income securities markets and modifications to address circumstances under which use of the FINRA guidance in the municipal securities market might be inappropriate (e.g., treatment of similar securities).[45] The MSRB also believes that the guidance would promote consistent compliance by dealers with their existing fair-pricing obligations under MSRB rules and would support effective compliance with the proposed amendments to Rule G-15.

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44 For example, a dealer that operates an alternative trading system or ATS may often, if not always, be in a position to identify its contemporaneous proceeds in connection with a purchase from a customer. Also, as discussed in supra n. 18, under Rule G-18, Supplementary Material .03, a dealer must make every effort to execute a customer transaction promptly, taking into account prevailing market conditions. Any intentional delay of a transaction to avoid recognizing proceeds as contemporaneous at the time of a transaction or otherwise would be contrary to these duties to customers. A dealer found to purposefully delay the execution of a customer order for such purposes also may be in violation of Rule G-17, on conduct of municipal securities and municipal advisory activities.

45 For example, the municipal securities market includes a larger number of issuers and larger number of outstanding securities than the corporate bond market, and most municipal securities trade less frequently in the secondary market. In addition, many municipal securities are subject to different tax rules and treatment, and have different credit structures, enhancements and redemption features that may not be applicable to or prevalent for other fixed income securities.

The MSRB recognizes, however, that the proposed rule change, comprised of amendments to both Rule G-15 and Rule G-30, would impose burdens and costs on dealers.[46] In MSRB Notices 2014-20, 2015-16 and 2016-07, the MSRB specifically solicited comment on the potential costs of the draft amendments contained in those notices. While commenters stated that the initial and the revised confirmation disclosure proposals would impose significant implementation costs, no commenters provided specific cost estimates, data to support cost estimates, or a framework to assess anticipated costs.

Among other things, the proposed rule change would require dealers to develop and deploy a methodology to satisfy the disclosure requirement, identify trades subject to the disclosure, convey the mark-up on the customer confirmation, determine the prevailing market price and the mark-up, and adopt policies and procedures to track and ensure compliance with the requirement. To apply the "look through" to non-arms-length transactions with affiliates, dealers also would need to obtain the price paid or proceeds received and the time of the affiliate's trade with the third party. The MSRB sought data in the above-referenced notices that would facilitate quantification of these costs, but did not receive any data from commenters.

Any such costs, however, may be mitigated under certain circumstances. Dealers choosing to provide disclosure on all customer transactions would not incur the cost associated with identifying trades subject to the disclosure requirement; dealers already disclosing mark-ups to retail customers likely would incur lower costs associated with modifying customer confirmations, and dealers with processes in place to evaluate prevailing market price in compliance with FINRA Rule 2121 and MSRB Rule G-30 may be able to leverage those processes to comply with the proposed amendments to Rule G-30.

Based on comments received in response to the Notices, the MSRB made a number of changes to the draft amendments in an effort to make implementation less burdensome. These changes include utilizing existing processes for identifying retail customers, providing detailed prevailing market price guidance alongside the mark-up disclosure proposal, and ensuring that prevailing market price could be determined in the least burdensome way among the reasonable alternatives.

The MSRB believes that the proposed rule change reflects the overall lowest cost approach to achieving the regulatory objective. To reach that conclusion, the MSRB

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46 The MSRB's evaluation of the potential costs does not consider all of the costs associated with the proposal, but instead focuses on the incremental costs attributable to it that exceed the baseline state. The costs associated with the baseline state are, in effect, subtracted from the costs associated with the proposed rule change to isolate the costs attributable to the incremental requirements of the proposal.

evaluated several reasonable regulatory alternatives including relying solely on modifications to EMMA, requiring the disclosure of a "reference price" rather than mark-up, and providing only a mark-up disclosure rule without accompanying prevailing market price guidance. These alternatives were deemed to either not sufficiently address the identified need (in the case of the EMMA alternative) or to represent approaches that offered lesser benefits and greater costs.

(b) Statutory Basis

The MSRB believes that the proposed rule change is consistent with the provisions of Section 15B(b)(2)(C) of the Act,[47] which provides that the MSRB's rules shall:

> be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2)(C) of the Act[48] because it would provide retail customers with meaningful and useful additional pricing information that retail customers typically cannot readily obtain through existing data sources such as EMMA. This belief is supported by the joint investor testing, which indicated that investors would find aspects of the proposed requirements useful, including disclosure of the time of execution and mark-up or mark-down in a municipal securities transaction both as a dollar amount and as a percentage of the prevailing market price. The MSRB believes that a reference and hyperlink to the Security Details page of EMMA, along with a brief description of the type of information available on that page, will provide retail investors with a more comprehensive picture of the market for a security on a given day and believes that requiring a link to EMMA would increase investors' awareness of, and ability to access, this information. Additionally, results from the joint investor survey support the value to investors of a security-specific link to EMMA, rather than a link to the EMMA homepage. The MSRB believes that the proposed rule change will better enable customers to evaluate the cost of the services that dealers provide by helping customers understand mark-ups or mark-downs from the prevailing market prices in specific transactions. The MSRB also believes that this type of information will promote transparency into dealers' pricing practices and encourage communications between dealers and their customers about the execution of their municipal securities transactions. The MSRB further believes the

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47 15 U.S.C. 78o-4(b)(2)(C).

48 Id.

proposed rule change will provide customers with additional information that may assist them in detecting practices that are possibly improper, which would supplement existing municipal securities enforcement programs.

The proposed amendment to Supplementary Material .01(a) to Rule G-30 will clarify the applicable "reasonable diligence" standard in that provision and conform to existing supplementary material referencing that standard. The proposed amendments to Supplementary Material .01(d) to Rule G-30 will clarify the relationship between that provision and the new proposed Supplementary Material .06 containing the proposed prevailing market price guidance and aid in understanding of the overall rule.

The proposed guidance on prevailing market price will provide dealers with additional guidance for determining prevailing market price in order to aid in compliance with their fair-pricing and mark-up disclosure obligations. The MSRB believes that clarifying the standard for correctly identifying the prevailing market price of a municipal security for purposes of calculating a mark-up, clarifying the additional obligations of a dealer when it seeks to use a measure other than the dealer's own contemporaneous cost (proceeds) as the prevailing market price and confirming that similar securities and economic models may be used in certain instances to determine the prevailing market price are measures designed to remove impediments to and perfect the mechanism of a free and open market in municipal securities, prevent fraudulent practices, promote just and equitable principles of trade and protect investors and the public interest.

4. Self-Regulatory Organization's Statement on Burden on Competition

Section 15B(b)(2)(C)[49] of the Act requires that MSRB rules not be designed to impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

The MSRB believes that the proposed rule change will improve price transparency and foster greater price competition among dealers. The MSRB recognizes that some dealers may exit the market or consolidate with other dealers as a result of the costs associated with the proposed rule change relative to the baseline. However, the MSRB does not believe—and is not aware of any data that suggest—that the number of dealers exiting the market or consolidating would materially impact competition.

Some commenters noted that the requirement to make a disclosure to retail customers if the dealer engaged in both the retail customer's transaction and one or more offsetting transactions on the same day could disproportionately impact smaller dealers as larger dealers might be more able to hold positions overnight and not trigger the proposed disclosure requirement. The MSRB has noted that any intentional delay of a customer execution to avoid a disclosure requirement would be contrary to a dealer's obligations under Rules G-30, G-18, on best execution, and G-17, on conduct of municipal securities and municipal advisory activities. If the proposed amendments are approved, the MSRB

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[49] Id.

expects that FINRA would monitor trading patterns to ensure dealers are not purposely delaying a customer execution to avoid the disclosure.

Although commenters did not provide any data to support a quantification of the costs associated with these proposals, commenters did indicate that the costs associated with modifying systems to comply with these proposals would be significant. It is possible that larger dealers may be better able to absorb these costs than smaller dealers and that smaller dealers could be forced to exit the market or pass a larger share of the implementation costs on to customers. The MSRB believes that these concerns may be mitigated by several factors. As noted above, dealers choosing to disclose to all customers may not incur the costs associated with identifying transactions that require disclosure and dealers engaging in relatively fewer transactions may be able to develop processes for determining prevailing market price that are relatively less costly than larger, more active dealers. In addition, the MSRB believes that smaller dealers are more likely to have their customer confirmations generated by clearing firms. To the extent that clearing firms would not pass along the full implementation cost to each introducing firm, small firms may incur lower costs in certain areas than large firms.

The proposed rule change may disproportionately impact less active dealers that, as indicated by data, currently charge relatively higher mark-ups than more active dealers. However, overall, the MSRB believes that the burdens on competition will be limited and the proposed rule change will not impose any additional burdens on competition that are not necessary or appropriate in furtherance of the purposes of the Act. In addition, the MSRB believes that the proposed rule change may foster additional price competition.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Proposed Amendments to Rule G-15

The revised confirmation disclosure proposal was published for comment in MSRB Notice 2015-16 (September 24, 2015), and was preceded by the initial confirmation disclosure proposal in MSRB Notice 2014-20 (November 17, 2014). The MSRB received 30 comments in response to MSRB Notice 2014-20,[50] and 25 comments

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50 See Letter from Eric Bederman, Chief Operating and Compliance Officer, Bernardi Securities, dated December 26, 2014 ("Bernardi Letter I"); Letter from Michael Nicholas, Chief Executive Officer, Bond Dealers of America, dated January 20, 2015 ("BDA Letter I"); Letter from Chris Melton, Executive Vice President, Coastal Securities, dated January 16, 2015 ("Coastal Securities Letter I"); Letter from Micah Hauptman, Financial Services Counsel, Consumer Federation of America, dated January 20, 2015 ("CFA Letter I"); Letter from Larry E. Fondren, President and Chief Executive Officer, DelphX LLC, dated January 7, 2015 ("DelphX Letter I"); Letter from Herbert Diamant, President, Diamant Investments Corp., dated January 9, 2015 ("Diamant Letter I"); Letter

in response to MSRB Notice 2015-16.[51] A copy of MSRB Notice 2014-20 is attached as Exhibit 2a; a list of comment letters received in response is attached as Exhibit 2b; and

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from Norman L. Ashkenas, Chief Compliance Officer, Fidelity Brokerage Services LLC and Richard J. O'Brien, Chief Compliance Officer, National Financial Services, LLC, Fidelity Investments, dated January 20, 2015 ("Fidelity Letter I"); Letter from Darren Wasney, Program Manager, Financial Information Forum, dated January 20, 2015 ("FIF Letter I"); Letter from David T. Bellaire, Executive Vice President and General Counsel, Financial Services Institute, dated January 20, 2015 ("FSI Institute Letter I"); Letter from Rich Foster, Vice President and Senior Counsel for Regulatory and Legal Affairs, Financial Services Roundtable, dated January 20, 2015 ("Financial Services Roundtable Letter I"); Emails from Gerald Heilpern, dated December 9, 2014, December 18, 2014 and January 8, 2015 (collectively "Heilpern Letter I"); Letter from Alexander I. Rorke, Senior Managing Director, Municipal Securities Group, Hilliard Lyons, dated January 20, 2015 ("Hilliard Letter I"); Letter from Thomas E. Dannenberg, President and Chief Executive Officer, Hutchinson Shockey Erley and Co., dated January 20, 2015 ("Hutchinson Shockey Letter I"); Letter from Andrew Hausman, President, Pricing & Reference Data, Interactive Data, dated January 20, 2015 ("Interactive Data Letter I"); Email from John Smith, dated December 10, 2014 ("Smith Letter I"); Email from Jorge Rosso, dated November 24, 2014 ("Rosso Letter I"); Letter from Karin Tex, dated January 12, 2015 ("Tex Letter I"); Email from George J. McLiney, Jr., McLiney and Company, dated December 22, 2014 ("McLiney Letter I"); Letter from Vincent Lumia, Managing Director, Morgan Stanley Smith Barney LLC, dated January 20, 2015 ("Morgan Stanley Letter I"); Letter from Peter G. Brandel, Senior Vice President, Municipal Bond Trading, and Kenneth T. Kerr, Senior Vice President, Municipal Bond Trading, Nathan Hale Capital, LLC, dated January 20, 2015 ("Nathan Hale Letter I"); Letter from Rick A. Fleming, Investor Advocate, Office of the Investor Advocate, U.S. Securities and Exchange Commission, dated January 20, 2015 ("SEC Investor Advocate Letter I"); Email from Private Citizen, dated November 23, 2014 ("Private Citizen Letter I"); Letter from Richard Seelaus, R. Seelaus & Co., Inc., dated January 8, 2015 ("R. Seelaus Letter I"); Email from Paige Pierce, RW Smith & Associates, LLC, dated January 21, 2015 ("RW Smith Letter I"); Letter from Sean Davy, Managing Director, Capital Markets Division, and David L. Cohen, Managing Director and Associate General Counsel, Municipal Securities Division, Securities Industry and Financial Markets Association, dated January 20, 2015 ("SIFMA Letter I"); Letter from Gregory Carlin, Vice President, Standard & Poor's Securities Evaluations, Inc., dated January 20, 2015 (S&P Letter I"); Letter from Kyle C. Wootten, Deputy Director – Compliance and Regulatory, Thomson Reuters, dated January 16, 2015 ("Thomson Reuters Letter I"); Letter from Robert J. McCarthy, Director of Regulatory Policy, Wells Fargo Advisors, LLC, dated January 20, 2015 ("Wells Fargo Letter I").

[51] See Email from Aaron Botbyl, dated October 9, 2015 ("Botbyl Letter II"); Letter from Eric Bederman, Senior Vice President, Chief Operating and Compliance

Officer, Bernardi Securities, Inc., dated December 4, 2015 (“Bernardi Letter II”); Letter from Michael Nicholas, Chief Executive Officer, Bond Dealers of America, dated December 11, 2015 (“BDA Letter II”); Letter from Kurt N. Schacht, Managing Director, Standards and Financial Market Integrity, and Linda L. Rittenhouse, Director, Capital Markets Policy, CFA Institute, dated December 11, 2015 (“CFA Institute Letter II”); Letter from Jason Clague, Senior Vice President, Trading & Middle Office Services, Charles Schwab & Co. Inc., dated December 11, 2015 (“Schwab Letter II”); Email from Chris Melton, Coastal Securities, dated October 30, 2015 (“Coastal Securities Letter II”); Email from Christopher [Last Name Withheld], dated September 25, 2015 (“Christopher Letter II”); Letter from Micah Hauptman, Financial Services Counsel, Consumer Federation of America, dated December 11, 2015 (“CFA Letter II”); Letter from Herbert Diamant, President, Diamant Investment Corporation, dated November 30, 2015 (“Diamant Letter II”); Letter from Norman L. Ashkenas, Chief Compliance Officer, Fidelity Brokerage Services, LLC, and Richard J. O’Brien, Chief Compliance Officer, National Financial Services, LLC, Fidelity Investments, dated December 11, 2015 (“Fidelity Letter II”); Letter from Darren Wasney, Program Manager, Financial Information Forum, dated December 11, 2015 (“FIF Letter II”); Letter from David T. Bellaire, Executive Vice President & General Counsel, Financial Services Institute, dated December 11, 2015, (“FSI Institute Letter II”); Letter from Gerald Heilpern, undated (“Heilpern Letter II”); Email from Jonathan Bricker, dated October 20, 2015; Letter from David P. Bergers, General Counsel, LPL Financial LLC, dated December 10, 2015 (“LPL Letter II”); Letter from Elizabeth Dennis, Managing Director, Morgan Stanley Smith Barney LLC, dated December 11, 2015 (“Morgan Stanley Letter II”); Letter from Rick A. Fleming, Investor Advocate, Office of the Investor Advocate, U.S. Securities and Exchange Commission, dated December 11, 2015 (“SEC Investor Advocate Letter II”); Letter from Patrick Luby, dated December 11, 2015 (“Luby Letter II”); Letter from Hugh D. Berkson, President, Public Investors Arbitration Bar Association, dated December 8, 2015 (“PIABA Letter II”); Letter from David L. Cohen, Senior Counsel and Director, RBC Capital Markets, LLC, dated December 15, 2015 (“RBC Letter II”); Letter from Paige W. Pierce, President & Chief Executive Officer, RW Smith and Associates, LLC, dated December 11, 2015 (“RW Smith Letter II”); Letter from Sean Davy, Managing Director, Capital Markets Division, and Leslie M. Norwood, Managing Director & Associate General Counsel, Municipal Securities Division, Securities Industry and Financial Markets Association, dated December 11, 2015 (“SIFMA Letter II”); Letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, Thomson Reuters, dated December 11, 2015 (“Thomson Reuters Letter II”); Letter from Thomas S. Vales, Chief Executive Officer, TMC Bonds LLC, dated December 11, 2015 (“TMC Bonds Letter II”); Letter from Robert J. McCarthy, Director of Regulatory Policy, Wells Fargo Advisors LLC, dated December 11, 2015 (“Wells Fargo Letter II”).

copies of the comment letters are attached as Exhibit 2c. A copy of MSRB Notice 2015-16 is attached as Exhibit 2d; a list of comment letters received in response is attached as Exhibit 2e; and copies of the comment letters are attached as Exhibit 2f.

Summary of Initial Confirmation Disclosure Proposal and Comments Received

As proposed in MSRB Notice 2014-20, for same-day principal transactions in municipal securities, dealers would have been required 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. The initial proposal would have applied where the transaction with the customer involved 100 bonds or fewer or bonds in a par amount of $100,000 or less, which was designed to capture those trades that are retail in nature.

Of the 30 comments the MSRB received on the proposal, six supported the proposal, while 24 commenters generally opposed the proposal or made recommendations on ways to narrow substantially the scope of the proposal. Generally, commenters that supported the proposal stated that the proposed confirmation disclosure would provide additional post-trade information to investors that would be otherwise difficult to ascertain.[52] Three commenters, including the Consumer Federation of America and the SEC Investor Advocate, stated that this additional information would put investors in a better position to assess whether they are paying fair prices and the quality of the services provided by their dealer, and also could assist investors in detecting improper practices.[53] The Consumer Federation of America indicated that the proposal would foster increased price competition in fixed income markets, which would ultimately lower investors' transaction costs.[54] Two commenters recommended that the proposal not be limited to retail trades under the proposed size threshold, but that disclosure should be made on all trades involving retail customers, regardless of size.[55]

Other commenters opposed the proposal on several grounds. Commenters questioned whether the proposed disclosure would provide investors with useful information,[56] or whether the disclosure would simply create confusion among investors.[57] Commenters asserted that the proposed methodology for determining the

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52 See, e.g., SEC Investor Advocate Letter I at 1-2.

53 See CFA Letter I at 1; DelphX Letter I at 2; SEC Investor Advocate Letter I at 2.

54 See CFA Letter I at 1.

55 See Hutchinson Shockey Letter I at 2; Thomson Reuters Letter I at 7.

56 See Diamant Letter I at 5.

57 See BDA Letter I at 4-5; FSI Institute Letter I at 3; Morgan Stanley Letter I at 2; SIFMA Letter I at 17; Wells Fargo Letter I at 5.

reference transaction would be overly complex[58] and costly for dealers to implement.[59] Commenters also indicated the proposal could impair liquidity in the municipal market.[60]

Several commenters suggested ways to narrow the scope of the proposal. Some commenters recommended that the MSRB limit the disclosure obligation to riskless principal transactions involving retail investors, as this would more accurately reflect dealer compensation and transaction costs,[61] and would be more consistent with the stated objectives of the SEC in this area and of the proposal itself.[62] Some commenters suggested that the proposed rule should apply to riskless principal transactions as previously defined by the Commission for equity trades, wherein the dealer has an "order in hand" at the time of execution.[63] One commenter, however, did not think that such a limitation would appreciably reduce the complexity or cost of the proposal.[64] Commenters also suggested that the MSRB eliminate institutional trades from the scope of the proposal: for example, by not covering institutional accounts as defined in Rule G-8(a)(xi) or sophisticated municipal market professionals ("SMMP") as defined in MSRB Rule D-15.[65] Both Fidelity and SIFMA stated that the proposal should permit trading desks that are separately operated within a firm to match only their own trades for purposes of pricing disclosure.[66] Morgan Stanley and SIFMA also stated that transactions between affiliates should not constitute a firm principal trade that, if accompanied by a same-day customer trade, would trigger the disclosure requirement.[67] Commenters also

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58 See Fidelity Letter I at 4; FIF Letter I at 2; SIFMA Letter I at 24-26; Thomson Reuters Letter I at 2; Wells Fargo Letter I at 8.

59 See BDA Letter I at 2-3; Diamant Letter I at 7-8; Fidelity Letter I at 4-5; FIF Letter I at 2; FSI Institute Letter I at 5; Financial Services Roundtable Letter I at 5; Morgan Stanley Letter I at 3; Wells Fargo Letter I at 7-9.

60 See Diamant Letter I at 8-9; FSI Institute Letter I at 3.

61 See Hilliard Letter I at 2; Morgan Stanley Letter I at 2; SIFMA Letter I at 29; Wells Fargo Letter I at 11.

62 See SIFMA Letter I at 31.

63 See Hilliard Letter I at 2; SIFMA Letter I at 30; Wells Fargo Letter I at 11.

64 See Thomson Reuters Letter I at 7.

65 See BDA Letter I at 6; FIF Letter I at 3; Morgan Stanley Letter I at 3; SIFMA Letter I at 35.

66 See Fidelity Letter I at 8; SIFMA Letter I at 36.

67 See Morgan Stanley Letter I at 3; SIFMA Letter I at 21.

suggested that the proposal exempt the disclosure of mark-ups on new issues.[68] One commenter suggested specifically that this exemption should cover transactions in new issues executed at the public offering price on the date of the issue's sale.[69]

Rather than proposing pricing reference disclosure, several commenters suggested that the MSRB instead enhance EMMA, in part by providing greater investor education about EMMA,[70] and requiring dealers to make EMMA more accessible[71] by, for example, providing more near-real-time EMMA information to investors[72] or providing a link to EMMA on customer confirmations,[73] or by aggregating all TRACE and EMMA data on a single website.[74]

Summary of Revised Confirmation Disclosure Proposal and Comments Received

In response to the comments received on MSRB Notice 2014-20, the MSRB proposed a different disclosure standard that was built upon the framework of the initial confirmation disclosure proposal, but modified a number of its key aspects and added several exceptions to the proposed disclosure requirement.[75]

First, in response to concerns that the disclosures may be misconstrued by investors who may equate them with mark-ups or believe that they are always reflective of contemporaneous market conditions, the MSRB proposed requiring dealers to disclose the amount of mark-up or mark-down, as calculated from the prevailing market price for the security, rather than disclose the difference between the customer's price and the dealer's price in a reference transaction. The MSRB also proposed that the mark-up or mark-down disclosure be expressed as a total dollar amount and as a percentage.

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68 See BDA Letter I at 6; Coastal Securities Letter I at 1; SIFMA Letter I at 22.

69 See Coastal Securities Letter I at 1.

70 See Fidelity Letter I at 7; FSI Institute Letter I at 6-7; Financial Services Roundtable Letter I at 6; Hilliard Letter I at 2-3; Morgan Stanley Letter I at 2; SIFMA Letter I at 15-16.

71 See Thomson Reuters Letter I at 6.

72 See Wells Fargo Letter I at 7.

73 See Fidelity Letter I at 7; FSI Institute Letter I at 6; Hilliard Letter I at 3; Morgan Stanley Letter I at 2; SIFMA Letter I at 15-16.

74 See FIF Letter I at 4.

75 See MSRB Notice 2015-16 (September 24, 2015).

Second, the MSRB proposed to narrow the disclosure time window from a same-day disclosure standard to a two-hour disclosure standard. Thus, mark-up disclosure would be required only where the dealer's same-side of the market transaction occurs within the two hours preceding or following the customer transaction. The MSRB explained that it believed that such a time frame would be sufficient to cover transactions that could be considered "riskless principal" transactions under any current market understanding of the term, but that it was not proposing a broader same-day trigger out of concern about the potential for additional costs and complexities associated with a broader disclosure time trigger. However, the MSRB specifically sought public comment as to whether a broader disclosure time trigger, such as a same-day standard, might be warranted.

Third, the MSRB proposed to replace the transaction size retail-customer proxy (i.e., 100 bonds or fewer or bonds in a par amount of $100,000 or less) proposed in the initial confirmation disclosure proposal with a status-based exclusion for transactions that involve an institutional account, as defined in Rule G-8(a)(xi). This would ensure that all eligible transactions involving retail customers, regardless of size or par amount, would be subject to the proposed disclosure and was responsive to dealer concerns about using disparate definitions of a retail customer.

Fourth, the MSRB proposed to require the disclosure of two additional data points, even if mark-up disclosure would not be required under the MSRB's proposal. The MSRB proposed to require that: (i) dealers add a CUSIP-specific link to EMMA on all customer confirmations and (ii) dealers disclose the time of execution of a customer's trade on all customer confirmations. These disclosures were intended to provide context for the mark-up disclosures received by providing retail customers with a comprehensive view of the market for their security, including the market as of the time of trade. They were also responsive to commenter suggestions that the MSRB leverage EMMA and direct investors to the more comprehensive information there.

Finally, the MSRB proposed three exceptions to the mark-up disclosure requirement. Under the first exception, in response to concerns from commenters that compensation disclosure is not warranted for primary market transactions, the MSRB proposed to provide an exclusion from a confirmation disclosure requirement for a customer transaction that is a "list offering price transaction," as defined in paragraph (d)(vii)(A) of Rule G-14 RTRS Procedures. A "list offering price transaction" is a primary market sale transaction executed on the first day of trading of a new issue by a sole underwriter, syndicate manager, syndicate member, selling group member, or distribution participant to a customer at the published list offering price for the security.

Under the second exception, in response to concerns from commenters that having the disclosure requirements triggered by trades made by separate trading departments or desks would undermine the legal and operational separation of those desks, the MSRB proposed to except from the mark-up disclosure requirement transactions between functionally separate trading desks. Under this exception, confirmation disclosure would not be required where, for example, the customer

transaction was executed by a principal trading desk that is functionally separate from the retail-side desk if the functionally separate principal trading desk had no knowledge of the customer transaction.

Under the third exception, in response to concerns from commenters about having the disclosure requirements triggered by certain trades between affiliates, the MSRB proposed to require dealers to "look through" a transaction with an affiliated dealer and substitute the affiliate's trade with the third party from whom the dealer purchased or to whom the dealer sold the security to determine whether disclosure of the mark-up would be required. This "look through" would apply only for dealers that, on an exclusive basis, acquire municipal securities from, or sell municipal securities to, an affiliate that holds inventory in such securities and transacts with other market participants. Some commenters stated that acquiring a security through an affiliate was functionally similar to an inventory trade, and that this trade would be of limited value,[76] particularly where the inter-affiliate trades are tantamount to a booking move across affiliates.[77]

As an ongoing alternative to the revised confirmation disclosure proposal, the MSRB also sought comment on a revised pricing reference proposal that was largely consistent with a revised confirmation disclosure proposal then under consideration by FINRA[78] and, more broadly, sought comment on the revised FINRA confirmation disclosure proposal itself. Under the revised FINRA confirmation disclosure proposal, if a firm sells to a customer as principal and on the same day buys the same security as principal from another party in one or more transaction(s) that equal or exceed the size of the customer transaction, the firm would have to disclose on the customer confirmation the price to the customer; the price to the firm of the same-day trade (the "reference price"); and the difference between those two prices. The revised FINRA confirmation disclosure proposal would permit firms to use alternative methodologies for calculating the reference price for more complex trade scenarios and would also permit firms to omit the reference price in the event of a material change in the price of the security between the time of the firm principal trade and the customer trade. Lastly, the revised FINRA confirmation disclosure proposal would require firms to provide a link to TRACE data on confirmations that are subject to the disclosure requirement.

The revised FINRA confirmation disclosure proposal also contained a number of exclusions that were generally consistent with those in the MSRB revised confirmation disclosure proposal. These included exclusions for: transactions that involve an institutional account; transactions that are part of a fixed price new issue and are sold at the fixed price offering price; firm principal trades that are executed on a trading desk functionally separate from the retail trading desk for purposes of calculating a reference

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76 See SIFMA Letter I at 21.

77 See Morgan Stanley Letter I at 3.

78 See FINRA Regulatory Notice 15-36 (October 2015).

price; and firm principal trades with affiliates for positions that were acquired by the affiliate on a previous trading day.

In response to the MSRB's revised confirmation disclosure proposal, some commenters reiterated that retail investors would benefit from some form of enhanced price disclosure. For example, the Consumer Federation of America stated that increased price disclosure would provide investors with the opportunity to make more informed investment decisions, and would foster increased price competition in the fixed income markets.[79] The SEC Investor Advocate stated that some kind of regulatory solution was necessary, as retail investors in fixed income securities "remain disadvantaged by the lack of information they receive in confirmation statements."[80] The PIABA stated that "abuse of undisclosed mark-ups and mark-downs is not a hypothetical problem," and that making additional pricing information available could result in customers being charged more favorable prices.[81]

A number of commenters supported the MSRB's proposal of disclosing the mark-up based on the prevailing market price instead of the reference price.[82] Both BDA and Schwab stated that the reference price proposal would be costly, difficult for dealers to implement and for retail customers to understand, and may not provide customers with meaningful information about the costs associated with particular transactions.[83] Schwab noted that, under the reference price proposal, a customer may receive disclosure for the execution of one lot of a particular order, but not for another lot of the same order.[84] Schwab stated that the reference price proposal would also reflect market fluctuations, so that a customer may infer that the dealer lost money on a transaction with a customer, even if a mark-up was charged.[85] FSI noted that using prevailing market price would ensure that customers "receive the most reasonably accurate understanding of the cost of their trade."[86] In addition, FSI indicated that "structuring pricing disclosure around prevailing market price will align any new disclosure requirements with existing fair

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79 See CFA Letter II at 6.

80 See SEC Investor Advocate Letter II at 2.

81 See PIABA Letter II at 3.

82 See BDA Letter II at 6; Fidelity Letter II at 5; FSI Letter II at 5; LPL Letter II at 1; Schwab Letter II at 3; SEC Investor Advocate Letter II at 5.

83 See BDA Letter II at 4-5; Schwab Letter II at 2.

84 See Schwab Letter II at 2.

85 See Schwab Letter II at 2.

86 See FSI Letter II at 5.

pricing policies enforced by both FINRA and the MSRB."[87] Fidelity stated that the proposed disclosure requirement should focus on the difference between the price the customer was charged for a fixed income security and the prevailing market price of the fixed income security.[88] Fidelity noted that a dealer's actual contemporaneous costs or proceeds are a reasonable proxy for the prevailing market price in some situations, but stated that there are many situations in which a dealer's costs or proceeds are not a reasonable proxy for the prevailing market price.[89] Fidelity proposed that the prevailing market price be defined as the dealer's best available price for the subject security under the best available market at the time of trade execution.[90] Fidelity proposed different methodologies that dealers could apply when determining the prevailing market price, including (1) looking at a trader's mark-to-market at the end of the day; (2) contemporaneous cost; (3) top of book; and (4) vendor solutions that offer real time valuations for certain securities.[91]

In supporting the MSRB's mark-up disclosure approach, the SEC Investor Advocate noted that although mark-up disclosure may lead to disclosure to an investor of information indicating a smaller cost under some circumstances than under the reference price proposal, it nonetheless provides relevant information about the actual compensation the investor is paying the dealer for the transaction, reflects market conditions and has the potential to provide a more accurate benchmark for calculating transaction costs.[92] LPL Financial noted that mark-up disclosure based on prevailing market price would be relevant to retail transactions in all kinds of fixed income securities that might be the subject of future disclosure requirements.[93]

Some commenters opposed limiting the disclosure requirement to circumstances where the dealer principal and customer trades occur closer in time to each other, such as two hours, as the MSRB previously had proposed. Coastal Securities, the Consumer Federation of America and the SEC Investor Advocate noted that a shorter timeframe would increase the possibility that dealers would attempt to evade the disclosure

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87 Id.

88 See Fidelity Letter II at 5, 7-8.

89 Id. at 7.

90 Id.

91 Id. at 8.

92 See SEC Investor Advocate Letter II at 5.

93 See LPL Letter II at 4.

requirement by holding onto positions.[94] Other commenters, including Morgan Stanley and SIFMA, supported the two-hour timeframe for disclosure.[95] These commenters stated that the two-hour window would capture the majority of the trades at issue, and would also be easier to implement.[96] Commenters stated that the concern that a shorter timeframe would facilitate gaming of the disclosure requirement was misplaced, as it was unlikely that dealers would change trading patterns and increase risk exposure merely to avoid disclosure.[97] One commenter also said that regulators have sufficient access to data that would show whether dealers were attempting to game a two-hour disclosure window.[98]

Commenters generally supported the change of the scope of the proposal from the "qualifying size" standard (transactions involving 100 bonds or fewer or $100,000 face amount or less) to all transactions with non-institutional accounts.[99] The Consumer Federation of America noted that the revised standard would help ensure that all retail transactions would receive disclosure, regardless of size.[100]

Three commenters opposed the proposal to require dealers to disclose the time of the execution of the customer transaction.[101] FIF stated that this proposal would create additional expense for dealers, and information related to time of execution could not be adjusted in connection with any trade modifications, cancellations or corrections.[102] FIF also indicated that the execution time is not necessary because "the number of trades in each CUSIP listed on EMMA are so limited that investors will not have difficulty in

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94 See Coastal Securities Letter II at 1; CFA Letter II at 2; SEC Investor Advocate Letter II at 5.

95 See Bernardi Letter II at 1; CFA Institute Letter II at 1; Coastal Securities Letter II; Morgan Stanley Letter II at 3; RBC Letter II at 2; SIFMA Letter II at 7.

96 See CFA Institute Letter II at 5; Morgan Stanley Letter II at 3; SIFMA Letter II at 7.

97 See Morgan Stanley Letter II at 3; RW Smith Letter II at 2; SIFMA Letter II at 10.

98 See RW Smith Letter II at 2.

99 See CFA Letter II at 4; PIABA Letter II at 2; Schwab Letter II at 5; SIFMA Letter II at 15.

100 See CFA Letter II at 4.

101 See FIF Letter II at 5; Schwab Letter II at 6; SIFMA Letter II at 16.

102 See FIF Letter II at 5.

ascertaining the prevailing market price at or around the time of their trade."[103] Schwab indicated that this would not be a necessary data point for investors if mark-ups are disclosed from the prevailing market price.[104]

Other commenters, however, supported including the time of execution of the customer trade.[105] Thomson Reuters stated that including the time of execution would allow retail investors to more easily identify relevant trade data on EMMA[106] and FSI stated that this would allow investors to understand the market for their security at the time of their trade.[107]

Several commenters supported adding a security-specific link to EMMA,[108] while other commenters, including FSI, SIFMA and Thomson Reuters, supported adding a general link to the EMMA website, noting that, in their view, a CUSIP-specific link could be inaccurate or misleading, and could be difficult for dealers to implement.[109] BDA stated that a general link to the main EMMA page would be operationally easier to achieve.[110]

Commenters supported the proposed exception for transactions involving separate trading desks,[111] although Schwab indicated that this exception should be subject to information barriers and rigorous oversight.[112] The Consumer Federation of America suggested the MSRB specifically require, in the rule text, that dealers have policies and

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103 See FIF Letter II at 6.

104 See Schwab Letter II at 6.

105 See CFA Institute Letter II at 4; FSI Letter II at 7; Thomson Reuters Letter II at 2.

106 See Thomson Reuters Letter II at 2.

107 See FSI Letter II at 7.

108 See Bernardi Letter at 1; CFA Institute Letter II at 3-4; Schwab Letter II at 6; Fidelity Letter II at 8; RBC Letter II at 2.

109 See FSI Institute Letter II at 6; SIFMA Letter II at 19; Thomson Reuters Letter II at 2.

110 See BDA Letter II at 3.

111 See CFA Letter II at 5; CFA Institute Letter II at 3; Schwab Letter II at 6; SIFMA Letter II at 14-15.

112 See Schwab Letter II at 6.

procedures in place to ensure functional separation between trading desks,[113] and the SEC Investor Advocate suggested that the MSRB provide more "robust" guidance as to what constitutes a functional separation and applicable requirements.[114]

Some commenters supported the proposed requirement, in cases of transactions between affiliates, to "look through" to the affiliate's principal transaction for purposes of determining whether disclosure is required.[115] FIF and Thomson Reuters stated, however, that not all dealers are able to "look through" principal trades, given information barriers and the fact that dealers often conduct inter-dealer business on a completely separate platform than the retail business.[116]

Summary of Proposed Amendments to Rule G-30

The proposed amendments to Rule G-30 to provide prevailing market price guidance was published for comment in MSRB Notice 2016-07 (February 18, 2016). The MSRB received nine comment letters in response to the request for comment on the draft guidance.[117] A copy of MSRB Notice 2016-07 is attached as Exhibit 2g. A list of comment letters received in response to MSRB Notice 2016-07 is attached as Exhibit 2h, and copies of the comment letters received are attached as Exhibit 2i.

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113 See CFA Letter II at 5.

114 See SEC Investor Advocate Letter II at 6.

115 See CFA Institute Letter II at 3; Fidelity Letter II at 11-12; PIABA Letter II at 2; Schwab Letter at 6; SIFMA Letter II at 18.

116 See FIF Letter II at 5; Thomson Reuters Letter II at 3.

117 Letter from Michael Nicholas, Chief Executive Officer, Bond Dealers of America, dated March 31, 2016 ("BDA Letter III"); E-mails from G. Lettieri, Breena LLC, dated February 23, 2016 and March 10, 2016 ("Breena Letter III"); Letter from Brian Shaw, dated March 28, 2016 ("Shaw Letter III"); E-mail from Herbert Murez, dated March 28, 2016 ("Murez Letter III"); Letter from Marcus Schuler, Head of Regulatory Affairs, Markit, dated March 31, 2016 ("Markit Letter III"); Letter from Rick A. Fleming, Investor Advocate, Office of the Investor Advocate, U.S. Securities and Exchange Commission, dated March 31, 2016 ("SEC Investor Advocate Letter III"); Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, Municipal Securities Division, and Sean Davy, Managing Director, Capital Markets Division, Securities Industry and Financial Markets Association, dated March 31, 2016 ("SIFMA Letter III"); Letter from J. Ben Watkins III, Director, State of Florida, Division of Bond Finance, dated March 31, 2016 ("State of Florida Letter III"); Letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, Thomson Reuters, dated March 31, 2016 ("Thomson Reuters Letter III").

Summary of the Proposed Guidance and Comments Received

As proposed in MSRB Notice 2016-07, generally, the prevailing market price of a municipal security would be presumptively established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained. If this presumption is either inapplicable or successfully rebutted, the prevailing market price would be determined by referring in sequence to: (1) a hierarchy of pricing factors, including contemporaneous inter-dealer transaction prices, institutional transaction prices, and if an actively traded security, contemporaneous quotations; (2) prices or yields from contemporaneous inter-dealer or institutional transactions in similar securities and yields from validated contemporaneous quotations in similar securities; and (3) economic models.

Of the nine comments the MSRB received on the proposal, the majority suggested alternatives or made recommendations to modify substantially more than one key aspect of the proposal.[118] The SEC Investor Advocate described the draft guidance as generally useful, clear, and consistent with the FINRA guidance, but urged the MSRB to tighten a perceived "loophole" with respect to transactions between affiliates.[119]

Other commenters opposed the draft guidance on several grounds. Commenters questioned the appropriateness of a hierarchical approach in the municipal market.[120] These commenters generally expressed a belief that while a prescriptive hierarchical approach may be appropriate for more liquid non-municipal debt securities, it is not appropriate for the more unique and heterogeneous municipal market.

A number of commenters stated that additional factors not permitted to be considered under the draft guidance should be expressly permitted to be considered when determining the prevailing market price of a municipal security. These include: trade size;[121] spread to an index;[122] and side of the market.[123] Others still suggested modifying or providing additional guidance for certain factors that are required or permitted to be

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118 See Shaw Letter III at 2; Markit Letter III at 1-5; SEC Investor Advocate III at 5-8; SIFMA Letter III at 3-14; Thomson Reuters Letter III at 2.

119 See SEC Investor Advocate Letter III at 8.

120 See BDA Letter III at 2; Markit Letter III at 2.

121 See SIFMA Letter III at 7; Thomson Reuters Letter III at 2; Markit Letter III at 4.

122 See Thomson Reuters Letter III at 2.

123 See SIFMA Letter III at 7.

considered under the draft guidance such as isolated transactions;[124] economic models;[125] and similar securities.[126] One commenter requested additional guidance on the meaning of the term, "contemporaneous."[127]

One commenter suggested that SMMPs should be exempted from the fair pricing requirement under Rule G-30, reasoning that, if SMMPs are sophisticated enough to opt out of Rule G-18 best-execution protections, they should similarly be able to opt out of fair pricing protections.[128] Another commenter suggested that the draft guidance should be limited to apply only to non-institutional accounts, consistent with the scope of the mark-up disclosure proposal.[129]

Based on a concern that a disclosed mark-up could appear misleadingly small when calculated from a non-arms-length transaction with an affiliated dealer, the SEC Investor Advocate urged the MSRB to require dealers acquiring securities from, or selling securities to, an affiliated dealer to always "look through" a non-arms-length transaction with an affiliate in establishing prevailing market price.[130] The SEC Investor Advocate further suggested that the underlying concern could be addressed in a number of ways (or combination thereof), including potentially modifying the draft guidance, modifying the proposed mark-up disclosure requirement or providing further explanation regarding non-arms-length inter-affiliate transactions in any filing of a proposed rule change.[131]

Commenters suggested that the MSRB should provide the market sufficient implementation time before any prevailing market price guidance is effective.[132] Two commenters specifically suggested that any final prevailing market price guidance and

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124 See Thomson Reuters Letter III at 2; SIFMA Letter III at 9.

125 See Thomson Reuters Letter III at 2.

126 See Thomson Reuters Letter III at 2; SIFMA Letter III at 8.

127 See SIFMA Letter III at 6.

128 See BDA Letter III at 4.

129 See SIFMA Letter III at 9-10.

130 See SEC Investor Advocate Letter III at 5-8.

131 Id.

132 See SIFMA Letter III at 13; Thomson Reuters Letter III at 2-3.

any final mark-up disclosure requirements should be adopted at the same time.[133] One commenter suggested a minimum three-year implementation period.[134]

A number of commenters suggested that the MSRB take an alternative approach to adopting prevailing market price guidance. One commenter suggested that the MSRB should permit dealers to rely on the use of third-party pricing vendors under certain conditions,[135] while another suggested the MSRB should calculate and disseminate a net weighted average price which should be used in place of the prevailing market price.[136]

One commenter stated that dealers may calculate different prevailing market prices from the same set of facts and that dealers should be permitted to rely on reasonably designed policies and procedures to determine, in an automated fashion, the prevailing market price of a security.[137] Others expressed concern about the burden on dealers in complying with the draft guidance, and questioned whether such burden would be outweighed by any benefits to the market.[138]

More generally, three commenters suggested that the MSRB should coordinate with FINRA to develop consistent guidance and standards with respect to determining the prevailing market price of a security, including, potentially, the making by FINRA of corresponding changes to the FINRA guidance.[139]

In response to the comments received on the draft guidance, the MSRB clarified in the text of the proposed guidance that the list of factors specifically set forth in the proposed guidance to be used in determining whether a municipal security is sufficiently similar to the subject security as to be a "similar" security under the proposed guidance is a non-exclusive list. The text of the proposed guidance also makes clear that the determination of whether such security is "similar" may be determined by all relevant factors.

With respect to isolated transactions, the proposed guidance now clarifies that the determination of whether a transaction is an "isolated transaction" as that term is used in

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133 See BDA Letter III at 2-3; SIFMA Letter III at 13.

134 See SIFMA Letter III at 13.

135 See Markit Letter III at 4.

136 See Shaw Letter III at 2.

137 See SIFMA Letter III at 3.

138 See BDA Letter III at 1; State of Florida Letter III at 1; SIFMA Letter III at 14.

139 See SIFMA Letter III at 5; Markit Letter III at 5; SEC Investor Advocate Letter III at 6.

the proposed guidance is not limited to a strictly temporal consideration, and that "off-market transactions" may be deemed isolated transactions under the proposed guidance.

The MSRB agrees with the SEC Investor Advocate's concern regarding the potential for misleading mark-up or mark-down calculations and disclosures when the mark-up or mark-down is determined by reference to a non-arms-length transaction with an affiliated dealer. The MSRB has addressed this concern, as discussed above, through a combination of provisions in the proposed mark-up disclosure requirement and explanation in this filing of the MSRB's intended meaning of the proposed prevailing market price guidance.[140]

The MSRB is not, at this time, providing any additional guidance regarding the defined term, "contemporaneous," as that term is used in the proposed guidance. This term is used in the FINRA guidance and adoption of the same term and definition within the proposed guidance promotes consistency and harmonization across fixed income markets. However, as discussed above, the determination of prevailing market price, as a final matter for purposes of confirmation disclosure, may be made at the time of a dealer's generation of the disclosure.

As noted above, the MSRB recognizes that the determination of the prevailing market price of a particular security may not be identical across dealers, although the MSRB expects that even where dealers may reasonably arrive at different prevailing market prices for the same security, the difference between such prevailing market price determinations would typically be small. The MSRB would expect that dealers have reasonable policies and procedures in place to calculate the prevailing market price and that such policies and procedures are applied consistently across customers.

Also as noted above, the MSRB has been in close coordination with FINRA on the development of the MSRB's mark-up disclosure proposal and the proposed guidance. The MSRB believes that the MSRB proposals are generally harmonized with the FINRA confirmation disclosure proposal and the interpretation of FINRA guidance, as applicable and to the extent appropriate in light of the differences between the markets.

The MSRB believes that the cumulative effect of the MSRB's modifications and clarifications contained in the proposed guidance is to make the waterfall generally less subjective and more easily susceptible to programming (e.g., specific guidance with respect to determining contemporaneous cost or proceeds, the ability to determine the prevailing market price at the time of the making of a disclosure and the ability to consider economic models earlier in the process to the extent there are no "similar" securities to be considered). At the same time, these modifications and clarifications provide dealers with a greater degree of flexibility with respect to certain elements of the waterfall (e.g., more flexibility in determining the similarity of securities). The MSRB

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140 See discussion supra, Non-Arms-Length Affiliate Transactions.

believes that these changes make the hierarchical approach more appropriate for the municipal market.

6. Extension of Time Period for Commission Action

The MSRB does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.[141]

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

11. Exhibits

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 2a. MSRB Notice 2014-20 (November 17, 2014).

Exhibit 2b. List of comment letters received in response to MSRB Notice 2014-20.

Exhibit 2c. Comments received in response to MSRB Notice 2014-20.

Exhibit 2d. MSRB Notice 2015-16 (September 24, 2015).

Exhibit 2e. List of comment letters received in response to MSRB Notice 2015-16.

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141 15 U.S.C. 78s(b)(2).

Exhibit 2f. Comments received in response to MSRB Notice 2015-16.

Exhibit 2g. MSRB Notice 2016-07 (February 18, 2016).

Exhibit 2h. List of comment letters received in response to MSRB Notice 2016-07.

Exhibit 2i. Comments received in response to MSRB Notice 2016-07.

Exhibit 5. Text of the proposed rule change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-_____; File No. SR-MSRB-2016-12)

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change to MSRB Rules G-15 and G-30 to Require Disclosure of Mark-Ups and Mark-Downs to Retail Customers on Certain Principal Transactions and to Provide Guidance on Prevailing Market Price

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Exchange Act" or "Act")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on the Municipal Securities Rulemaking Board (the "MSRB" or "Board") filed with the Securities and Exchange Commission (the "SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the MSRB. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The MSRB filed with the Commission a proposed rule change to amend MSRB Rule G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to customer transactions, and MSRB Rule G-30, on prices and commissions, (the "proposed rule change") to require brokers, dealers and municipal securities dealers (collectively, "dealers") to disclose mark-ups and mark-downs to retail customers on certain principal transactions and to provide dealers guidance on prevailing market price for the purpose of calculating mark-ups and mark-downs and other Rule G-30 determinations.

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1 15 U.S.C. 78s(b)(i).

2 17 CFR 240.19b-4.

If the Commission approves the proposed rule change, the MSRB will announce the effective date of the proposed rule change no later than 90 days following Commission approval. The effective date will be no later than 365 days following Commission approval.

The text of the proposed rule change is available on the MSRB's website at www.msrb.org/Rules-and-Interpretations/SEC-Filings/2016-Filings.aspx, at the MSRB's principal office, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the MSRB included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The MSRB has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Proposed Amendments to Rule G-15

The MSRB is proposing to amend Rule G-15 to require dealers to provide additional pricing information on customer confirmations in connection with specified municipal securities transactions with retail customers. Specifically, if a dealer trades as principal with a retail (i.e., non-institutional) customer in a municipal security, the dealer must disclose the dealer's mark-up or mark-down (collectively, "mark-up," unless the context requires otherwise) from the prevailing market price for the security on the customer confirmation, if the dealer also executes one or more offsetting principal transaction(s) on the same trading day as the customer, on the

same side of the market as the customer, in an aggregate size that meets or exceeds the size of the customer trade.

Many dealers already are required to disclose additional pricing information to customers for certain types of transactions under certain circumstances. Pursuant to Exchange Act Rule 10b-10, dealers effecting equity transactions in which they act in a riskless principal capacity must disclose on the customer confirmation the difference between the price to the customer and the dealer's contemporaneous purchase or sale price.[3] Pursuant to Rule G-15, dealers effecting municipal securities transactions in which they act in an agent capacity must disclose on the customer confirmation the amount of remuneration received from the customer in connection with the transaction (i.e., the commission).

The MSRB has conducted analyses of various data reported to its Electronic Municipal Market Access (EMMA®) system[4] in order to evaluate the potential need for the proposed mark-up disclosure rule. Over the period from July 1, 2015 through September 30, 2015 (Q3 2015),[5]

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3 See 17 CFR 240.10b-10. Under Rule 10b-10, where a broker or dealer is acting as principal for its own account and is not a market maker in an equity security, and receives a customer order in that equity security that it executes by means of a principal trade to offset the contemporaneous trade with the customer, the rule requires the broker or dealer to disclose the difference between the price to the customer and the dealer's contemporaneous purchase (for customer purchases) or sale price (for customer sales). See Rule 10b-10(a)(2)(ii)(A). Where the broker or dealer acts as principal for any other transaction in a defined National Market System stock, or an equity security that is listed on a national securities exchange and is subject to last sale reporting, the rule requires the broker or dealer to report the reported trade price, the price to the customer in the transaction, and the difference, if any, between the reported trade price and the price to the customer. See Rule 10b-10(a)(2)(ii)(B).

4 EMMA is a registered trademark of the MSRB.

5 Q3 2015 trading activity was substantially similar to trading activity in the preceding two and following one quarter. For example, the total number of trades reported to EMMA in Q3 2015 was 2,319,070 while the average number of trades reported to EMMA per quarter in 2015 was 2,305,705. Similarly, the number of retail-size, customer transactions

the average daily number of retail-size[6] customer transactions in the secondary market for municipal securities in which the dealer acted in a principal capacity was 15,538. The transactions were mainly concentrated among large firms. These trades were reported by approximately 700 dealers, however, the top 20 dealers with the highest volumes accounted for approximately 73 percent of the transactions in municipal securities. Of those retail-size customer transactions in the secondary market in which the dealer acted in a principal capacity, approximately 55 percent would have likely received a disclosure if the proposed rule had been in place.[7]

Of those trades which likely would have received disclosure, 38 percent of the offsetting trade(s) that would have triggered the disclosure occurred simultaneously (the reported times of both the customer trade and the offsetting trade(s) were identical), 50 percent of the offsetting trade(s) occurred within 19 seconds of the customer trade, and 83 percent of the offsetting trades occurred within 30 minutes.

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in the secondary market in which the dealer acted in a principal capacity in Q3 2015 was 994,409 while the average number of trades per quarter with the same characteristics during 2015 was 980,809.

6 The data reported to the MSRB do not indicate whether the customer purchasing or selling a security has an "institutional" account as defined in Rule G-8(a)(xi). Therefore, for the purposes of the analysis included here, the MSRB has defined a "retail-size" transaction as any customer transaction with a reported trade amount of 100 bonds or fewer or a face value of $100,000 or less. The MSRB recognizes that this proxy for retail customers may, in some cases, include transactions with institutional account holders and may also fail to include transactions with some retail customers.

7 That is, the customer's trade with a dealer was preceded or followed, on the same trading day, by one or more trades equal to the customer trade, by the dealer on the other side of the market in the same security. The percentage of customer trades that would have received a disclosure may be overestimated because in some cases, the dealer trade on the other side of the market may have been with an affiliate and the "look through" provision of the proposed rule may not have identified another trade that would have required disclosure.

For those trades that likely would have received disclosure, the median value of the estimated mark-up for customer purchases was approximately 1.20 percent and the median value of the estimated mark-down was approximately 0.50 percent.[8] For both mark-ups on customer purchases and mark-downs on customer sales, many customers paid considerably more than the median value. For example, five percent of customer purchases that would have been eligible for disclosure (representing approximately 14,900 trades) had estimated mark-ups higher than 2.25 percent while five percent of customer sales (representing approximately 6,500 trades) had estimated mark-downs higher than 1.51 percent.

The MSRB believes that retail investors are currently limited in their ability to assess and compare transaction costs associated with the purchase or sale of municipal securities. Joint investor testing conducted by the Financial Industry Regulatory Authority ("FINRA") and the MSRB ("joint investor survey") revealed that investors lack a clear understanding of how dealers are compensated when dealers act in a principal capacity and that investors have a desire for more information on this topic. Retail investors transacting with dealers acting in a principal capacity may, therefore, participate in the municipal securities market with less information than other market participants and be less able to foster price competition.[9] This information asymmetry may be observable, in part, in the large differences between estimated median mark-

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8 The mark-up and mark-down calculations involved matching customer trades to one or more offsetting same-day principal trades by the same dealer in the same CUSIP. This included matching same-size trades as well as trades of different sizes where there was no same-size match (e.g., a dealer purchase of 100 bonds matched to two sales to customers of 50 bonds each). The mark-ups (mark-downs) on customer buys (sells) correspond to the percentage difference in price in customer trades and the offsetting principal trade.

9 The SEC's 2012 Report on the Municipal Securities Market reached similar conclusions based on multiple studies. See U.S. Securities and Exchange Commission, Report on the Municipal Securities Market (July 31, 2012).

ups and the highest mark-ups paid by retail customers. As noted above, the five percent of customer trades with the highest mark-ups have mark-ups that are more than twice as large as the median mark-up.

Some market participants have asserted that the observed dispersion in mark-ups might be explained by bond- or execution-specific characteristics (e.g., that higher mark-ups can be explained by the additional dealer costs associated with transacting in relatively small quantities). The data do not support this conclusion. An analysis of the transactions that took place during Q3 2015 and that likely would have received disclosures if the proposed rule had been in place indicates that not only are the large dispersions in mark-ups not fully explained by bond- or execution-specific characteristics, but also that, in some cases, factors that might be expected to result in lower mark-ups appear to be associated with higher mark-ups. For example, the median quantity of bonds traded in transactions with the highest mark-ups was either the same or similar to the median quantity of bonds traded in transactions with significantly lower mark-ups and bonds with higher trading frequencies in Q3 2015, and presumably higher liquidity, actually had higher estimated mark-ups than bonds that traded less frequently. The MSRB believes that requiring dealers to disclose their mark-ups on retail customer confirmations would provide meaningful and useful pricing information and may lower transaction costs for retail transactions.

As described in greater detail in the section on comments received on the proposed rule change, the MSRB initially solicited comment on a related proposal in MSRB Notice 2014-20 (the "initial confirmation disclosure proposal"),[10] and subsequently on a revised proposal in

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[10] See MSRB Notice 2014-20 (November 17, 2014).

MSRB Notice 2015-16 (the "revised confirmation disclosure proposal").[11] The MSRB also has been coordinating with FINRA regarding the development of similar proposals, as appropriate, to foster generally consistent potential disclosures to customers across debt securities and to reduce the operational burdens for firms that trade multiple fixed income securities. The MSRB and FINRA published their initial and revised confirmation disclosure proposals on similar timelines,[12] and FINRA filed with the Commission a substantially similar proposed rule change to the proposed amendments to Rule G-15 on August 12, 2016.[13]

Provided below is a more detailed description of each significant aspect of the proposed amendments to Rule G-15.

Scope of the Disclosure Requirement

The proposed mark-up disclosure requirement would apply where the dealer buys (or sells) a municipal security on a principal basis from (or to) a non-institutional customer and engages in one or more offsetting principal trade(s) on the same trading day in the same security, where the size of the dealer's offsetting principal trade(s), in the aggregate, equals or exceeds the size of the customer trade. A non-institutional customer would be a customer with an account that is not an institutional account, as defined in Rule G-8(a)(xi), (i.e., a retail customer account).[14] The proposed rule change would apply to transactions in municipal securities, other than municipal fund securities.[15]

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11 See MSRB Notice 2015-16 (September 24, 2015).

12 See FINRA Regulatory Notice 14-52 (November 2014) and FINRA Regulatory Notice 15-36 (October 2015).

13 See SR-FINRA-2016-032 (Aug. 12, 2016).

14 Rule G-8(a)(xi) defines an institutional account as

The MSRB believes that the proposed amendments would provide meaningful pricing information to retail investors, which would most benefit from such disclosure, while not imposing unduly burdensome disclosure requirements on dealers. The MSRB believes that requiring disclosure for retail customers, i.e., those with accounts that are not institutional accounts, would be appropriate because retail customers typically have less ready access to market and pricing information than institutional customers. The MSRB believes that using the definition of an institutional account as set forth in Rule G-8(a)(xi) to define the scope of the disclosure requirement would be appropriate because reliance on an existing standard would simplify implementation and thereby reduce costs associated with the requirement.[16]

Same-Day Triggering Timeframe

The MSRB believes that it would be appropriate to require disclosure of the mark-up where the dealer's offsetting principal trade(s) equaled or exceeded the size of the customer trade on the same trading day. To the extent that a dealer will often refer to its contemporaneous cost or proceeds, e.g., the price it paid or received for the bond, in determining the prevailing market

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the account of (i) a bank, savings and loan association, insurance company, or registered investment company; (ii) an investment adviser registered 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.

15 See discussion infra, Exceptions for Functionally Separate Trading Desks, List Offering Price Transactions and Municipal Fund Securities.

16 As discussed in greater detail below, the MSRB initially proposed that the disclosure requirement would apply to customer trades involving 100 bonds or fewer or bonds in a par amount of $100,000 or less. In response to comments that the proposed size-based standard could either exclude retail customer transactions above that amount from the proposed disclosure, or subject institutional transactions below that amount to the proposed disclosure, the MSRB revised the proposal to incorporate the Rule G-8(a)(xi) definition of an institutional account.

price for purposes of calculating the mark-up or mark-down, the MSRB believes that limiting the disclosure requirement to those instances where there is an offsetting trade in the same trading day would generally make determination of the prevailing market price easier.

As is discussed in greater detail below, a number of commenters stated that the window for triggering disclosure should be limited to two hours. Among other things, commenters argued that a two-hour window would be easier to implement, and would more closely capture riskless principal trades, which would align the proposed disclosure to the riskless principal disclosure requirements for equity securities under Exchange Act Rule 10b-10.[17]

The MSRB believes that there are added benefits to requiring disclosure for trades that occur within the same trading day, rather than only trades that occur within two hours. First, the full-day window would ensure that more investors receive mark-up disclosure. Second, the full-day window may make dealers less likely to alter their trading patterns in response to the proposed requirement, as dealers would need to hold positions overnight to avoid the proposed disclosure.[18]

Some commenters recommended that the proposed disclosure obligation be limited to riskless principal transactions involving retail investors, which, in their view, would more

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17 See 17 CFR 240.10b-10.

18 It is important to note that, under Rule G-18, on best execution, dealers must use reasonable diligence to ascertain the best market for the security and buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions. Rule G-18, Supplementary Material .03 emphasizes that a dealer must make every effort to execute a customer transaction promptly, taking into account prevailing market conditions. Any intentional delay of a customer execution to avoid the proposed disclosure requirement or otherwise would be contrary to these duties to customers. A dealer that purposefully delayed the execution of a customer order to avoid the proposed disclosure also may be in violation of the MSRB's fundamental fair-dealing rule, Rule G-17, on conduct of municipal securities and municipal advisory activities.

accurately reflect dealer compensation and transaction costs and be more consistent with the stated objectives of the SEC in this area. These commenters would apply the requirement to riskless principal transactions as previously defined in the equity context by the Commission, where the dealer has an "order in hand" at the time of execution. However, the MSRB believes that it may be difficult to objectively define, implement and monitor a riskless principal trigger standard for municipal securities. The MSRB also believes that customers would benefit from the disclosure irrespective of whether the dealer's capacity on the transaction was riskless principal and believes, at this juncture, that using the riskless principal standard ultimately would be too narrow.

Non-Arms-Length Affiliate Transactions

With respect to the offsetting principal trade(s), where a dealer buys from, or sells to, certain affiliates, the proposal would require the dealer to "look through" the dealer's transaction with the affiliate to the affiliate's transaction(s) with third parties in determining when the security was acquired and whether the "same trading day" requirement has been triggered. Specifically, the MSRB proposes to require dealers to apply the "look through" where a dealer's transaction with its affiliate was not at arms-length. For purposes of the proposed rule change, an "arms-length transaction" would be considered a transaction that was conducted through a competitive process in which non-affiliate dealers could also participate -- e.g., pricing sought from multiple dealers, or the posting of multiple bids and offers -- and where the affiliate relationship did not influence the price paid or proceeds received by the dealer. As a general matter, the MSRB would expect that the competitive process used in an "arms-length" transaction, e.g., the request for pricing or platform for posting bids and offers, is one in which non-affiliates have frequently participated. The MSRB believes that, for example, sourcing

liquidity through a non-arms-length transaction with an affiliate is functionally equivalent to selling out of a dealer's own inventory for purposes of the proposed disclosure trigger. The MSRB therefore believes it would be appropriate in those circumstances to require a dealer to "look through" its transaction in a security with its affiliate to the affiliate's transactions in the security with third parties to determine whether the proposed mark-up disclosure requirement applies in these circumstances.[19]

Exceptions for Functionally Separate Trading Desks, List Offering Price Transactions and Municipal Fund Securities

Functionally Separate Trading Desks. The proposed amendments contain a number of exceptions from the mark-up disclosure requirement. First, if the offsetting same-day dealer principal trade was executed by a trading desk that is functionally separate from the dealer's trading desk that executed the transaction with the customer, the principal trade by that separate trading desk would not trigger the disclosure requirement. Dealers must have in place policies and procedures reasonably designed to ensure that the functionally separate principal trading desk through which the dealer purchase or dealer sale was executed had no knowledge of the customer transaction. The MSRB believes that this exception is appropriate because it recognizes the operational cost and complexity that may result from using a dealer principal trade executed by a separate, unrelated trading desk as the basis for determining whether a mark-up disclosure is triggered on the customer confirmation. For example, the exception would allow an institutional

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19 Similarly, as explained in greater detail, infra, in the discussion of the proposed prevailing market price guidance, in the case of a non-arms-length transaction with an affiliate, the dealer also would be required to "look through" to the affiliate's transaction(s) with third parties in the security and the time of trade and related cost or proceeds of the affiliate in determining the dealer's calculation of the mark-up pursuant to Rule G-30.

desk within a dealer to service an institutional customer without triggering the disclosure requirement for an unrelated trade performed by a separate retail desk within the dealer. At the same time, in requiring that the dealer have policies and procedures in place that are reasonably designed to ensure that the other trading desk had no knowledge of the customer transaction,[20] the MSRB believes that the safeguards surrounding the exception are sufficiently rigorous to minimize concerns about the potential misuse of the exception. In other words, in the example above, the dealer could not use the functionally separate trading desk exception to avoid the proposed disclosure requirement if trades at the institutional desk were used to source securities for transactions at the retail desk.

The MSRB also believes that this exception is appropriate and consistent with the concept of functional and legal separation that exists in connection with other regulatory requirements, such as SEC Regulation SHO, and notes that some dealers may already have experience maintaining functionally separate trading desks to comply with these requirements, depending upon their particular mix of business.

List Offering Price Transactions. Second, the mark-up would not be required to be disclosed if the customer transaction is a list offering price transaction, as defined in paragraph

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20 This provision is distinguished from the "look through" provision noted above, whereby the customer transaction is being sourced through a non-arms-length transaction with the affiliate. Under the separate trading desk exception, functionally separate trading desks are required to have policies and procedures in place that are reasonably designed to ensure that trades occurring on the functionally separate trading desks are executed with no knowledge of each other and reflect unrelated trading decisions. Additionally, the MSRB notes that this exception would only apply to determine whether or not the proposed disclosure requirement has been triggered; it does not change the dealer's requirements relating to the calculation of its mark-up or mark-down under Rule G-30.

(d)(vii)(A) of Rule G-14 RTRS Procedures.[21] For such transactions, bonds are sold at the same published list offering price to all investors, and the compensation paid to the dealer, such as the underwriting fee, is paid for by the issuer and typically is described in the official statement.[22] Given the availability of information in connection with such transactions, the MSRB believes that the proposed mark-up disclosure would not be warranted for list offering price transactions.

Municipal Fund Securities. Lastly, disclosure of mark-ups would not be required for transactions in municipal fund securities. Because dealer compensation for municipal fund securities transactions is typically not in the form of a mark-up, the MSRB believes that the proposed mark-up disclosure would not have application for transactions in municipal fund securities. Additionally, the proposed requirement to disclose the time of execution and a reference and hyperlink to the Security Details page for the customer's security on EMMA (both discussed below) also would not be established for transactions in such securities.

Proposed Information to be Disclosed on the Customer Confirmation

If the transaction meets the criteria described above, the dealer would be required to disclose on the customer confirmation the dealer's mark-up from the prevailing market price for

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21 The term "list offering price transaction" is defined as a primary market sale transaction executed on the first day of trading of a new issue "by a sole underwriter, syndicate manager, syndicate member, selling group member, or distribution participant [to a customer] at the published list offering price for the security." Rule G-14 RTRS Procedures (d)(vii)(A).

22 Under Rule G-32, on disclosures in connection with primary offerings, a dealer selling offered municipal securities generally must deliver to its customers a copy of the official statement by no later than the settlement of the transaction. Under Rule G-32(a)(iii), any dealer that satisfies the official statement delivery obligation by making certain submissions to EMMA in compliance with Rule G-32(a)(ii) must also provide to the customer, in connection with offered municipal securities sold by the issuer on a negotiated basis to the extent not included in the official statement, among other things, certain specified information about the underwriting arrangements, including the underwriting spread.

the security. The mark-up would be required to be calculated in compliance with Rule G-30 and the supplementary material thereunder, including proposed Supplementary Material .06 (discussed below), and expressed as a total dollar amount and as a percentage of the prevailing market price of the municipal security.[23] The MSRB believes that it would be appropriate to require dealers to calculate the mark-up in compliance with Rule G-30, as new Supplementary Material .06 would provide extensive guidance on how to calculate the mark-up for transactions in municipal securities, including transactions for which disclosure would be required under the proposed rule change, and incorporates a presumption that prevailing market price is established by reference to contemporaneous cost or proceeds. While some commenters noted the operational cost and complexity of implementing a mark-up disclosure requirement, the MSRB notes that dealers are currently subject to Rule G-30, on prices and commissions, and already are required to evaluate the mark-ups that they charge to ensure that they are fair and reasonable.[24]

The MSRB recognizes that the determination of the prevailing market price of a particular security may not be identical across dealers.[25] Existing Rule G-30, however, requires

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23 Some commenters stated that the mark-up should be expressed as a total dollar amount, while others suggested that disclosure as a total dollar amount should not be required. Others still stated that the mark-up should be required to be disclosed as both a percentage and a total dollar amount. While commenters did not uniformly favor any particular format of disclosure, results of the joint investor survey indicated that investors found that disclosing the mark-up or mark-down both as a dollar amount and as a percentage of the prevailing market price would be more useful than only disclosing it in one of those forms.

24 Rule G-30, Supplementary Material .01(d).

25 For example, because the prevailing market price of a security is presumptively established by reference to the dealer's contemporaneous cost or proceeds, different dealers may arrive at different prevailing market prices for the same security depending on the price at which they contemporaneously acquired or sold such security. However, even where dealers may reasonably arrive at different prevailing market prices for the

dealers to exercise reasonable diligence in establishing the prevailing market price.[26] The MSRB, therefore, would expect that dealers have reasonable policies and procedures in place to establish the prevailing market price and that such policies and procedures are applied consistently across customers.

The MSRB understands that some dealers provide confirmations on an intra-day basis. As explained in detail below in the context of the proposed amendments to Rule G-30, the proposed requirement to disclose a mark-up calculated "in compliance with" Rule G-30 (including the proposed prevailing market price guidance) need not delay the confirmation process. A dealer may determine, as a final matter for disclosure purposes, the prevailing market price based on the information the dealer has, based on the use of reasonable diligence as required by proposed amended Rule G-30, at the time of the dealer's generation of the disclosure.

The proposed rule change also would require the dealer to provide a reference and hyperlink to the Security Details page for a customer's security on EMMA, along with a brief description of the type of information available on that page. This disclosure requirement would be limited to transactions with retail (i.e., non-institutional) customers, but would apply for all such transactions regardless of whether a mark-up disclosure is required for the transaction.[27]

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same security, the MSRB believes that the difference between such prevailing market price determinations would typically be small.

[26] Rule G-30, Supplementary Material .04(b).

[27] Because institutional customers typically have more ready access to the type of information available on EMMA, the MSRB is not proposing to require this disclosure for transactions with institutional customers. Of course, dealers are free to voluntarily provide such a disclosure on all customer confirmations, including those for institutional customers.

The MSRB believes that such a link would provide retail investors with a broad picture of the market for a security on a given day and believes that requiring a link to EMMA would increase investors' awareness of, and ability to access, this information. Additionally, results from the joint investor survey support the value to investors of a security-specific link to EMMA, rather than a link to the EMMA homepage.[28] The MSRB believes that a link to EMMA or such other enhancements would not be sufficient, as customers are not always able to identify with certainty a principal trade in the same security that was made by that customer's dealer. As a result, the customer would not always be able to ascertain the exact amount of the price differential between the dealer and customer trade or to determine whether such a trade accurately reflects the "prevailing market price" for purposes of calculating the dealer's compensation.

The proposed rule change also would require the dealer to disclose on all customer confirmations, other than those for transactions in municipal fund securities, the time of execution. Dealers are already under an obligation to either disclose such information on the customer confirmation or to include a statement that the time of execution will be furnished upon written request.[29] The proposed amendments to Rule G-15 would essentially delete the option to provide this information upon request. The MSRB believes that the provision of a security-

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[28] Some commenters stated that EMMA already contains sufficient pricing information for municipal securities, such as the last trade price for a security, and recommended that the MSRB focus solely on enhancing access to EMMA instead of requiring additional pricing disclosure.

[29] Dealers have an existing obligation to report "time of trade" to the Real-Time Transaction Reporting System pursuant to Rule G-14, on reports of sales or purchases. In addition, dealers have an existing obligation to make and keep records of the time of execution of principal transactions under Rule G-8(a)(vii). The time of execution for proposed confirmation disclosure purposes is the same as the time of trade for Rule G-14 reporting purposes and the time of execution for purposes of Rule G-8(a)(vii), except that dealers should omit all seconds from the disclosure because the trade data displayed on EMMA does not include seconds (e.g., dealers should disclose a time of trade of 10:00:59 as 10:00).

specific link to EMMA on retail customer confirmations, together with the time of execution would provide retail customers a comprehensive view of the market for their security, including the market as of the time of their trade. This combined disclosure also would reduce the risk that a customer may overly focus on dealer compensation and not appropriately consider other factors relevant to the investment decision. Even in instances in which the mark-up would not be required to be disclosed to customers, the MSRB believes that the inclusion of the time of execution on all customer confirmations (retail and institutional) would increase market transparency at relatively low cost. Results from the joint investor survey support the MSRB's view that time of execution disclosure is valued by investors.

As noted above, if the Commission approves the proposed rule change, the MSRB will announce the effective date of the proposed rule change no later than 90 days following Commission approval. The effective date will be no later than 365 days following Commission approval.

Proposed Amendments to Rule G-30

The MSRB is proposing to add new supplementary material (paragraph .06 entitled "Mark-Up Policy") and amend existing supplementary material under MSRB Rule G-30, on prices and commissions, to provide guidance on establishing the prevailing market price and calculating mark-ups and mark-downs for principal transactions in municipal securities (the "proposed guidance" or "proposed prevailing market price guidance"). The MSRB believes additional guidance on these subjects would promote consistent compliance by dealers with their existing fair-pricing obligations under MSRB rules, in a manner that would be generally harmonized with the approach taken in other fixed income markets. The MSRB also believes that such guidance would support effective compliance with the proposed amendments to Rule

G-15, discussed above. In addition, commenters indicated that compliance with the proposed amendments to MSRB Rule G-15 would be less burdensome if the MSRB were to provide guidance on establishing the prevailing market price. Significantly, municipal securities dealers that also transact in corporate or agency debt securities must comply with FINRA Rule 2121, including Supplementary Material .02 ("FINRA guidance") for transactions in those securities.[30]

The proposed rule change also includes amendments to the Supplementary Material to Rule G-30. For example, the MSRB proposes to clarify in Supplementary Material .01(a) that a dealer must exercise "reasonable" diligence in establishing the market value of a security and the reasonableness of the compensation received. This requirement is consistent with existing Supplementary Material .04(b) ("[D]ealers must establish market value as accurately as possible using reasonable diligence under the facts and circumstances") and clarifies that the same standard applies under the Supplementary Material .01(a). Similarly, the proposed amendments to Supplementary Material .01(d) to Rule G-30 will clarify the relationship between that provision and the new proposed Supplementary Material .06 containing the proposed prevailing market price guidance. In addition, this provision will assist in understanding of the overall rule.

When a dealer acts in a principal capacity and sells a municipal security to a customer, the dealer generally "marks up" the security, increasing the total price the customer pays. Conversely, when buying a security from a customer, a dealer that is acting as a principal generally "marks down" the security, reducing the total proceeds the customer receives. Rule G-30(a) prohibits a dealer from engaging in a principal transaction with customers except at an aggregate price (including any mark-up or mark-down) that is fair and reasonable. The

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30 See FINRA Rule 2121, Fair Prices and Commissions, Supplementary Material .02, Additional Mark-Up Policy For Transactions in Debt Securities, Except Municipal Securities.

Supplementary Material to Rule G-30, among other things, provides that as part of the aggregate price to the customer, the mark-up or mark-down also must be a fair and reasonable amount, taking into account all relevant factors.[31]

A critical step in determining whether the mark-up or mark-down on a principal transaction with a customer and the aggregate price to such customer is fair and reasonable is correctly identifying the prevailing market price of the security. Currently, under Rule G-30, the total transaction price to the customer must bear a reasonable relationship to the prevailing market price of the security, and, in a principal transaction, the dealer's compensation must be computed from the inter-dealer market price prevailing at the time of the customer transaction.[32] Moreover, existing Rule G-30 requires dealers to exercise diligence in establishing the market value of the security and the reasonableness of their compensation.[33]

Under the proposed guidance, the prevailing market price of a municipal security generally would be presumptively established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained. This presumption could be overcome in limited circumstances. If the presumption is overcome, or if it is not applicable because the dealer's cost is (or proceeds are) not contemporaneous, various factors discussed below would be either required or permitted to be considered, in successive order, to determine the prevailing market price. Generally, a subsequent factor or series of factors could be considered only if previous factors in the hierarchy, or "waterfall," are inapplicable.

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31 Rule G-30, Supplementary Material .01(d).

32 Rule G-30, Supplementary Material .01(c), (d).

33 Rule G-30, Supplementary Material .01(a).

As described in greater detail below, the MSRB solicited comment on draft prevailing market price guidance in MSRB Notice 2016-07 (the "draft guidance"). The draft guidance was substantially similar to and generally harmonized with the FINRA guidance for non-municipal fixed income securities. As discussed below, the proposed guidance is substantially in the form of the draft guidance on which public comment was sought, with some minor changes. In addition, the MSRB provides additional explanation of the proposed guidance herein in response to commenters and to clearly express the MSRB's intended meaning of the proposed guidance. Moreover, the MSRB will continue to engage with FINRA with the goal of promoting generally harmonized interpretations of the proposed guidance, if approved, and the FINRA guidance, as applicable and to the extent appropriate in light of the differences between the markets.

Provided below is a more detailed description of each significant aspect of the proposed amendments to Rule G-30.

Rebuttable Presumption Based on Contemporaneous Costs or Proceeds

The proposed guidance builds on the standard in existing Supplementary Material to Rule G-30 that the prevailing market price of a security is generally the price at which dealers trade with one another (i.e., the inter-dealer price).[34] The proposed guidance provides that the best measure of prevailing market price is presumptively established by referring to the dealer's contemporaneous cost (proceeds), as consistent with other MSRB pricing rules, such as the best-execution rule (Rule G-18). Under the proposed guidance, a dealer's cost is (or proceeds are) considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the

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[34] See Rule G-30, Supplementary Material .01(d) ("Dealer 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.").

municipal security. The reference to dealer contemporaneous cost or proceeds in determining the prevailing market price reflects a recognition of the principle that the prices paid or received for a security by a dealer in actual transactions closely related in time are normally a highly reliable indication of the prevailing market price and that the burden is appropriately on the dealer to establish the contrary.

A dealer may look to other evidence of the prevailing market price (other than contemporaneous cost) only where the dealer, when selling the security, made no contemporaneous purchases in the municipal security or can show that in the particular circumstances the dealer's contemporaneous cost is not indicative of the prevailing market price. When buying a municipal security from a customer, the dealer may look to other evidence of the prevailing market price (other than contemporaneous proceeds) only where the dealer made no contemporaneous sales in the municipal security or can show that in the particular circumstances the dealer's contemporaneous proceeds are not indicative of the prevailing market price.

A dealer may be able to show that its contemporaneous cost (when it is making a sale to a customer) or proceeds (when it is making a purchase from a customer) are not indicative of the prevailing market price, and thus overcome the presumption, in instances where: (i) interest rates changed to a degree that such change would reasonably cause a change in municipal securities pricing; (ii) the credit quality of the municipal security changed significantly;[35] or (iii) news was

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[35] Consistent with FINRA statements with respect to other fixed income securities, although an announcement by a nationally recognized statistical rating organization ("NRSRO") that it has reviewed the issuer's credit and has changed the issuer's credit rating is an easily identifiable incidence of a change of credit quality, the category is not limited to such announcements. It may be possible for a dealer to establish that the issuer's credit quality changed in the absence of such an announcement; conversely, a relevant regulator may determine that the issuer's credit quality had changed and such change was known to the market and factored into the price of the municipal security before the dealer's transaction (the transaction used to measure the dealer's contemporaneous cost) occurred. See Exchange

issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the municipal security.[36]

Hierarchy of Pricing Factors. Under the proposed guidance, if the dealer has established that the dealer's cost is (or proceeds are) not contemporaneous or if the dealer has overcome the presumption that its contemporaneous cost or amount of proceeds provides the best measure of the prevailing market price, the dealer must consider, in the order listed (subject to Supplementary Material .06(a)(viii), on isolated transactions and quotations), a hierarchy of three additional types of pricing information, referred to here as the hierarchy of pricing factors: (i) prices of any contemporaneous inter-dealer transactions in the municipal security; (ii) prices of contemporaneous dealer purchases (or sales) in the municipal security from (or to) institutional accounts with which any dealer regularly effects transactions in the same municipal security; or (iii) if an actively traded security, contemporaneous bid (or offer) quotations for the municipal security made through an inter-dealer mechanism, through which transactions generally occur at the displayed quotations. Pricing information of a succeeding type may only be considered where the prior type does not generate relevant pricing information. In reviewing the available pricing information of each type, the relative weight of the information depends on the facts and circumstances of the comparison transaction or quotation. The proposed guidance also makes

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Act Release No. 54799 (Nov. 21, 2006); 71 FR 68856 (Nov. 28, 2006) (FINRA Notice of Filing of Amendments Related to Mark-Up Policy).

36 Consistent with FINRA statements with respect to other fixed income securities, certain news affecting an issuer, such as news of legislation, may affect either a particular issuer or a group or sector of issuers and may not clearly fit within the two previously identified categories – interest rate changes and credit quality changes. Such news may cause price shifts in a municipal security, and could, depending on the facts and circumstances, invalidate the use of the dealer's own contemporaneous cost as a reliable and accurate measure of prevailing market price. See id.

clear the expectation that, because of the lack of active trading in many municipal securities, these factors may frequently not be available in the municipal market. Accordingly, dealers may often need to consult factors further down the waterfall, such as "similar" securities and economic models, to identify sufficient relevant and probative pricing information to establish the prevailing market price of a municipal security.

Similar Securities. If the above factors are not available, the proposed guidance provides that the dealer may take into consideration a non-exclusive list of factors that are generally analogous to those set forth under the hierarchy of pricing factors, but applied here to prices and yields of specifically defined "similar" securities. However, unlike the factors set forth in the hierarchy of pricing factors, which must be considered in the specified order, the factors related to similar securities are not required to be considered in a particular order or particular combination. The non-exclusive factors specifically listed are:

- Prices, or yields calculated from prices, of contemporaneous inter-dealer transactions in a specifically defined "similar" municipal security;
- Prices, or yields calculated from prices, of contemporaneous dealer purchase (sale) transactions in a "similar" municipal security with institutional accounts with which any dealer regularly effects transactions in the "similar" municipal security with respect to customer mark-ups (mark-downs); and
- Yields calculated from validated contemporaneous inter-dealer bid (offer) quotations in "similar" municipal securities for customer mark-ups (mark-downs").

When applying one or more of the factors, a dealer would be required to consider that the ultimate evidentiary issue is whether the prevailing market price of the municipal security will be correctly identified. As stated in the proposed guidance, the relative weight of the pricing

information obtained from the factors depends on the facts and circumstances surrounding the comparison transaction, such as whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction, the timeliness of the information and, with respect to the final bulleted factor above, the relative spread of the quotations in the "similar" municipal security to the quotations in the subject security. As noted below, regarding isolated transactions generally, in considering yields of "similar" securities, except in extraordinary circumstances, dealers may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" municipal securities taken as a whole.

The proposed guidance provides that a "similar" municipal security should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor. At a minimum, the municipal security or securities should be sufficiently similar that a market yield for the subject security can be fairly estimated from the yields of the "similar" security or securities. Where a municipal security has several components, appropriate consideration may also be given to the prices or yields of the various components of the security. The proposed guidance also sets forth a number of non-exclusive factors that may be used in determining the degree to which a security is "similar." These include: (i) credit quality considerations;[37] (ii) the extent to which the spread at which the "similar" municipal security trades is comparable to the spread at which the subject security trades; (iii) general

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[37] Credit quality considerations include, but are not limited to, whether the municipal security is issued by the same or similar entity, bears the same or similar credit rating, or is supported by a similarly strong guarantee or collateral as the subject security (to the extent securities of other issuers are designated as "similar" securities, significant recent information concerning either the "similar" security's issuer or subject security's issuer that is not yet incorporated in credit ratings should be considered (e.g., changes to ratings outlooks)).

structural characteristics and provisions of the issue;[38] (iv) technical factors such as the size of the issue, the float and recent turnover of the issue, and legal restrictions on transferability as compared with the subject security; and (v) the extent to which the federal and/or state tax treatment of the "similar" municipal security is comparable to such tax treatment of the subject security.

Because of the unique characteristics of the municipal securities market, including the large number of vastly different issuers and the highly diverse nature of most outstanding securities, the MSRB expects that, in order for a security to qualify as sufficiently "similar" to the subject security, such security will be at least highly similar to the subject security with respect to nearly all of the listed "similar" security factors that are relevant to the subject security at issue. The MSRB believes that this recognition of a practical aspect of the municipal securities market supports a more rational comparison of a municipal security to only those that are likely to produce relevant and probative pricing information in determining the prevailing market price of the subject security. Pricing information, for example, for a taxable security will not be useful in evaluating a tax-exempt security without making some price adjustment for that difference, which would constitute a form of economic modeling that is not permitted except at the next level of the waterfall analysis. The same is true, just as additional examples, of a bond versus another with a different credit rating, a general obligation bond versus a revenue bond, a bond with bond insurance versus one without, a bond with a sinking fund versus one without, and a bond with a call provision versus one without. As a result of these practical aspects, and due also in part to the lack of active trading in many municipal securities, dealers in the municipal

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[38] General structural characteristics and provisions of the issue include, but are not limited to, coupon, maturity, duration, complexity or uniqueness of the structure, callability, the likelihood that the municipal security will be called, tendered or exchanged, and other embedded options, as compared with the characteristics of the subject security.

securities market likely may not often find pricing information from sufficiently similar securities and may frequently need to then consider economic models at the next level of the waterfall analysis.

When a security's value and pricing is based substantially on, and is highly dependent on, the particular circumstances of the issuer, including creditworthiness and the ability and willingness of the issuer to meet the specific obligations of the security (often referred to as "story bonds"), in most cases other securities would not be sufficiently similar, and therefore, other securities may not be used to establish the prevailing market price.

Economic Models. If information concerning the prevailing market price of a security cannot be obtained by applying any of the factors at the higher levels of the waterfall, dealers may consider as a factor in assessing the prevailing market price of a security the prices or yields derived from economic models. Such economic models may take into account measures such as reported trade prices, credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value, and may consider all applicable pricing terms and conventions used.[39]

Isolated Transactions and Quotations. The ultimate issue the proposed guidance is intended to address is the prevailing market price of the security; therefore, isolated transactions

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[39] Consistent with FINRA's commentary with respect to other fixed income securities, when a dealer seeks to identify prevailing market price using other than the dealer's contemporaneous cost or contemporaneous proceeds, the dealer must be prepared to provide evidence that would establish the dealer's basis for not using contemporaneous cost (proceeds), and information about the other values reviewed (e.g., the specific prices and/or yields of securities that were identified as similar securities) in order to determine the prevailing market price of the subject security. If a dealer relies upon pricing information from a model the dealer uses or has developed, the dealer must be able to provide information that was used on the day of the transaction to develop the pricing information (i.e., the data that was input and the data that the model generated and the dealer used to arrive at prevailing market price). See supra n. 35, FINRA Notice of Filing of Amendments Related to Mark-Up Policy.

or isolated quotations generally would have little or no weight or relevance in establishing the prevailing market price. Due to the unique nature of the municipal securities market, including the large number of issuers and outstanding securities and the infrequent trading of many securities in the secondary market, the proposed guidance recognizes that isolated transactions and quotations may be more prevalent in the municipal securities market than other fixed income markets and explicitly recognizes that an off-market transaction may qualify as an "isolated transaction" under the proposed guidance.

The proposed guidance also addresses the application of the "isolated" transactions and quotations provision. The proposed guidance explains that, for example, in considering the factors in the hierarchy of pricing factors, a dealer may give little or no weight to pricing information derived from an isolated transaction or quotation. The proposed guidance also provides that, in considering yields of "similar" securities, except in extraordinary circumstances, dealers may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" municipal securities taken as a whole.

Contemporaneous Customer Transactions

Because the proposed guidance ultimately seeks to identify the prevailing inter-dealer market price, a dealer's contemporaneous cost (for customer sales) or proceeds (for customer purchases) in an inter-dealer transaction is presumptively the prevailing market price of the security. Where the dealer has no contemporaneous cost or proceeds, as applicable, from an inter-dealer transaction, the dealer must then consider whether it has contemporaneous cost or proceeds, as applicable, from a customer transaction. In establishing the presumptive prevailing market price, in such instances, the dealer should refer to such contemporaneous cost or proceeds

and make an adjustment for any mark-up or mark-down charged in that customer transaction. This methodology for establishing the presumptive prevailing market price is appropriate because, as explained in the relevant case law, it reflects the fact that the price at which a dealer, for example, purchases securities from customers generally is less than the amount that the dealer would have paid for the security in the inter-dealer market. To identify the prevailing market price for the purpose of calculating the mark-up or mark-down in the contemporaneous customer transaction, the dealer should proceed down the waterfall, according to its terms, identifying the most relevant and probative evidence of the prevailing inter-dealer market price.

This approach is supported by the relevant case law, in which the prevailing market price has been established by reference to a customer price by adjusting the customer price based on an "imputed" mark-up or mark-down.[40] This approach is also consistent with the text of the proposed guidance because the presumptive prevailing market price is, through this methodology, established "by referring to" the dealer's contemporaneous cost or proceeds, as required by proposed Supplementary Material .06(a)(i).[41] Moreover, this approach is consistent

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40 In a number of instances, where a dealer lacked contemporaneous inter-dealer transactions, the prevailing market price in connection with a sale to a customer was calculated by identifying contemporaneous cost from a transaction with another customer and then making an upward adjustment. The adjustment, referred to in the cases as an "imputed markdown," was then added to the dealer's purchase price from the customer to establish pricing at the level at which an inter-dealer trade might have occurred. Similarly, in determining the prevailing market price of a municipal security in connection with a purchase from a customer, the prevailing market price was determined by identifying the dealer's contemporaneous proceeds in a transaction with another customer, and then making a downward adjustment by deducting an "imputed mark-up" from such contemporaneous proceeds.

41 For example, assume that Dealer A sells municipal security X to Dealer B at a price of 98.5. Then, assume that Dealer C purchases municipal security X from a customer at a price of 98 and contemporaneously sells the security to a customer at a price of 100. Because Dealer C itself has no other contemporaneous transactions in the security, it would proceed down the waterfall to the hierarchy of pricing factors, discussed supra. A

with the fundamental principle underlying the proposed guidance, because it results in a reasonable proxy for what the dealer's contemporaneous cost or proceeds would have been in an inter-dealer transaction. Indeed, because this adjustment methodology occurs at the first step of the waterfall analysis (proposed Supplementary Material .06(a)(i)), the resulting price from this methodology is presumed to be the prevailing market price for any contemporaneous transactions with the same strength of the presumption that applies to prices from inter-dealer transactions.

This interpretation of the proposed prevailing market price guidance takes on special significance in the context of a mark-up disclosure requirement, such as contained in the proposed amendments to Rule G-15. Where, for example, a dealer purchases a security from one retail customer and contemporaneously sells it to another retail customer, with no relevant market changes in the interim, the total difference between the two prices may be attributed to dealer compensation, but each customer pays only a portion of this difference (as either a mark-up or a mark-down). Without adjustments to the contemporaneous cost and proceeds based on the mark-down and mark-up, respectively, the confirmation disclosures to both customers would reflect "double counting." By contrast, under the adjustment approach, where there are no

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dealer at that level of the waterfall analysis must first consider prices of any contemporaneous inter-dealer transaction in establishing the prevailing market price. Accordingly, Dealer C would consider the contemporaneous inter-dealer transaction between Dealer A and Dealer B at 98.5 in determining the amount of the mark-down, and deduct its contemporaneous cost of 98 from 98.5 to arrive at a mark-down of 0.5. Then, Dealer C would add the amount of the mark-down to the dealer's contemporaneous cost for a presumptive prevailing market price (or adjusted contemporaneous cost) of 98.5. In the absence of evidence to rebut the presumption, when disclosing the mark-up to the customer to whom Dealer C sold municipal security X, Dealer C would then disclose the difference between Dealer C's adjusted contemporaneous cost (98.5) and the price paid by the customer to whom Dealer C sold municipal security X (100) for a mark-up of 1.5 (1.02% of the prevailing market price).

relevant market changes in the interim that would rebut the presumption, there is a complete apportionment of the total difference in price (i.e., no double counting and no part of the total difference in price left undisclosed to either customer).

Non-Arms-Length Affiliate Transactions. The ultimate issue the proposed guidance is intended to address is the prevailing market price of the security, using the most relevant and probative evidence of the market price in the inter-dealer market. Therefore, as noted in the discussion above of the mark-up disclosure requirement, a non-arms-length transaction in a security (as defined in that context) with an affiliate should not be used to identify a dealer's contemporaneous cost or proceeds and presumptively the prevailing market price of the security. The MSRB believes that, for example, sourcing liquidity through a non-arms-length transaction with an affiliate is functionally equivalent to selling out of a dealer's own inventory for purposes of the calculation of the mark-up. The MSRB therefore believes it would be appropriate in those circumstances to require a dealer to "look through" its transaction in a security with its affiliate to the affiliate's transaction(s) in the security with third parties and the related time of trade and cost or proceeds of the affiliate in determining the dealer's calculation of the mark-up pursuant to Rule G-30. This is the case not only for transactions for which mark-up disclosure would be required under the proposed amendments to Rule G-15, but for the application of proposed amended Rule G-30 generally, including the proposed prevailing market price guidance, for purposes of evaluating the fairness and reasonableness of mark-ups and mark-downs.[42]

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[42] For example, assume Dealer A1, a market-facing dealer, and Dealer A2, a retail customer-facing dealer, are affiliates both owned by Company A. On the same trading day, Dealer A1 purchases municipal security X from an unaffiliated dealer at $90 ("Transaction 1"). Dealer A1 displays municipal security X for sale at $93 on Dealer A2's customer-facing platform, on which other dealers have not frequently participated. A retail customer places an order to purchase municipal security X from Dealer A2 at the displayed price of $93. Dealer A2 purchases municipal security X from Dealer A1 at $93

Compliance at the Time of Generation of Disclosure. As noted, the MSRB understands that some dealers provide confirmations on an intra-day basis. The requirement under the proposed amendments to Rule G-15 to disclose a mark-up or mark-down calculated "in compliance with" Rule G-30 (including the proposed prevailing market price guidance) need not delay the confirmation process. A dealer may determine, as a final matter for disclosure purposes, the prevailing market price based on the information the dealer has, based on the use of reasonable diligence as required by proposed amended Rule G-30, at the time the dealer inputs the information into its systems to generate the mark-up disclosure.[43] Such timing of the determination of prevailing market price would avoid potentially open-ended delays that could otherwise result if dealers were required to wait to generate a disclosure until they could

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in a non-arms-length transaction within the meaning of proposed amended Rule G-15 ("Transaction 2"). Dealer A2 then sells municipal security X to the retail customer at $93, plus $1 trading fee ("Transaction 3"). During the day, there are no other transactions in municipal security X and no other dealers display any price for municipal security X. In this example, Transaction 2 should not be used to indicate Dealer A2's contemporaneous cost. Instead, Dealer A2 would be required to "look through" Transaction 2, a non-arm's length transaction with affiliated Dealer A1, and use Transaction 1 and the time of that trade and the related cost to Dealer A1 in determining the prevailing market price.

[43] For example, assume Dealer A systematically inputs the mark-up-related information into its systems intra-day for the generation of confirmations. At 9:00 AM, Dealer A purchases municipal security X from a customer at a price of 98. At 1:00 PM, Dealer A sells such security to another dealer at a price of 100. Dealer A does not sell municipal security X at any other time before 1:00 PM. At the time of the 9:00 AM transaction, Dealer A does not have any contemporaneous proceeds for municipal security X. Therefore, to determine the prevailing market price for municipal security X, Dealer A would proceed down the waterfall to the next category of factors—in this case, the hierarchy of pricing factors, as discussed supra. Dealer A would not be required to consider the price of 100, which the dealer would only know at 1:00 PM. In contrast, assuming instead that Dealer A systematically inputs the mark-up-related information into its systems for confirmation generation at the end of the day, under the same facts as above, it would be required to consider, to the extent required by the prevailing market price guidance, the 1:00 PM inter-dealer trade price in determining the prevailing market price and the related mark-down to be disclosed for the 9:00 AM purchase.

determine, for example, that they do not have any "contemporaneous" proceeds for a particular transaction. Such timing would also permit dealers who, on a voluntary basis, choose to disclose mark-ups and mark-downs on all principal transactions to generate customer confirmations at the time of trade, should they choose to do so. To clarify, a dealer would not be expected to cancel and resend a confirmation to revise the mark-up or mark-down disclosure solely based on the occurrence of a subsequent transaction or event that would otherwise be relevant to the calculation of the mark-up or mark-down under the proposed guidance. Where, however, a dealer has contemporaneous proceeds by the time of generation of the disclosure, the dealer presumptively must establish the prevailing market price of the municipal security by reference to such contemporaneous proceeds.[44]

Consideration of Benefits and Costs

The MSRB believes that requiring dealers to disclose their mark-ups on retail customer confirmations based on the proposed amendments to Rule G-30 would provide meaningful and useful pricing information to a significant number of retail investors and may lower transaction costs for retail transactions. The MSRB also believes that the proposed amendments would provide retail customers engaged in municipal securities transactions covered by the rule with information more comparable to that currently received by retail customers in equity securities

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[44] For example, a dealer that operates an alternative trading system or ATS may often, if not always, be in a position to identify its contemporaneous proceeds in connection with a purchase from a customer. Also, as discussed in supra n. 18, under Rule G-18, Supplementary Material .03, a dealer must make every effort to execute a customer transaction promptly, taking into account prevailing market conditions. Any intentional delay of a transaction to avoid recognizing proceeds as contemporaneous at the time of a transaction or otherwise would be contrary to these duties to customers. A dealer found to purposefully delay the execution of a customer order for such purposes also may be in violation of Rule G-17, on conduct of municipal securities and municipal advisory activities.

transactions and municipal securities transactions in which the dealer acts in an agent capacity. In addition, the disclosure may improve investor confidence, better enable customers to evaluate the costs and quality of the execution service that dealers provide, promote transparency into dealers' pricing practices, improve communication between dealers and their customers, and make the enforcement of Rule G-30 more efficient.

The MSRB believes that the proposed amendments to Rule G-30 reflect an appropriate balance between consistency with existing FINRA guidance for determining prevailing market price in other fixed income securities markets and modifications to address circumstances under which use of the FINRA guidance in the municipal securities market might be inappropriate (e.g., treatment of similar securities).[45] The MSRB also believes that the guidance would promote consistent compliance by dealers with their existing fair-pricing obligations under MSRB rules and would support effective compliance with the proposed amendments to Rule G-15.

The MSRB recognizes, however, that the proposed rule change, comprised of amendments to both Rule G-15 and Rule G-30, would impose burdens and costs on dealers.[46] In MSRB Notices 2014-20, 2015-16 and 2016-07, the MSRB specifically solicited comment on the

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45 For example, the municipal securities market includes a larger number of issuers and larger number of outstanding securities than the corporate bond market, and most municipal securities trade less frequently in the secondary market. In addition, many municipal securities are subject to different tax rules and treatment, and have different credit structures, enhancements and redemption features that may not be applicable to or prevalent for other fixed income securities.

46 The MSRB's evaluation of the potential costs does not consider all of the costs associated with the proposal, but instead focuses on the incremental costs attributable to it that exceed the baseline state. The costs associated with the baseline state are, in effect, subtracted from the costs associated with the proposed rule change to isolate the costs attributable to the incremental requirements of the proposal.

potential costs of the draft amendments contained in those notices. While commenters stated that the initial and the revised confirmation disclosure proposals would impose significant implementation costs, no commenters provided specific cost estimates, data to support cost estimates, or a framework to assess anticipated costs.

Among other things, the proposed rule change would require dealers to develop and deploy a methodology to satisfy the disclosure requirement, identify trades subject to the disclosure, convey the mark-up on the customer confirmation, determine the prevailing market price and the mark-up, and adopt policies and procedures to track and ensure compliance with the requirement. To apply the "look through" to non-arms-length transactions with affiliates, dealers also would need to obtain the price paid or proceeds received and the time of the affiliate's trade with the third party. The MSRB sought data in the above-referenced notices that would facilitate quantification of these costs, but did not receive any data from commenters.

Any such costs, however, may be mitigated under certain circumstances. Dealers choosing to provide disclosure on all customer transactions would not incur the cost associated with identifying trades subject to the disclosure requirement; dealers already disclosing mark-ups to retail customers likely would incur lower costs associated with modifying customer confirmations, and dealers with processes in place to evaluate prevailing market price in compliance with FINRA Rule 2121 and MSRB Rule G-30 may be able to leverage those processes to comply with the proposed amendments to Rule G-30.

Based on comments received in response to the Notices, the MSRB made a number of changes to the draft amendments in an effort to make implementation less burdensome. These changes include utilizing existing processes for identifying retail customers, providing detailed prevailing market price guidance alongside the mark-up disclosure proposal, and ensuring that

prevailing market price could be determined in the least burdensome way among the reasonable alternatives.

The MSRB believes that the proposed rule change reflects the overall lowest cost approach to achieving the regulatory objective. To reach that conclusion, the MSRB evaluated several reasonable regulatory alternatives including relying solely on modifications to EMMA, requiring the disclosure of a "reference price" rather than mark-up, and providing only a mark-up disclosure rule without accompanying prevailing market price guidance. These alternatives were deemed to either not sufficiently address the identified need (in the case of the EMMA alternative) or to represent approaches that offered lesser benefits and greater costs.

2. Statutory Basis

The MSRB believes that the proposed rule change is consistent with the provisions of Section 15B(b)(2)(C) of the Act,[47] which provides that the MSRB's rules shall:

> be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2)(C) of the Act[48] because it would provide retail customers with meaningful and useful additional pricing information that retail customers typically cannot readily obtain through existing data sources such as EMMA. This belief is supported by the joint investor testing, which indicated that investors would find aspects of the proposed requirements useful, including

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47 15 U.S.C. 78o-4(b)(2)(C).

48 Id.

disclosure of the time of execution and mark-up or mark-down in a municipal securities transaction both as a dollar amount and as a percentage of the prevailing market price. The MSRB believes that a reference and hyperlink to the Security Details page of EMMA, along with a brief description of the type of information available on that page, will provide retail investors with a more comprehensive picture of the market for a security on a given day and believes that requiring a link to EMMA would increase investors' awareness of, and ability to access, this information. Additionally, results from the joint investor survey support the value to investors of a security-specific link to EMMA, rather than a link to the EMMA homepage. The MSRB believes that the proposed rule change will better enable customers to evaluate the cost of the services that dealers provide by helping customers understand mark-ups or mark-downs from the prevailing market prices in specific transactions. The MSRB also believes that this type of information will promote transparency into dealers' pricing practices and encourage communications between dealers and their customers about the execution of their municipal securities transactions. The MSRB further believes the proposed rule change will provide customers with additional information that may assist them in detecting practices that are possibly improper, which would supplement existing municipal securities enforcement programs.

The proposed amendment to Supplementary Material .01(a) to Rule G-30 will clarify the applicable "reasonable diligence" standard in that provision and conform to existing supplementary material referencing that standard. The proposed amendments to Supplementary Material .01(d) to Rule G-30 will clarify the relationship between that provision and the new proposed Supplementary Material .06 containing the proposed prevailing market price guidance and aid in understanding of the overall rule.

The proposed guidance on prevailing market price will provide dealers with additional guidance for determining prevailing market price in order to aid in compliance with their fair-pricing and mark-up disclosure obligations. The MSRB believes that clarifying the standard for correctly identifying the prevailing market price of a municipal security for purposes of calculating a mark-up, clarifying the additional obligations of a dealer when it seeks to use a measure other than the dealer's own contemporaneous cost (proceeds) as the prevailing market price and confirming that similar securities and economic models may be used in certain instances to determine the prevailing market price are measures designed to remove impediments to and perfect the mechanism of a free and open market in municipal securities, prevent fraudulent practices, promote just and equitable principles of trade and protect investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

Section 15B(b)(2)(C)[49] of the Act requires that MSRB rules not be designed to impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

The MSRB believes that the proposed rule change will improve price transparency and foster greater price competition among dealers. The MSRB recognizes that some dealers may exit the market or consolidate with other dealers as a result of the costs associated with the proposed rule change relative to the baseline. However, the MSRB does not believe—and is not aware of any data that suggest—that the number of dealers exiting the market or consolidating would materially impact competition.

Some commenters noted that the requirement to make a disclosure to retail customers if the dealer engaged in both the retail customer's transaction and one or more offsetting

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49 Id.

transactions on the same day could disproportionately impact smaller dealers as larger dealers might be more able to hold positions overnight and not trigger the proposed disclosure requirement. The MSRB has noted that any intentional delay of a customer execution to avoid a disclosure requirement would be contrary to a dealer's obligations under Rules G-30, G-18, on best execution, and G-17, on conduct of municipal securities and municipal advisory activities. If the proposed amendments are approved, the MSRB expects that FINRA would monitor trading patterns to ensure dealers are not purposely delaying a customer execution to avoid the disclosure.

Although commenters did not provide any data to support a quantification of the costs associated with these proposals, commenters did indicate that the costs associated with modifying systems to comply with these proposals would be significant. It is possible that larger dealers may be better able to absorb these costs than smaller dealers and that smaller dealers could be forced to exit the market or pass a larger share of the implementation costs on to customers. The MSRB believes that these concerns may be mitigated by several factors. As noted above, dealers choosing to disclose to all customers may not incur the costs associated with identifying transactions that require disclosure and dealers engaging in relatively fewer transactions may be able to develop processes for determining prevailing market price that are relatively less costly than larger, more active dealers. In addition, the MSRB believes that smaller dealers are more likely to have their customer confirmations generated by clearing firms. To the extent that clearing firms would not pass along the full implementation cost to each introducing firm, small firms may incur lower costs in certain areas than large firms.

The proposed rule change may disproportionately impact less active dealers that, as indicated by data, currently charge relatively higher mark-ups than more active dealers.

However, overall, the MSRB believes that the burdens on competition will be limited and the proposed rule change will not impose any additional burdens on competition that are not necessary or appropriate in furtherance of the purposes of the Act. In addition, the MSRB believes that the proposed rule change may foster additional price competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Proposed Amendments to Rule G-15

The revised confirmation disclosure proposal was published for comment in MSRB Notice 2015-16 (September 24, 2015), and was preceded by the initial confirmation disclosure proposal in MSRB Notice 2014-20 (November 17, 2014). The MSRB received 30 comments in response to MSRB Notice 2014-20,[50] and 25 comments in response to MSRB Notice 2015-16.[51]

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50 See Letter from Eric Bederman, Chief Operating and Compliance Officer, Bernardi Securities, dated December 26, 2014 ("Bernardi Letter I"); Letter from Michael Nicholas, Chief Executive Officer, Bond Dealers of America, dated January 20, 2015 ("BDA Letter I"); Letter from Chris Melton, Executive Vice President, Coastal Securities, dated January 16, 2015 ("Coastal Securities Letter I"); Letter from Micah Hauptman, Financial Services Counsel, Consumer Federation of America, dated January 20, 2015 ("CFA Letter I"); Letter from Larry E. Fondren, President and Chief Executive Officer, DelphX LLC, dated January 7, 2015 ("DelphX Letter I"); Letter from Herbert Diamant, President, Diamant Investments Corp., dated January 9, 2015 ("Diamant Letter I"); Letter from Norman L. Ashkenas, Chief Compliance Officer, Fidelity Brokerage Services LLC and Richard J. O'Brien, Chief Compliance Officer, National Financial Services, LLC, Fidelity Investments, dated January 20, 2015 ("Fidelity Letter I"); Letter from Darren Wasney, Program Manager, Financial Information Forum, dated January 20, 2015 ("FIF Letter I"); Letter from David T. Bellaire, Executive Vice President and General Counsel, Financial Services Institute, dated January 20, 2015 ("FSI Institute Letter I"); Letter from Rich Foster, Vice President and Senior Counsel for Regulatory and Legal Affairs, Financial Services Roundtable, dated January 20, 2015 ("Financial Services Roundtable Letter I"); Emails from Gerald Heilpern, dated December 9, 2014, December 18, 2014 and January 8, 2015 (collectively "Heilpern Letter I"); Letter from Alexander I. Rorke, Senior Managing Director, Municipal Securities Group, Hilliard Lyons, dated January 20, 2015 ("Hilliard Letter I"); Letter from Thomas E. Dannenberg, President and Chief Executive Officer, Hutchinson Shockey Erley and Co., dated January 20, 2015 ("Hutchinson Shockey Letter I"); Letter from Andrew Hausman, President, Pricing & Reference Data, Interactive Data, dated January 20, 2015 ("Interactive Data Letter I");

Email from John Smith, dated December 10, 2014 ("Smith Letter I"); Email from Jorge Rosso, dated November 24, 2014 ("Rosso Letter I"); Letter from Karin Tex, dated January 12, 2015 ("Tex Letter I"); Email from George J. McLiney, Jr., McLiney and Company, dated December 22, 2014 ("McLiney Letter I"); Letter from Vincent Lumia, Managing Director, Morgan Stanley Smith Barney LLC, dated January 20, 2015 ("Morgan Stanley Letter I"); Letter from Peter G. Brandel, Senior Vice President, Municipal Bond Trading, and Kenneth T. Kerr, Senior Vice President, Municipal Bond Trading, Nathan Hale Capital, LLC, dated January 20, 2015 ("Nathan Hale Letter I"); Letter from Rick A. Fleming, Investor Advocate, Office of the Investor Advocate, U.S. Securities and Exchange Commission, dated January 20, 2015 ("SEC Investor Advocate Letter I"); Email from Private Citizen, dated November 23, 2014 ("Private Citizen Letter I"); Letter from Richard Seelaus, R. Seelaus & Co., Inc., dated January 8, 2015 ("R. Seelaus Letter I"); Email from Paige Pierce, RW Smith & Associates, LLC, dated January 21, 2015 ("RW Smith Letter I"); Letter from Sean Davy, Managing Director, Capital Markets Division, and David L. Cohen, Managing Director and Associate General Counsel, Municipal Securities Division, Securities Industry and Financial Markets Association, dated January 20, 2015 ("SIFMA Letter I"); Letter from Gregory Carlin, Vice President, Standard & Poor's Securities Evaluations, Inc., dated January 20, 2015 (S&P Letter I"); Letter from Kyle C. Wootten, Deputy Director – Compliance and Regulatory, Thomson Reuters, dated January 16, 2015 ("Thomson Reuters Letter I"); Letter from Robert J. McCarthy, Director of Regulatory Policy, Wells Fargo Advisors, LLC, dated January 20, 2015 ("Wells Fargo Letter I").

51 See Email from Aaron Botbyl, dated October 9, 2015 ("Botbyl Letter II"); Letter from Eric Bederman, Senior Vice President, Chief Operating and Compliance Officer, Bernardi Securities, Inc., dated December 4, 2015 ("Bernardi Letter II"); Letter from Michael Nicholas, Chief Executive Officer, Bond Dealers of America, dated December 11, 2015 ("BDA Letter II"); Letter from Kurt N. Schacht, Managing Director, Standards and Financial Market Integrity, and Linda L. Rittenhouse, Director, Capital Markets Policy, CFA Institute, dated December 11, 2015 ("CFA Institute Letter II"); Letter from Jason Clague, Senior Vice President, Trading & Middle Office Services, Charles Schwab & Co. Inc., dated December 11, 2015 ("Schwab Letter II"); Email from Chris Melton, Coastal Securities, dated October 30, 2015 ("Coastal Securities Letter II"); Email from Christopher [Last Name Withheld], dated September 25, 2015 ("Christopher Letter II"); Letter from Micah Hauptman, Financial Services Counsel, Consumer Federation of America, dated December 11, 2015 ("CFA Letter II"); Letter from Herbert Diamant, President, Diamant Investment Corporation, dated November 30, 2015 ("Diamant Letter II"); Letter from Norman L. Ashkenas, Chief Compliance Officer, Fidelity Brokerage Services, LLC, and Richard J. O'Brien, Chief Compliance Officer, National Financial Services, LLC, Fidelity Investments, dated December 11, 2015 ("Fidelity Letter II"); Letter from Darren Wasney, Program Manager, Financial Information Forum, dated December 11, 2015 ("FIF Letter II"); Letter from David T. Bellaire, Executive Vice President & General Counsel, Financial Services Institute, dated December 11, 2015, ("FSI Institute Letter II"); Letter from Gerald Heilpern, undated ("Heilpern Letter II"); Email from Jonathan Bricker, dated October 20, 2015; Letter from David P. Bergers,

A copy of MSRB Notice 2014-20 is attached as Exhibit 2a; a list of comment letters received in response is attached as Exhibit 2b; and copies of the comment letters are attached as Exhibit 2c. A copy of MSRB Notice 2015-16 is attached as Exhibit 2d; a list of comment letters received in response is attached as Exhibit 2e; and copies of the comment letters are attached as Exhibit 2f.

Summary of Initial Confirmation Disclosure Proposal and Comments Received

As proposed in MSRB Notice 2014-20, for same-day principal transactions in municipal securities, dealers would have been required 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. The initial proposal would have applied where the transaction with the customer involved 100 bonds or fewer or bonds in a par amount of $100,000 or less, which was designed to capture those trades that are retail in nature.

Of the 30 comments the MSRB received on the proposal, six supported the proposal, while 24 commenters generally opposed the proposal or made recommendations on ways to

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General Counsel, LPL Financial LLC, dated December 10, 2015 ("LPL Letter II"); Letter from Elizabeth Dennis, Managing Director, Morgan Stanley Smith Barney LLC, dated December 11, 2015 ("Morgan Stanley Letter II"); Letter from Rick A. Fleming, Investor Advocate, Office of the Investor Advocate, U.S. Securities and Exchange Commission, dated December 11, 2015 ("SEC Investor Advocate Letter II"); Letter from Patrick Luby, dated December 11, 2015 ("Luby Letter II"); Letter from Hugh D. Berkson, President, Public Investors Arbitration Bar Association, dated December 8, 2015 ("PIABA Letter II"); Letter from David L. Cohen, Senior Counsel and Director, RBC Capital Markets, LLC, dated December 15, 2015 ("RBC Letter II"); Letter from Paige W. Pierce, President & Chief Executive Officer, RW Smith and Associates, LLC, dated December 11, 2015 ("RW Smith Letter II"); Letter from Sean Davy, Managing Director, Capital Markets Division, and Leslie M. Norwood, Managing Director & Associate General Counsel, Municipal Securities Division, Securities Industry and Financial Markets Association, dated December 11, 2015 ("SIFMA Letter II"); Letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, Thomson Reuters, dated December 11, 2015 ("Thomson Reuters Letter II"); Letter from Thomas S. Vales, Chief Executive Officer, TMC Bonds LLC, dated December 11, 2015 ("TMC Bonds Letter II"); Letter from Robert J. McCarthy, Director of Regulatory Policy, Wells Fargo Advisors LLC, dated December 11, 2015 ("Wells Fargo Letter II").

narrow substantially the scope of the proposal. Generally, commenters that supported the proposal stated that the proposed confirmation disclosure would provide additional post-trade information to investors that would be otherwise difficult to ascertain.[52] Three commenters, including the Consumer Federation of America and the SEC Investor Advocate, stated that this additional information would put investors in a better position to assess whether they are paying fair prices and the quality of the services provided by their dealer, and also could assist investors in detecting improper practices.[53] The Consumer Federation of America indicated that the proposal would foster increased price competition in fixed income markets, which would ultimately lower investors' transaction costs.[54] Two commenters recommended that the proposal not be limited to retail trades under the proposed size threshold, but that disclosure should be made on all trades involving retail customers, regardless of size.[55]

Other commenters opposed the proposal on several grounds. Commenters questioned whether the proposed disclosure would provide investors with useful information,[56] or whether the disclosure would simply create confusion among investors.[57] Commenters asserted that the proposed methodology for determining the reference transaction would be overly complex[58] and

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52 See, e.g., SEC Investor Advocate Letter I at 1-2.

53 See CFA Letter I at 1; DelphX Letter I at 2; SEC Investor Advocate Letter I at 2.

54 See CFA Letter I at 1.

55 See Hutchinson Shockey Letter I at 2; Thomson Reuters Letter I at 7.

56 See Diamant Letter I at 5.

57 See BDA Letter I at 4-5; FSI Institute Letter I at 3; Morgan Stanley Letter I at 2; SIFMA Letter I at 17; Wells Fargo Letter I at 5.

58 See Fidelity Letter I at 4; FIF Letter I at 2; SIFMA Letter I at 24-26; Thomson Reuters Letter I at 2; Wells Fargo Letter I at 8.

costly for dealers to implement.[59] Commenters also indicated the proposal could impair liquidity in the municipal market.[60]

Several commenters suggested ways to narrow the scope of the proposal. Some commenters recommended that the MSRB limit the disclosure obligation to riskless principal transactions involving retail investors, as this would more accurately reflect dealer compensation and transaction costs,[61] and would be more consistent with the stated objectives of the SEC in this area and of the proposal itself.[62] Some commenters suggested that the proposed rule should apply to riskless principal transactions as previously defined by the Commission for equity trades, wherein the dealer has an "order in hand" at the time of execution.[63] One commenter, however, did not think that such a limitation would appreciably reduce the complexity or cost of the proposal.[64] Commenters also suggested that the MSRB eliminate institutional trades from the scope of the proposal: for example, by not covering institutional accounts as defined in Rule G-8(a)(xi) or sophisticated municipal market professionals ("SMMP") as defined in MSRB Rule D-

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59 See BDA Letter I at 2-3; Diamant Letter I at 7-8; Fidelity Letter I at 4-5; FIF Letter I at 2; FSI Institute Letter I at 5; Financial Services Roundtable Letter I at 5; Morgan Stanley Letter I at 3; Wells Fargo Letter I at 7-9.

60 See Diamant Letter I at 8-9; FSI Institute Letter I at 3.

61 See Hilliard Letter I at 2; Morgan Stanley Letter I at 2; SIFMA Letter I at 29; Wells Fargo Letter I at 11.

62 See SIFMA Letter I at 31.

63 See Hilliard Letter I at 2; SIFMA Letter I at 30; Wells Fargo Letter I at 11.

64 See Thomson Reuters Letter I at 7.

15.[65] Both Fidelity and SIFMA stated that the proposal should permit trading desks that are separately operated within a firm to match only their own trades for purposes of pricing disclosure.[66] Morgan Stanley and SIFMA also stated that transactions between affiliates should not constitute a firm principal trade that, if accompanied by a same-day customer trade, would trigger the disclosure requirement.[67] Commenters also suggested that the proposal exempt the disclosure of mark-ups on new issues.[68] One commenter suggested specifically that this exemption should cover transactions in new issues executed at the public offering price on the date of the issue's sale.[69]

Rather than proposing pricing reference disclosure, several commenters suggested that the MSRB instead enhance EMMA, in part by providing greater investor education about EMMA,[70] and requiring dealers to make EMMA more accessible[71] by, for example, providing

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65 See BDA Letter I at 6; FIF Letter I at 3; Morgan Stanley Letter I at 3; SIFMA Letter I at 35.

66 See Fidelity Letter I at 8; SIFMA Letter I at 36.

67 See Morgan Stanley Letter I at 3; SIFMA Letter I at 21.

68 See BDA Letter I at 6; Coastal Securities Letter I at 1; SIFMA Letter I at 22.

69 See Coastal Securities Letter I at 1.

70 See Fidelity Letter I at 7; FSI Institute Letter I at 6-7; Financial Services Roundtable Letter I at 6; Hilliard Letter I at 2-3; Morgan Stanley Letter I at 2; SIFMA Letter I at 15-16.

71 See Thomson Reuters Letter I at 6.

more near-real-time EMMA information to investors[72] or providing a link to EMMA on customer confirmations,[73] or by aggregating all TRACE and EMMA data on a single website.[74]

Summary of Revised Confirmation Disclosure Proposal and Comments Received

In response to the comments received on MSRB Notice 2014-20, the MSRB proposed a different disclosure standard that was built upon the framework of the initial confirmation disclosure proposal, but modified a number of its key aspects and added several exceptions to the proposed disclosure requirement.[75]

First, in response to concerns that the disclosures may be misconstrued by investors who may equate them with mark-ups or believe that they are always reflective of contemporaneous market conditions, the MSRB proposed requiring dealers to disclose the amount of mark-up or mark-down, as calculated from the prevailing market price for the security, rather than disclose the difference between the customer's price and the dealer's price in a reference transaction. The MSRB also proposed that the mark-up or mark-down disclosure be expressed as a total dollar amount and as a percentage.

Second, the MSRB proposed to narrow the disclosure time window from a same-day disclosure standard to a two-hour disclosure standard. Thus, mark-up disclosure would be required only where the dealer's same-side of the market transaction occurs within the two hours preceding or following the customer transaction. The MSRB explained that it believed that such a time frame would be sufficient to cover transactions that could be considered "riskless

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72 See Wells Fargo Letter I at 7.

73 See Fidelity Letter I at 7; FSI Institute Letter I at 6; Hilliard Letter I at 3; Morgan Stanley Letter I at 2; SIFMA Letter I at 15-16.

74 See FIF Letter I at 4.

75 See MSRB Notice 2015-16 (September 24, 2015).

principal" transactions under any current market understanding of the term, but that it was not proposing a broader same-day trigger out of concern about the potential for additional costs and complexities associated with a broader disclosure time trigger. However, the MSRB specifically sought public comment as to whether a broader disclosure time trigger, such as a same-day standard, might be warranted.

Third, the MSRB proposed to replace the transaction size retail-customer proxy (i.e., 100 bonds or fewer or bonds in a par amount of $100,000 or less) proposed in the initial confirmation disclosure proposal with a status-based exclusion for transactions that involve an institutional account, as defined in Rule G-8(a)(xi). This would ensure that all eligible transactions involving retail customers, regardless of size or par amount, would be subject to the proposed disclosure and was responsive to dealer concerns about using disparate definitions of a retail customer.

Fourth, the MSRB proposed to require the disclosure of two additional data points, even if mark-up disclosure would not be required under the MSRB's proposal. The MSRB proposed to require that: (i) dealers add a CUSIP-specific link to EMMA on all customer confirmations and (ii) dealers disclose the time of execution of a customer's trade on all customer confirmations. These disclosures were intended to provide context for the mark-up disclosures received by providing retail customers with a comprehensive view of the market for their security, including the market as of the time of trade. They were also responsive to commenter suggestions that the MSRB leverage EMMA and direct investors to the more comprehensive information there.

Finally, the MSRB proposed three exceptions to the mark-up disclosure requirement. Under the first exception, in response to concerns from commenters that compensation disclosure is not warranted for primary market transactions, the MSRB proposed to provide an

exclusion from a confirmation disclosure requirement for a customer transaction that is a "list offering price transaction," as defined in paragraph (d)(vii)(A) of Rule G-14 RTRS Procedures. A "list offering price transaction" is a primary market sale transaction executed on the first day of trading of a new issue by a sole underwriter, syndicate manager, syndicate member, selling group member, or distribution participant to a customer at the published list offering price for the security.

Under the second exception, in response to concerns from commenters that having the disclosure requirements triggered by trades made by separate trading departments or desks would undermine the legal and operational separation of those desks, the MSRB proposed to except from the mark-up disclosure requirement transactions between functionally separate trading desks. Under this exception, confirmation disclosure would not be required where, for example, the customer transaction was executed by a principal trading desk that is functionally separate from the retail-side desk if the functionally separate principal trading desk had no knowledge of the customer transaction.

Under the third exception, in response to concerns from commenters about having the disclosure requirements triggered by certain trades between affiliates, the MSRB proposed to require dealers to "look through" a transaction with an affiliated dealer and substitute the affiliate's trade with the third party from whom the dealer purchased or to whom the dealer sold the security to determine whether disclosure of the mark-up would be required. This "look through" would apply only for dealers that, on an exclusive basis, acquire municipal securities from, or sell municipal securities to, an affiliate that holds inventory in such securities and transacts with other market participants. Some commenters stated that acquiring a security through an affiliate was functionally similar to an inventory trade, and that this trade would be of

limited value,[76] particularly where the inter-affiliate trades are tantamount to a booking move across affiliates.[77]

As an ongoing alternative to the revised confirmation disclosure proposal, the MSRB also sought comment on a revised pricing reference proposal that was largely consistent with a revised confirmation disclosure proposal then under consideration by FINRA[78] and, more broadly, sought comment on the revised FINRA confirmation disclosure proposal itself. Under the revised FINRA confirmation disclosure proposal, if a firm sells to a customer as principal and on the same day buys the same security as principal from another party in one or more transaction(s) that equal or exceed the size of the customer transaction, the firm would have to disclose on the customer confirmation the price to the customer; the price to the firm of the same-day trade (the "reference price"); and the difference between those two prices. The revised FINRA confirmation disclosure proposal would permit firms to use alternative methodologies for calculating the reference price for more complex trade scenarios and would also permit firms to omit the reference price in the event of a material change in the price of the security between the time of the firm principal trade and the customer trade. Lastly, the revised FINRA confirmation disclosure proposal would require firms to provide a link to TRACE data on confirmations that are subject to the disclosure requirement.

The revised FINRA confirmation disclosure proposal also contained a number of exclusions that were generally consistent with those in the MSRB revised confirmation disclosure proposal. These included exclusions for: transactions that involve an institutional

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76 See SIFMA Letter I at 21.

77 See Morgan Stanley Letter I at 3.

78 See FINRA Regulatory Notice 15-36 (October 2015).

account; transactions that are part of a fixed price new issue and are sold at the fixed price offering price; firm principal trades that are executed on a trading desk functionally separate from the retail trading desk for purposes of calculating a reference price; and firm principal trades with affiliates for positions that were acquired by the affiliate on a previous trading day.

In response to the MSRB's revised confirmation disclosure proposal, some commenters reiterated that retail investors would benefit from some form of enhanced price disclosure. For example, the Consumer Federation of America stated that increased price disclosure would provide investors with the opportunity to make more informed investment decisions, and would foster increased price competition in the fixed income markets.[79] The SEC Investor Advocate stated that some kind of regulatory solution was necessary, as retail investors in fixed income securities "remain disadvantaged by the lack of information they receive in confirmation statements."[80] The PIABA stated that "abuse of undisclosed mark-ups and mark-downs is not a hypothetical problem," and that making additional pricing information available could result in customers being charged more favorable prices.[81]

A number of commenters supported the MSRB's proposal of disclosing the mark-up based on the prevailing market price instead of the reference price.[82] Both BDA and Schwab stated that the reference price proposal would be costly, difficult for dealers to implement and for retail customers to understand, and may not provide customers with meaningful information

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79 See CFA Letter II at 6.

80 See SEC Investor Advocate Letter II at 2.

81 See PIABA Letter II at 3.

82 See BDA Letter II at 6; Fidelity Letter II at 5; FSI Letter II at 5; LPL Letter II at 1; Schwab Letter II at 3; SEC Investor Advocate Letter II at 5.

about the costs associated with particular transactions.[83] Schwab noted that, under the reference price proposal, a customer may receive disclosure for the execution of one lot of a particular order, but not for another lot of the same order.[84] Schwab stated that the reference price proposal would also reflect market fluctuations, so that a customer may infer that the dealer lost money on a transaction with a customer, even if a mark-up was charged.[85] FSI noted that using prevailing market price would ensure that customers "receive the most reasonably accurate understanding of the cost of their trade."[86] In addition, FSI indicated that "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."[87] Fidelity stated that the proposed disclosure requirement should focus on the difference between the price the customer was charged for a fixed income security and the prevailing market price of the fixed income security.[88] Fidelity noted that a dealer's actual contemporaneous costs or proceeds are a reasonable proxy for the prevailing market price in some situations, but stated that there are many situations in which a dealer's costs or proceeds are not a reasonable proxy for the prevailing market price.[89] Fidelity proposed that the prevailing market price be defined as the dealer's best available price for the

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83 See BDA Letter II at 4-5; Schwab Letter II at 2.

84 See Schwab Letter II at 2.

85 See Schwab Letter II at 2.

86 See FSI Letter II at 5.

87 Id.

88 See Fidelity Letter II at 5, 7-8.

89 Id. at 7.

subject security under the best available market at the time of trade execution.[90] Fidelity proposed different methodologies that dealers could apply when determining the prevailing market price, including (1) looking at a trader's mark-to-market at the end of the day; (2) contemporaneous cost; (3) top of book; and (4) vendor solutions that offer real time valuations for certain securities.[91]

In supporting the MSRB's mark-up disclosure approach, the SEC Investor Advocate noted that although mark-up disclosure may lead to disclosure to an investor of information indicating a smaller cost under some circumstances than under the reference price proposal, it nonetheless provides relevant information about the actual compensation the investor is paying the dealer for the transaction, reflects market conditions and has the potential to provide a more accurate benchmark for calculating transaction costs.[92] LPL Financial noted that mark-up disclosure based on prevailing market price would be relevant to retail transactions in all kinds of fixed income securities that might be the subject of future disclosure requirements.[93]

Some commenters opposed limiting the disclosure requirement to circumstances where the dealer principal and customer trades occur closer in time to each other, such as two hours, as the MSRB previously had proposed. Coastal Securities, the Consumer Federation of America and the SEC Investor Advocate noted that a shorter timeframe would increase the possibility that

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90 Id.

91 Id. at 8.

92 See SEC Investor Advocate Letter II at 5.

93 See LPL Letter II at 4.

dealers would attempt to evade the disclosure requirement by holding onto positions.[94] Other commenters, including Morgan Stanley and SIFMA, supported the two-hour timeframe for disclosure.[95] These commenters stated that the two-hour window would capture the majority of the trades at issue, and would also be easier to implement.[96] Commenters stated that the concern that a shorter timeframe would facilitate gaming of the disclosure requirement was misplaced, as it was unlikely that dealers would change trading patterns and increase risk exposure merely to avoid disclosure.[97] One commenter also said that regulators have sufficient access to data that would show whether dealers were attempting to game a two-hour disclosure window.[98]

Commenters generally supported the change of the scope of the proposal from the "qualifying size" standard (transactions involving 100 bonds or fewer or $100,000 face amount or less) to all transactions with non-institutional accounts.[99] The Consumer Federation of America noted that the revised standard would help ensure that all retail transactions would receive disclosure, regardless of size.[100]

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94 See Coastal Securities Letter II at 1; CFA Letter II at 2; SEC Investor Advocate Letter II at 5.

95 See Bernardi Letter II at 1; CFA Institute Letter II at 1; Coastal Securities Letter II; Morgan Stanley Letter II at 3; RBC Letter II at 2; SIFMA Letter II at 7.

96 See CFA Institute Letter II at 5; Morgan Stanley Letter II at 3; SIFMA Letter II at 7.

97 See Morgan Stanley Letter II at 3; RW Smith Letter II at 2; SIFMA Letter II at 10.

98 See RW Smith Letter II at 2.

99 See CFA Letter II at 4; PIABA Letter II at 2; Schwab Letter II at 5; SIFMA Letter II at 15.

100 See CFA Letter II at 4.

Three commenters opposed the proposal to require dealers to disclose the time of the execution of the customer transaction.[101] FIF stated that this proposal would create additional expense for dealers, and information related to time of execution could not be adjusted in connection with any trade modifications, cancellations or corrections.[102] FIF also indicated that the execution time is not necessary because "the number of trades in each CUSIP listed on EMMA are so limited that investors will not have difficulty in ascertaining the prevailing market price at or around the time of their trade."[103] Schwab indicated that this would not be a necessary data point for investors if mark-ups are disclosed from the prevailing market price.[104]

Other commenters, however, supported including the time of execution of the customer trade.[105] Thomson Reuters stated that including the time of execution would allow retail investors to more easily identify relevant trade data on EMMA[106] and FSI stated that this would allow investors to understand the market for their security at the time of their trade.[107]

Several commenters supported adding a security-specific link to EMMA,[108] while other commenters, including FSI, SIFMA and Thomson Reuters, supported adding a general link to the EMMA website, noting that, in their view, a CUSIP-specific link could be inaccurate or

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101 See FIF Letter II at 5; Schwab Letter II at 6; SIFMA Letter II at 16.

102 See FIF Letter II at 5.

103 See FIF Letter II at 6.

104 See Schwab Letter II at 6.

105 See CFA Institute Letter II at 4; FSI Letter II at 7; Thomson Reuters Letter II at 2.

106 See Thomson Reuters Letter II at 2.

107 See FSI Letter II at 7.

108 See Bernardi Letter at 1; CFA Institute Letter II at 3-4; Schwab Letter II at 6; Fidelity Letter II at 8; RBC Letter II at 2.

misleading, and could be difficult for dealers to implement.[109] BDA stated that a general link to the main EMMA page would be operationally easier to achieve.[110]

Commenters supported the proposed exception for transactions involving separate trading desks,[111] although Schwab indicated that this exception should be subject to information barriers and rigorous oversight.[112] The Consumer Federation of America suggested the MSRB specifically require, in the rule text, that dealers have policies and procedures in place to ensure functional separation between trading desks,[113] and the SEC Investor Advocate suggested that the MSRB provide more "robust" guidance as to what constitutes a functional separation and applicable requirements.[114]

Some commenters supported the proposed requirement, in cases of transactions between affiliates, to "look through" to the affiliate's principal transaction for purposes of determining whether disclosure is required.[115] FIF and Thomson Reuters stated, however, that not all dealers are able to "look through" principal trades, given information barriers and the fact that dealers often conduct inter-dealer business on a completely separate platform than the retail business.[116]

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109 See FSI Institute Letter II at 6; SIFMA Letter II at 19; Thomson Reuters Letter II at 2.

110 See BDA Letter II at 3.

111 See CFA Letter II at 5; CFA Institute Letter II at 3; Schwab Letter II at 6; SIFMA Letter II at 14-15.

112 See Schwab Letter II at 6.

113 See CFA Letter II at 5.

114 See SEC Investor Advocate Letter II at 6.

115 See CFA Institute Letter II at 3; Fidelity Letter II at 11-12; PIABA Letter II at 2; Schwab Letter at 6; SIFMA Letter II at 18.

116 See FIF Letter II at 5; Thomson Reuters Letter II at 3.

Summary of Proposed Amendments to Rule G-30

The proposed amendments to Rule G-30 to provide prevailing market price guidance was published for comment in MSRB Notice 2016-07 (February 18, 2016). The MSRB received nine comment letters in response to the request for comment on the draft guidance.[117] A copy of MSRB Notice 2016-07 is attached as Exhibit 2g. A list of comment letters received in response to MSRB Notice 2016-07 is attached as Exhibit 2h, and copies of the comment letters received are attached as Exhibit 2i.

Summary of the Proposed Guidance and Comments Received

As proposed in MSRB Notice 2016-07, generally, the prevailing market price of a municipal security would be presumptively established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained. If this presumption is either inapplicable or successfully rebutted, the prevailing market price would be determined by referring in sequence to: (1) a hierarchy of pricing factors, including contemporaneous inter-dealer transaction prices, institutional transaction prices, and if an actively traded security, contemporaneous quotations; (2) prices or yields from contemporaneous inter-dealer or

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117 Letter from Michael Nicholas, Chief Executive Officer, Bond Dealers of America, dated March 31, 2016 ("BDA Letter III"); E-mails from G. Lettieri, Breena LLC, dated February 23, 2016 and March 10, 2016 ("Breena Letter III"); Letter from Brian Shaw, dated March 28, 2016 ("Shaw Letter III"); E-mail from Herbert Murez, dated March 28, 2016 ("Murez Letter III"); Letter from Marcus Schuler, Head of Regulatory Affairs, Markit, dated March 31, 2016 ("Markit Letter III"); Letter from Rick A. Fleming, Investor Advocate, Office of the Investor Advocate, U.S. Securities and Exchange Commission, dated March 31, 2016 ("SEC Investor Advocate Letter III"); Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, Municipal Securities Division, and Sean Davy, Managing Director, Capital Markets Division, Securities Industry and Financial Markets Association, dated March 31, 2016 ("SIFMA Letter III"); Letter from J. Ben Watkins III, Director, State of Florida, Division of Bond Finance, dated March 31, 2016 ("State of Florida Letter III"); Letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, Thomson Reuters, dated March 31, 2016 ("Thomson Reuters Letter III").

institutional transactions in similar securities and yields from validated contemporaneous quotations in similar securities; and (3) economic models.

Of the nine comments the MSRB received on the proposal, the majority suggested alternatives or made recommendations to modify substantially more than one key aspect of the proposal.[118] The SEC Investor Advocate described the draft guidance as generally useful, clear, and consistent with the FINRA guidance, but urged the MSRB to tighten a perceived "loophole" with respect to transactions between affiliates.[119]

Other commenters opposed the draft guidance on several grounds. Commenters questioned the appropriateness of a hierarchical approach in the municipal market.[120] These commenters generally expressed a belief that while a prescriptive hierarchical approach may be appropriate for more liquid non-municipal debt securities, it is not appropriate for the more unique and heterogeneous municipal market.

A number of commenters stated that additional factors not permitted to be considered under the draft guidance should be expressly permitted to be considered when determining the prevailing market price of a municipal security. These include: trade size;[121] spread to an index;[122] and side of the market.[123] Others still suggested modifying or providing additional

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118 See Shaw Letter III at 2; Markit Letter III at 1-5; SEC Investor Advocate III at 5-8; SIFMA Letter III at 3-14; Thomson Reuters Letter III at 2.

119 See SEC Investor Advocate Letter III at 8.

120 See BDA Letter III at 2; Markit Letter III at 2.

121 See SIFMA Letter III at 7; Thomson Reuters Letter III at 2; Markit Letter III at 4.

122 See Thomson Reuters Letter III at 2.

123 See SIFMA Letter III at 7.

guidance for certain factors that are required or permitted to be considered under the draft guidance such as isolated transactions;[124] economic models;[125] and similar securities.[126] One commenter requested additional guidance on the meaning of the term, "contemporaneous."[127]

One commenter suggested that SMMPs should be exempted from the fair pricing requirement under Rule G-30, reasoning that, if SMMPs are sophisticated enough to opt out of Rule G-18 best-execution protections, they should similarly be able to opt out of fair pricing protections.[128] Another commenter suggested that the draft guidance should be limited to apply only to non-institutional accounts, consistent with the scope of the mark-up disclosure proposal.[129]

Based on a concern that a disclosed mark-up could appear misleadingly small when calculated from a non-arms-length transaction with an affiliated dealer, the SEC Investor Advocate urged the MSRB to require dealers acquiring securities from, or selling securities to, an affiliated dealer to always "look through" a non-arms-length transaction with an affiliate in establishing prevailing market price.[130] The SEC Investor Advocate further suggested that the underlying concern could be addressed in a number of ways (or combination thereof), including potentially modifying the draft guidance, modifying the proposed mark-up disclosure

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124 See Thomson Reuters Letter III at 2; SIFMA Letter III at 9.

125 See Thomson Reuters Letter III at 2.

126 See Thomson Reuters Letter III at 2; SIFMA Letter III at 8.

127 See SIFMA Letter III at 6.

128 See BDA Letter III at 4.

129 See SIFMA Letter III at 9-10.

130 See SEC Investor Advocate Letter III at 5-8.

requirement or providing further explanation regarding non-arms-length inter-affiliate transactions in any filing of a proposed rule change.[131]

Commenters suggested that the MSRB should provide the market sufficient implementation time before any prevailing market price guidance is effective.[132] Two commenters specifically suggested that any final prevailing market price guidance and any final mark-up disclosure requirements should be adopted at the same time.[133] One commenter suggested a minimum three-year implementation period.[134]

A number of commenters suggested that the MSRB take an alternative approach to adopting prevailing market price guidance. One commenter suggested that the MSRB should permit dealers to rely on the use of third-party pricing vendors under certain conditions,[135] while another suggested the MSRB should calculate and disseminate a net weighted average price which should be used in place of the prevailing market price.[136]

One commenter stated that dealers may calculate different prevailing market prices from the same set of facts and that dealers should be permitted to rely on reasonably designed policies and procedures to determine, in an automated fashion, the prevailing market price of a security.[137] Others expressed concern about the burden on dealers in complying with the draft

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131 Id.

132 See SIFMA Letter III at 13; Thomson Reuters Letter III at 2-3.

133 See BDA Letter III at 2-3; SIFMA Letter III at 13.

134 See SIFMA Letter III at 13.

135 See Markit Letter III at 4.

136 See Shaw Letter III at 2.

137 See SIFMA Letter III at 3.

guidance, and questioned whether such burden would be outweighed by any benefits to the market.[138]

More generally, three commenters suggested that the MSRB should coordinate with FINRA to develop consistent guidance and standards with respect to determining the prevailing market price of a security, including, potentially, the making by FINRA of corresponding changes to the FINRA guidance.[139]

In response to the comments received on the draft guidance, the MSRB clarified in the text of the proposed guidance that the list of factors specifically set forth in the proposed guidance to be used in determining whether a municipal security is sufficiently similar to the subject security as to be a "similar" security under the proposed guidance is a non-exclusive list. The text of the proposed guidance also makes clear that the determination of whether such security is "similar" may be determined by all relevant factors.

With respect to isolated transactions, the proposed guidance now clarifies that the determination of whether a transaction is an "isolated transaction" as that term is used in the proposed guidance is not limited to a strictly temporal consideration, and that "off-market transactions" may be deemed isolated transactions under the proposed guidance.

The MSRB agrees with the SEC Investor Advocate's concern regarding the potential for misleading mark-up or mark-down calculations and disclosures when the mark-up or mark-down is determined by reference to a non-arms-length transaction with an affiliated dealer. The MSRB has addressed this concern, as discussed above, through a combination of provisions in the

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138 See BDA Letter III at 1; State of Florida Letter III at 1; SIFMA Letter III at 14.

139 See SIFMA Letter III at 5; Markit Letter III at 5; SEC Investor Advocate Letter III at 6.

proposed mark-up disclosure requirement and explanation in this filing of the MSRB's intended meaning of the proposed prevailing market price guidance.[140]

The MSRB is not, at this time, providing any additional guidance regarding the defined term, "contemporaneous," as that term is used in the proposed guidance. This term is used in the FINRA guidance and adoption of the same term and definition within the proposed guidance promotes consistency and harmonization across fixed income markets. However, as discussed above, the determination of prevailing market price, as a final matter for purposes of confirmation disclosure, may be made at the time of a dealer's generation of the disclosure.

As noted above, the MSRB recognizes that the determination of the prevailing market price of a particular security may not be identical across dealers, although the MSRB expects that even where dealers may reasonably arrive at different prevailing market prices for the same security, the difference between such prevailing market price determinations would typically be small. The MSRB would expect that dealers have reasonable policies and procedures in place to calculate the prevailing market price and that such policies and procedures are applied consistently across customers.

Also as noted above, the MSRB has been in close coordination with FINRA on the development of the MSRB's mark-up disclosure proposal and the proposed guidance. The MSRB believes that the MSRB proposals are generally harmonized with the FINRA confirmation disclosure proposal and the interpretation of FINRA guidance, as applicable and to the extent appropriate in light of the differences between the markets.

The MSRB believes that the cumulative effect of the MSRB's modifications and clarifications contained in the proposed guidance is to make the waterfall generally less

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140 See discussion supra, Non-Arms-Length Affiliate Transactions.

subjective and more easily susceptible to programming (e.g., specific guidance with respect to determining contemporaneous cost or proceeds, the ability to determine the prevailing market price at the time of the making of a disclosure and the ability to consider economic models earlier in the process to the extent there are no "similar" securities to be considered). At the same time, these modifications and clarifications provide dealers with a greater degree of flexibility with respect to certain elements of the waterfall (e.g., more flexibility in determining the similarity of securities). The MSRB believes that these changes make the hierarchical approach more appropriate for the municipal market.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period of up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-MSRB-

2016-12 on the subject line.

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File Number SR-MSRB-2016-12. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 am and 3:00 pm. Copies of the filing also will be available for inspection and copying at the principal office of the MSRB. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-MSRB-2016-12 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, pursuant to delegated authority.[141]

Secretary

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[141] 17 CFR 200.30-3(a)(12).

MSRB Municipal Securities Rulemaking Board

Regulatory Notice

2014-20

Publication Date
November 17, 2014

Stakeholders
Municipal Securities Dealers, Municipal Advisors, Investors, General Public

Notice Type
Request for Comment

Comment Deadline
January 20, 2015

Category
Uniform Practice

Affected Rules
Rule G-15

Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations

Overview

The Municipal Securities Rulemaking Board ("MSRB") is seeking comment on draft rule amendments to require a broker, dealer, or municipal securities dealer ("dealer") to disclose additional information on customer confirmations for transactions in municipal securities. Specifically, the MSRB is proposing that, for same-day, retail-size principal transactions, dealers 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. This potential disclosure, made in connection with the investor's transaction, may be significantly beneficial for purposes of the investor's understanding of the market for the traded security. The MSRB and the Financial Industry Regulatory Authority ("FINRA") have been engaged in ongoing dialogue in furtherance of a coordinated approach to potential rulemaking in this area. FINRA is also publishing a notice soliciting comment on a similar proposal that would apply to other areas of the fixed income market.[1] The MSRB is seeking comment as to all elements of its proposal, including the scope of pricing information that should be disclosed, the transactions for which such disclosures should be made, and the likely benefits and economic consequences of such a requirement for investors and dealers, including the likely costs and burdens. Specific comment is also sought as to alternatives that could similarly increase price transparency, particularly for retail customers.

Comments should be submitted no later than January 20, 2015, and may be submitted in electronic or paper form. Comments may be submitted electronically by clicking here. Comments submitted in paper form should

[1] *See* FINRA Regulatory Notice 14-52 (Nov. 2014) ("FINRA Proposal").

Receive emails about MSRB regulatory notices.

be sent to Ronald W. Smith, Corporate Secretary, Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314. All comments will be available for public inspection on the MSRB's website.[2]

Questions about this notice should be directed to Michael L. Post, Deputy General Counsel, or Saliha Olgun, Counsel, at 703-797-6600.

Background

The MSRB is charged by Congress to protect investors and foster a free and open municipal securities market.[3] Under this mandate, the MSRB has advanced many initiatives to create and enhance MSRB products and rules with the goal of improving transparency, efficiency and other structural aspects of the market.[4]

First effective in 1978 and most recently amended in 2014, the MSRB's fair-pricing standards are a cornerstone of the municipal securities market.[5] MSRB Rule G-30, on prices and commissions, applies to dealer principal and agency transactions in municipal securities. Generally, it provides that dealers acting in a principal capacity may only purchase municipal securities from or sell municipal securities to a customer at an aggregate price (including any markup or markdown, collectively "markup") that is fair and reasonable. Similarly, when acting in an agency capacity, dealers may only

[2] Comments are posted on the MSRB website without change. Personal identifying information such as name, address, telephone number, or email address will not be edited from submissions. Therefore, commenters should only submit information that they wish to make available publicly.

[3] Securities and Exchange Act of 1934 § 15B(b)(2)(C), 15 U.S.C. 78o-4(b)(2)(C).

[4] *See* MSRB Long-Range Plan for Market Transparency Products (Jan. 27, 2012). The MSRB has requested comment and is analyzing information from market participants on potential improvements to the timeliness, fairness and efficiency of price transparency in the municipal market. *See* Concept Release on Pre-Trade and Post-Trade Pricing Data Dissemination through a New Central Transparency Platform, MSRB Notice 2013-14 (Jul. 31, 2013); Request for Comment on More Contemporaneous Trade Price Information Through a New Central Transparency Platform, MSRB Notice 2013-02 (Jan. 17, 2013). *See also* U.S. Securities and Exchange Commission, Report on the Municipal Securities Market, at pp. 117, 141 (Jul. 31, 2012) ("SEC Report") (noting MSRB transparency initiatives).

[5] Effective July 7, 2014, Rule G-18, on execution of transactions, and Rule G-30, on prices and commissions, were consolidated into a single rule under amended Rule G-30. *See* MSRB to Consolidate Dealers' Fair-Pricing Obligations into MSRB Rule G-30, MSRB Notice 2014-11 (May 12, 2014).

purchase or sell municipal securities for a commission or service charge that is fair and reasonable. Further, Rule G-30 requires dealers to exercise diligence in establishing the market value of the securities and the reasonableness of their compensation. FINRA Rule 2121, on fair prices and commissions, sets forth an analogous, although not identical, standard applicable to equity securities and certain debt securities, including corporate bonds.

While Rule G-30 requires that prices with respect to municipal securities transactions with customers be fair and reasonable, it does not require the disclosure of dealer compensation and/or transaction costs that are often factored into customer prices. For many securities other than municipal securities, the disclosure of such information is required on a customer confirmation under Securities and Exchange Commission ("SEC") Rule 10b-10. For example, the rule generally requires broker-dealers, when acting in an agency capacity, to disclose the amount of any remuneration received from the customer in connection with the transaction.[6] Additionally, the provisions of Rule 10b-10 that require a broker-dealer to disclose the amount of its markup do not apply to municipal securities, or for that matter to any fixed income securities.

In the municipal market, MSRB Rule G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to transactions with customers, requires the dealer to disclose on the confirmation the price of a municipal securities transaction. With respect to agency transactions, the dealer must also disclose on the confirmation the amount of remuneration received from the customer in connection with the transaction. If the dealer is acting as principal, however, there is no requirement that the dealer disclose its markup on the confirmation. Similarly, in the corporate bond market, broker-dealers executing agency transactions must generally disclose the amount of remuneration,[7] but are not required to disclose the amount of any markup.

Since the 1970s, the SEC has undertaken efforts to improve price transparency and reduce transaction costs in the municipal securities and corporate bond markets, prompting several SEC rulemaking efforts. In 1976,

[6] *See* Rule 10b-10(a)(2)(i).

[7] *See id.* and accompanying text. FINRA Rule 2232 on customer confirmations requires, in relevant part, a broker-dealer to send to a customer a confirmation of the transaction in accordance with SEC Rule 10b-10.

the SEC proposed to require markup disclosure by non-market makers in riskless principal transactions involving both equity and debt securities. This was followed by a 1977 proposal to require markup disclosure by non-market makers in riskless principal transactions involving equity and debt securities, but not municipal securities. In 1978, the SEC proposed to require markup disclosure for riskless principal trades in municipal securities. More recently, in 1994, the SEC again proposed to require confirmation disclosure of markups for riskless principal transactions in municipal securities.

These markup disclosure proposals were met with significant resistance. Commenter concerns focused primarily on: the potential negative effects of such disclosure on competition and market liquidity; possible compliance difficulties, including concerns about identifying the intended "riskless" principal transactions; the potential for customer confusion; and whether there was a need for such disclosures.[8]

In 2012, the SEC issued the Report on the Municipal Securities Market in which it broadly examined the market, including regulatory structure, market structure and market practices.[9] A common theme in the report was concern about transparency and pricing for customers, particularly retail customers. The report noted that, while the compensation on a municipal securities agency transaction must be disclosed as a commission, the compensation or markup on a principal transaction is not required to be disclosed.[10] It also noted that retail customers typically have access to substantially less pricing information than other market participants.[11] Without such information, investors may find it difficult to evaluate the fairness of the pricing of their securities or the costs associated with their transactions.

To address these concerns, the SEC recommended, among other things, that the MSRB consider: requiring dealers to disclose to customers, on confirmations for riskless principal transactions, the amount of any markup; encouraging or requiring dealers to provide retail customers relevant pricing reference information with respect to a municipal securities transaction effected by the dealer for the customer; and requiring dealers to seek the

[8] *See e.g.* Securities Exchange Act Release No. 34962 (Nov. 10, 1994), 59 FR 59612, 59615 (Nov. 17, 1994) ("1994 Release").

[9] *See* SEC Report.

[10] SEC Report at 147.

[11] SEC Report at 147.

best-execution of customer orders. In 2014, the MSRB announced that it was developing a proposal regarding disclosure of information by dealers to their retail customers to help them independently assess the prices they are receiving from dealers and to better understand some of the factors associated with the costs of their transactions. The MSRB further stated that the proposal would broadly seek input on alternative regulatory approaches, including markup disclosure on confirmations for trades that could be considered riskless principal transactions.[12]

Significant advances in the fixed income markets have helped to improve price transparency since the SEC's previous rulemaking efforts. Indeed, the SEC deferred consideration of its 1994 markup disclosure proposal due, in large part, to the planned development of systems that would make publicly available pricing information for municipal securities transactions. The SEC noted that the industry's efforts to improve transparency would result in enhanced price transparency for a broader number of transactions in the debt markets than the 1994 rule proposal would have affected.[13]

Launched in 2009, the MSRB's Electronic Municipal Market Access ("EMMA®") website is the municipal market's official free source of data and information on municipal securities. Through the EMMA website, market participants may access official disclosure documents, trade prices and yields, market statistics and more about virtually all municipal securities. MSRB Rule G-14, on reports of sales or purchases, currently requires dealers to report all executed transactions in municipal securities to the MSRB's Real-time Transaction Reporting System ("RTRS") within fifteen minutes of the time of trade, with limited exceptions. The RTRS system has been operational since 2005.[14] Since the launch of RTRS and EMMA, the MSRB has continually sought to improve price transparency in the municipal market through

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[12] *See* MSRB Holds Quarterly Meeting, Press Release (May 6, 2014); MSRB Holds Quarterly Meeting, Press Release (Aug. 5, 2014); MSRB Holds Quarterly Meeting, Press Release (Nov. 3, 2014). In the May press release, the MSRB also announced that it would seek SEC approval to implement a best-execution standard for transactions in the municipal securities market. The MSRB sought such approval on August 20, 2014. *See* Securities Exchange Act Release No. 72956 (Sept. 2, 2014), 79 FR 53236 (Sept. 8, 2014), File No. SR-MSRB-2014-07 (Aug. 20, 2014).

[13] *See* 1994 Release at 59612.

[14] In 2009, the MSRB additionally established the Short-Term Obligation Rate Transparency ("SHORT") system to collect and disseminate current interest rates and related information for auction rate securities and variable rate demand obligations.

enhancements to these systems.[15] In 2014, for example, the MSRB launched a new Price Discovery Tool on EMMA that permits market participants to more easily find and compare trade prices of municipal securities with similar characteristics.

Advances have also been made in other areas of the fixed income markets. In 2002, FINRA launched the Trade Reporting and Compliance Engine ("TRACE®") to improve post-trade price transparency in the corporate bond market. TRACE is the over-the-counter real-time transaction reporting and dissemination service for transactions in eligible fixed income securities.[16] Similar to the reporting time applicable to the MSRB's RTRS, transactions in eligible fixed income securities must be reported to TRACE generally within fifteen minutes of the time of execution. This transaction information is immediately disseminated for all securities subject to dissemination.[17]

With the use of information disseminated through these platforms, investors can make a more informed evaluation of the price paid or received for their fixed income securities. But because there is currently no markup disclosure requirement for fixed income securities, including municipal securities, dealers do not generally report their markups and such information is not disseminated to the market through EMMA or TRACE. Investors may, however, use EMMA and TRACE to view recent trade prices in the same or similar securities in similar quantities to compare trade prices.

Additionally, by viewing this trade data, in some cases, an investor may determine dealer acquisition cost and the investor's transaction costs for the securities. For example, if the reported trade data on EMMA showed that only moments before an investor purchased a quantity of securities, a dealer purchase was made for the same quantity of the same securities, the

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[15] *See supra* n. 4 and accompanying text. On July 15, 2014, the MSRB published a report on municipal market trading patterns, associated pricing and the effect of price transparency on pricing. The report provides a baseline set of statistics about municipal bond trading to enable market stakeholders and the MSRB to make further advancements with respect to the fairness, efficiency and transparency of the municipal market.

[16] TRACE eligible securities generally include debt securities denominated in USD and issued by a US or foreign private issuer and with a maturity of greater than one year. Eligible securities include corporate debt, agency debentures, and asset and mortgage backed securities.

[17] The securities subject to dissemination by TRACE currently include publicly traded and 144A corporate debt securities, agency debentures, agency pass through mortgage backed securities traded TBA and in specified pool transactions and, as of April 2015, asset-back securities.

investor could reasonably infer that the prior trade involved his or her dealer. The investor could further infer that the differential between those trade prices accounted for the investor's transaction costs. The table below illustrates this example. While this differential is not necessarily the same as a markup,[18] it can provide the investor increased price transparency and significant insight into the market for the security. An analysis of this differential may also achieve many of the regulatory objectives of a markup disclosure requirement.

Table 1

Trade Date/Time	Settlement Date	Price (%)	Yield (%)	Trade Amount ($)	Trade Type
11/5/2014 3:30 PM	11/13/2014	100.975	3.882	25,000	Customer bought
11/5/2014 3:29 PM	11/13/2014	98.996	4.058	25,000	Inter-dealer trade

While these advances have generally helped to make pricing information more accessible to the market, such information still is generally directly beneficial only to those who actively seek it out. The disclosure of such information on a retail customer's confirmation would provide additional transparency even to those investors who do not actively seek out the information, including those who may not know of EMMA or may not have the time or wherewithal to conduct their own transaction research.

The MSRB, FINRA and the SEC are engaged in ongoing dialogue in furtherance of a coordinated approach to this topic.[19] If the MSRB and FINRA determine that rulemaking is warranted, the MSRB and FINRA plan to

[18] A markup is commonly considered to be the differential between the prevailing market price of a security at the time the dealer sells the security to the customer and the higher price paid by the customer to the dealer. Similarly, a markdown is commonly considered to be the differential between the prevailing market price of a security at the time the dealer purchases the security from the customer and the lower price paid to the customer by the dealer. *See* Municipal Securities Rulemaking Board, MSRB Glossary.

[19] In a June 20, 2014 speech, SEC Chair Mary Jo White announced support for additional disclosures to help investors better understand the costs of their fixed income transactions. *See Intermediation in the Modern Securities Markets: Putting Technology and Competition to Work for Investors,* Economic Club of New York, New York, NY, available at http://www.sec.gov/News/Speech/Detail/Speech/1370542122012. With input from SEC staff, the MSRB and FINRA have developed complementary proposals for their respective markets and will continue to pursue a coordinated approach to this issue.

institute coordinated requirements to the extent possible and appropriate in light of the differences in the municipal securities market and other areas of the fixed income markets. Among other things, this approach should assist in mitigating the potential compliance burden on dually registered dealers.

Request for Comment

A pricing reference information disclosure requirement could be a logical next step in the MSRB's efforts to improve price transparency in the municipal securities market, and could effectively complement any future best-execution rule.

The goal of the proposed disclosures is ultimately to better inform retail investors. With relevant pricing reference information, received in the context of their securities transactions, retail investors could gain valuable insight into the market for the securities they trade. They may also more easily evaluate their transaction costs and the fairness of the price they paid or received for the securities. Additionally, knowledge on the part of dealers that such pricing information will be provided to investors may help to ensure that prices and markups are appropriate in light of the market for the security.

Pricing Reference Information Disclosures

Under the draft amendments, a new provision would be added to Rule G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to transactions with customers. This provision would require a dealer to disclose on the customer confirmation its trade price for a defined "reference transaction" as well as the difference in price between the reference transaction and the customer trade. A reference transaction generally is one in which the dealer, as principal, purchases or sells the same security that is the subject of the confirmation on the same date as the customer trade. The disclosure requirement would be triggered only where the dealer is on the same side of the transaction as the customer (as purchaser or seller) and the size of such dealer transaction(s), in total, would equal or exceed the size of the customer transaction. Accordingly, for a customer sale of municipal securities to the dealer, the dealer would be required to disclose pricing information for same-day reference transactions in which the dealer sold the securities in a principal capacity. Similarly, for a customer purchase of municipal securities from the dealer, the dealer would be required to disclose pricing information for same-day reference transactions in which it purchased the securities in a principal capacity.

The proposal would require 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. Thus, for example, if a dealer purchases 50 bonds in XYZ securities at a price of 100 for $50,000 and, on the same day, sells 50 bonds in those same securities to a customer at a price of 102 for $51,000, the dealer would be required to disclose on the customer's confirmation both the price of the reference transaction (100), which is currently available to the customer on EMMA, as well as the differential between the price of each trade (2).[20]

Applying the example from Table 1 above, the dealer would be required to disclose the reference transaction price of 98.996, which again is currently available to the customer on EMMA, as well as the price differential of 1.979 (calculated by subtracting the reference transaction price of 98.996 from the customer transaction price of 100.975).

An alternative approach would be to require dealers to disclose the total dollar amount differential between the reference transaction and the customer transaction.[21] If such an approach were pursued, in the same example above, the dealer would be required to disclose a total dollar amount differential of $1,000 (2% of $50,000 par amount). This approach could be pursued either in lieu of or in addition to the disclosure of the price differential as currently contemplated in the proposal. The MSRB seeks comment as to the type of pricing information dealers should be required to disclose on the customer confirmation. Are any or all of the options discussed optimal for providing customers the information that would be the most helpful to them? Are there better alternatives or equally effective alternatives that would impose fewer costs or burdens on dealers?

Retail Customers

Because a goal of the proposed disclosures is to provide relevant and helpful pricing information to retail investors in particular, the proposal would require a dealer to make pricing reference information disclosures only where the transaction with the customer is a retail-size transaction. The proposal categorizes a transaction involving 100 bonds or fewer or bonds in a par amount of $100,000 or less as a retail-size transaction. However, this

[20] The price of a transaction is an expression of percentage of the principal amount of the securities. The price differential would reflect the difference in percentages of principal between the acquisition cost and transaction cost. Multiplying the price differential by the par amount transacted would provide the dollar amount difference between the acquisition cost and transaction cost. A price differential of 2 means 2% of the par amount (2% of $50,000 or .02 x $50,000).

[21] *See* n. 20.

approach may not necessarily capture every retail trade and may, in some instances, capture some small trades executed on behalf of an institutional customer. An alternative approach would be to require the disclosures to be made to customers that are not sophisticated municipal market professionals or SMMPs as defined in MSRB Rule D-15. The MSRB specifically requests comment as to whether these approaches or a different approach would best serve the goals of the proposal. The MSRB is interested in input, in particular, regarding whether dealers would prefer to make the proposed disclosures to all customers, rather than a subset of customers likely to be retail investors. Specifically, to the extent that the proposal would require dealers to reprogram their systems for generating confirmations to determine when the disclosures would be made, would disclosing pricing reference information to all customers mitigate the compliance burden for dealers?

Same-day Period

The proposal would require a reference transaction price to be disclosed on the customer confirmation when the reference transaction is executed on the same trade date as the customer transaction. A review of EMMA trade data suggests that a significant percentage of retail-size trades have an offsetting trade in exactly the same quantity or similarly sized quantities within a short time from the customer trade. The number of these trades increases when this time period is lengthened to capture trades executed on the same date.[22] The MSRB believes that the disclosure of pricing reference information for trades in the same security in which the dealer acted on the same side of the transaction as the customer can provide helpful pricing information to investors. However, the MSRB recognizes that as the time period between trades increases, the degree to which the price of the reference transaction will be helpful to the customer may decrease.

An alternative to the same-day standard would be to limit the universe of trades for which pricing information must be disclosed to those trades that occur within a shorter or longer time range from the customer trade (*e.g.,* within thirty minutes of the customer trade or within two days of the customer trade). However, a shorter time period would likely result in fewer pricing reference disclosures to customers and may incentivize some dealers to time the execution of a trade so as not to trigger the disclosure

[22] Trade data from EMMA shows that approximately 21.32% of retail-size trades conducted during the twelve-month period of June 2013 through June 2014 had an offsetting trade transacted by the same dealer in the same size as the customer trade and on the same trade date as the customer trade (excluding new issue trades, which for purposes of this analysis were deemed to be any trade within fifteen days of the offering sale date).

requirement. The MSRB seeks comment as to the appropriate time relation between trades for the purposes of the proposed pricing disclosures.

Reference Transaction Size

Under the proposal, pricing reference information must be disclosed for reference transaction(s) that, in total, equal or exceed the size of the customer transaction. Thus, a dealer would be required to disclose pricing information for a single trade that equals or exceeds the size of the customer trade. Additionally, a dealer would be required to disclose such information for a trade that, when combined with one or more other same-day reference transactions, equals or exceeds the size of the customer trade.

When multiple dealer trades equal or exceed the amount of the customer trade, many methodologies may be available to a dealer to determine which price to disclose on the customer confirmation. These may include: disclosing the trade that is closest in time proximity to the customer trade; disclosing the last principal trade that preceded the customer trade (a last in, first out (LIFO) methodology); or disclosing the weighted average price of multiple trades. The MSRB seeks comment as to the appropriate standard(s) to apply under the proposal, as well as the situations in which such standards should be used. The MSRB also requests comment as to the costs and burdens as well as programming issues surrounding the use of one or more of these or any alternate methodologies for determining the appropriate pricing information to disclose. The MSRB specifically seeks comment on the methodologies that should be applied in the municipal securities market in examples 7, 9 and 10 in the FINRA Proposal.

The proposal assumes that one or more transactions that, in total, equal or exceed the size of the customer transaction are sufficiently similar to the customer trade or may form the basis from which a dealer may fill a customer order on the same day, such that the disclosure of pricing information for these transactions may be beneficial to the customer. Notably, because the proposal would apply to customer trades for 100 bonds or fewer or bonds in a par amount of $100,000 or less, the disclosure requirement should not have a significant impact on the institutional market for municipal securities.

Alternate size parameters might be equally or better suited to provide customers with relevant pricing information. One alternative might be to limit the disclosure of pricing information to only trade sizes that are identical to the customer's trade size. However, such a standard would result in less pricing information disclosed to the customer and may incentivize some dealers to modify trade sizes. Another alternative would be to require the dealer to disclose pricing information for its transactions in the same

securities on the same trade date if the trade sizes are within a specified range that is either smaller or larger than the customer's transaction (*e.g.* 50% smaller and 100% larger). These approaches would likely result in the disclosure of pricing reference information to fewer customers, but may result in disclosures that are more pertinent to a customer when they are made. As discussed below, the MSRB invites comment as to the proper parameters for reference transaction sizes for which pricing information should be required to be disclosed on the customer confirmation.

Explanatory Notations

To help ensure that the proposed pricing reference disclosures are meaningful to customers, dealers may wish to provide explanations or descriptions, in plain language, to assist customers in understanding the disclosures. For example, such descriptions might explain that the disclosed pricing information is expressed as a percentage and might further provide brief explanation as to how the price differential was calculated. Such explanations may also be utilized to provide some context for customer interpretation and analysis of the prices, which may be particularly helpful in the event of intra-day market events or other circumstances that might at least partially explain price differentials. Explanations and descriptions, if not included on the confirmation, could be provided in materials accompanying the delivery of the confirmation. The MSRB specifically invites comment as to these aspects of the proposal.

Economic Analysis

The MSRB has historically given careful consideration to the costs and benefits of its new and amended rules. The MSRB's policy on the use of economic analysis in rulemaking states that prior to proceeding with a rulemaking, the Board should evaluate the need for the rule and determine whether the rule as drafted will, in its judgment, meet that need. During the same timeframe, the Board also should identify the data and other information it would need in order to make an informed judgment about the potential economic consequences of the rule, make a preliminary identification of both relevant baselines and reasonable alternatives to the proposed rule, and consider the potential benefits and costs of the draft rule and the main alternative regulatory approaches.

1. The need for the proposed rule and how the proposed rule will meet that need.

The need for the proposed rule arises from the MSRB's regulatory obligations under the Exchange Act to protect investors and foster a free and open market in municipal securities.[23] Ensuring that customer transactions are effected at a fair and reasonable price[24] and making meaningful and useful information about transactions publicly available are two important ways in which the MSRB meets this mandate.

This rule builds on previous MSRB initiatives and addresses an ongoing concern that because retail municipal securities investors have access to less pricing information than other market participants, have a more limited ability to identify the most relevant pricing information, and may encounter significant burdens associated with access and acquisition of relevant information, they may not be able to effectively evaluate the market for their securities or the transaction costs associated with their securities.[25]

Currently, retail customers may use EMMA to gain insight into the market for the securities they trade by viewing recent trade prices in the same or similar securities in similar quantities. However, using EMMA to conduct the relevant pricing analysis requires that customers actively seek out information and make inferences as to which transactions are most relevant. Conducting this type of pricing analysis places a burden on retail customers.

The proposal also addresses the lack of a consistent standard for disclosure of pricing information via customer confirmations for similar types of securities transactions. The SEC has addressed this issue for certain equity securities in Rule 10b-10 and FINRA is proposing similar disclosures for its members engaged in transactions of non-municipal security fixed income securities.

[23] Securities and Exchange Act of 1934 § 15B(b)(2)(C), 15 U.S.C. 78o-4(b)(2)(C).

[24] *See* MSRB Rule G-30, on prices and commissions.

[25] *See generally* SEC Report.

2. Relevant baselines against which the likely economic impact of elements of the proposed rule can be measured.

To evaluate the potential impact of the proposed rule, a baseline, or baselines, must be established as a point of reference. The analysis proceeds by comparing the expected state with the proposed rule in effect to the baseline state prior to the proposed rule taking effect. The economic impact of the proposed rule is measured as the difference between these two states.

Three existing MSRB rules serve as relevant baselines: Rules G-14, on reports of sales or purchases, G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to transactions with customers, and G-30, on prices and commissions. Proposed revisions to Rule G-18 that would establish a best-execution obligation on dealers may also be a relevant baseline.

Rule G-14 requires dealers to report all executed transactions in municipal securities to RTRS within fifteen minutes of the time of trade, with limited exceptions. This information is made public through EMMA. The proposal would require dealers to identify which of its transactions reported to RTRS will serve as a reference transaction, and to disclose both the price of a reference transaction and the difference in price between a reference transaction and the customer trade. The disclosures would only be required for transactions in which the dealer is a party on the same side of the transaction as the customer.

Rule G-15 requires, among other things, dealers to disclose on the confirmation the price of a municipal securities transaction. With respect to agency transactions, the dealer must also disclose on the confirmation the amount of remuneration received from the customer in connection with the transaction.

Rule G-30 provides that dealers acting in a principal capacity may only purchase municipal securities from, or sell municipal securities, to a customer at an aggregate price that is fair and reasonable and requires that dealers exercise diligence in establishing the market value of the securities and the reasonableness of their compensation.

3. Identifying and evaluating reasonable alternative regulatory approaches.

The MSRB recognizes that there are alternatives to the proposed approach that range from taking no action, providing additional information via EMMA,

requiring dealers to disclose information on the customer confirmation other than what is proposed above (including disclosure of markups on riskless principal transactions), requiring disclosure of pricing reference information under alternative parameters, or some combination thereof.

The MSRB could take no action. Under this alternative, retail customers would continue to use EMMA to acquire market information and evaluate the costs associated with their transactions. Retail customers would not be able to ascertain with certainty the specific price paid by its dealer and may, therefore, be relying on less useful information. To address this, the MSRB could develop an internal methodology for identifying a reference transaction and provide this information to the public. The MSRB seeks comments that would help to quantify the existing burdens of accessing market information via EMMA and the degree to which changes to what is currently provided to the public would mitigate or increase these burdens.

The MSRB could require dealers to disclose information other than the price of a reference transaction and the difference in price between a reference transaction and the customer trade. For example, the MSRB could require disclosure of only the price of a reference transaction and not require disclosure of the price differential or the MSRB could require disclosure of the total trade price differential between a reference transaction and the customer transaction in lieu of or in addition to the disclosure of the price differential as proposed.

The MSRB could also require the inclusion of other market information (*e.g.,* prices provided by external pricing services) on the confirmation. The MSRB seeks comments on whether any of these alternatives provide customers with more meaningful and useful information, whether that value of additional information can be quantified, and the degree to which any of these alternatives would be more or less costly to implement.

The MSRB could specify a shorter or longer period during which a reference transaction may take place. For example, an alternative to the same-day threshold could be to limit the disclosure requirement for those principal trades that occur within thirty minutes of the customer trade or extend the time period to beyond one day. The MSRB seeks comments that would support quantification of the relevance of transactions that occur more or less closely in time to the customer transaction and the degree to which a change in the threshold would increase or decrease costs associated with disclosure.

The MSRB could specify an alternative definition of the size that a dealer transaction must be to meet the definition of a reference transaction. For

example, the MSRB could specify that reference transactions are only those dealer transactions that are identical in size to the customer transaction or meet an alternative definition of "similar size" (*e.g.,* 50 percent smaller or 100 percent larger than the customer transaction). The MSRB seeks comments that would support the quantitative evaluation of the degree to which transactions need to be similarly sized to provide meaningful and useful market information and the degree to which a change in the size definition of a reference transaction would increase or decrease costs associated with disclosure.

The MSRB could specify the methodology by which a reference transaction price is determined when the size of a reference transaction is not identical to the size of the customer transaction. As noted above, the FINRA Proposal identifies methodologies for calculating a reference price under a range of scenarios. The MSRB seeks comment on the degree to which particular methodologies are more or less likely to result in a disclosed reference transaction price for municipal securities that is meaningful and useful and whether particular methodologies are more or less costly to implement.

Finally, the MSRB could reduce or increase the size and/or value of customer transactions for which pricing reference information disclosures would be required. Alternative thresholds would provide confirmation disclosures to customers beyond those that transact in retail sizes. These could include providing disclosures to all customers, or to all customers that are not sophisticated municipal market professionals. The MSRB seeks comment on whether the 100 bonds or fewer or bonds in the par amount of $100,000 or less is an appropriate threshold and the degree to which a change in the threshold would increase or decrease costs associated with disclosure.

Another possible approach would be to require disclosure of the same pricing information, but limited to "riskless principal" trades, which would be consistent with the amendments to Rule 10b-10 that were previously proposed by the SEC.

4. **Assessing the benefits and costs, both quantitative and qualitative, of proposal and the main alternative regulatory approaches.**

The MSRB policy on economic analysis in rulemaking addresses consideration of the likely costs and benefits of the rule with the draft amendments fully implemented, against the context of the economic baselines discussed above.

The MSRB is able to identify some data to help quantify the economic effects of the proposal. For example, trade data from EMMA provides some insight

into the portion of retail-size trades in municipal securities to which a potential disclosure requirement might apply. However, additional information will be necessary to fully assess the economic effect of the proposal.

Benefits

The proposal is intended to provide additional information to retail investors and reduce the burden on retail investors for obtaining relevant information for purposes of the investor's understanding of the market for the traded security. The MSRB expects that the proposal will result in important benefits for investors who are customers in retail-size transactions. The MSRB expects that the proposal will promote a free and open market.

While EMMA has generally helped to make pricing information available and more accessible to the market, such information is generally directly beneficial only to those who actively seek it out and requires investors to make inferences about transactions. By requiring dealers acting in a principal capacity to disclose additional information to customers on the customer confirmation, the proposed rule would provide additional useful information and reduce the burden currently placed upon retail investors to actively search the EMMA database.

Costs

Our analysis of the potential costs does not consider all of the costs associated with the proposal, but instead focuses on the incremental costs attributable to it that exceed the baseline state. The costs associated with the baseline state are, in effect, subtracted from the costs associated with the draft rule to isolate the costs attributable to the incremental requirements of the proposal.

The proposal would likely require firms to modify their operational systems to identify reference transactions and provide the required disclosure on customer confirmations. For many firms, the reprogramming of existing systems may be costly. The MSRB seeks comments on the anticipated costs of such changes.

The MSRB is also requesting comments on whether the proposal could have unintended impacts on market behavior including, but not limited to: firms holding fewer bonds in inventory, firms holding more bonds in inventory, or dealers reducing service in retail-size trades.

Finally, the MSRB recognizes that, in some cases, additional information may cause customer confusion. The MSRB seeks comment on how this proposal could best ensure that customers receive relevant and useful information.

Effect on Competition, Efficiency, and Capital Formation

One of the likely effects of the proposal is that competition between dealers will be enhanced. Retail customers will have information that will allow them to make more informed choices about which dealers to use for future transactions, incentivizing dealers to offer competitive prices in retail transactions.

It is possible that the costs associated with the requirements of the proposal relative to the baseline may lead some dealers to reduce services to retail investors. In some cases, the costs could lead smaller dealers to consolidate with larger dealers or to exit the market.

The MSRB seeks public comment on the following questions, as well as any other comments on this topic, to assist it in determining whether to proceed with the development of a proposed pricing reference disclosure requirement for dealers. The MSRB particularly welcomes statistical, empirical, and other data from commenters that may support their views and/or support or refute the views or assumptions or issues raised in this request for comment.

1. Would the proposed disclosures provide investors with greater transparency into the compensation of their brokers or the costs associated with the execution of their municipal securities trades? Would the proposed disclosures help ensure investors receive fair and reasonable prices? What are the other potential benefits of the proposal?
2. What costs would this proposal impose on firms, including the cost of reprogramming the systems that create customer confirmations? Would such costs be mitigated by the coordinated approach of the MSRB and FINRA to this topic?
3. For what time period should the dealer's trades be disclosed? Is the same trading day standard appropriate in light of the objectives, costs and benefits of the proposal?
4. For which transactions should pricing reference disclosures be made?
    - Is it appropriate to provide that a dealer is only obligated to disclose pricing reference information when the customer trade is likely to be a retail trade? If so, should retail be defined by reference to the trade size, as in the proposal, or by some other standard?
    - Should there be any exclusions for certain types of transactions, notwithstanding the fact that they are retail-size transactions? For example, should the proposed disclosures not be required for new issue trades?

5. What are the viable alternatives to the proposal?
    - In lieu of the proposed disclosure of pricing reference information, should the MSRB require dealers to disclose their "markups" on "riskless principal" transactions as in the SEC's recommendation? If so, how could "riskless principal" transactions be defined to minimize market participant concerns?
    - Would the disclosure of additional information on EMMA meet some or all of the objectives of this proposal? If so, what information should be disclosed?
    - Is there a more principles-based approach that would achieve the objectives of the proposal?
6. To what extent, if any, do dealers already provide or make available such information or similar information to customers in any format?
7. Are there any situations in which pricing reference information that would normally require disclosure under the proposal should not require such disclosure?
8. When a firm executes multiple municipal securities transactions as principal, what should be the appropriate methodology or methodologies to use in determining the reference transaction price and differential to be disclosed on the confirmation? Are any of the methodologies referenced in this notice (*e.g.,* closest in time proximity to the customer trade or last in, first out) appropriate? Are there other methodologies that may be more appropriate?
9. Would the required disclosures encourage dealers to take actions to avoid making the proposed disclosures? For example: selling from inventory; taking a portion of securities from certain trades into inventory to avoid meeting the "reference transaction" definition; or holding securities until the relevant time period requiring disclosure has lapsed? If so, what effect might such actions have on the market? Would the risks associated with holding such securities in inventory weigh significantly against such actions?
10. For dealers with multiple market participant identifiers (MPIDs) registered to the same legal entity, what are the operational issues and associated costs with the proposal?
11. What information should be required to be disclosed on the customer confirmation?
    - Should the price differential between the customer's trade price and a reference transaction be disclosed as a percentage of par as in the proposal, or on a total dollar amount basis (*i.e.,* a differential that calculates the total dollar amount differential based on the number of bonds purchased or sold by the customer)? Should both be required to be disclosed? Is

there a better alternative to requiring the disclosure of the price differential?

- Should a reference transaction for which a dealer must disclose pricing information be more limited or more expansive in trade size? For example, should the proposal be limited to require only the disclosure of information pertaining to trade sizes that are identical to, or within a specified range as compared to, the customer trade size? Are the sizes that would currently require disclosure under the proposal over-inclusive or under-inclusive? For example, under the proposal, pricing information for a single trade that would otherwise meet the reference transaction definition, but that is in a trade size slightly below the customer trade size, would not require disclosure (*e.g.,* the customer purchased 100 bonds from the dealer, and the dealer purchased 95 of those same bonds on the same trading day). How probative would these disclosures be for retail investors?
- Should pricing information also be disclosed for transactions in which the dealer transacted on the side opposite the customer's side of the transaction (*e.g.* transactions in which the dealer sold the same securities to both the customer and another party)?

12. Should pricing information for a reference transaction between affiliates be required to be disclosed, as is currently the case under the proposal, or should the required disclosures be limited to transactions with other dealers or customers?
13. Would a requirement to disclose pricing reference information on the confirmation cause any problematic delays in sending the confirmation to a customer?
14. Do the disclosures have the potential to mislead or confuse investors to a degree that cannot be remedied by education, explanations or descriptions supplementing the disclosures?

November 17, 2014

* * * * *

Text of Draft Amendments[26]

Rule G-15: Confirmation, Clearance, Settlement and Other Uniform Practice Requirements with Respect to Transactions with Customers

(a) *Customer Confirmations.*

(i) At or before the completion of a transaction in municipal securities with or for the account of a customer, each broker, dealer or municipal securities dealer shall give or send to the customer a written confirmation that complies with the requirements of this paragraph (i):

(A) – (E) No change.

(F) Pricing reference information. If the broker, dealer or municipal securities dealer is effecting a transaction as principal for 100 bonds or fewer or bonds in a par amount of $100,000 or less, the confirmation shall include:

(1) the price for any reference transaction (as defined in paragraph (a)(vi)(I) of this rule); and

(2) the difference in price between the reference transaction (as defined in paragraph (a)(vi)(I) of this rule) and the customer trade, expressed as a percentage of par.

(ii) – (v) No change.

(vi) Definitions. For purposes of this rule, the following terms shall have the following meanings:

(A) – (H) No change.

(I) The term "reference transaction" is a transaction in which the broker, dealer or municipal securities dealer transacts: (1) in a principal capacity; (2) with a third party to purchase or sell municipal securities; (3) in the same security as the customer; (4) on the same side of the transaction as the customer (as purchaser or seller); (5) on the same date as the customer transaction; and (6) in a single trade amount that equals or exceeds the size of the customer transaction or in a trade amount that, when combined with one or more other transactions that meet the requirements of clauses (1) through (5) of this paragraph, equals or exceeds the size of the customer transaction.

(vii) – (viii) No change.

[26] Underlining indicates new language.

(b) – (g) No change.

EXHIBIT 2b

ALPHABETICAL LIST OF COMMENT LETTERS ON MSRB NOTICE 2014-20 (NOVEMBER 17, 2014)

1. Bernardi Securities: Letter from Eric Bederman, Chief Operating and Compliance Officer, dated December 26, 2014

2. Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated January 20, 2015

3. Coastal Securities: Letter from Chris Melton, Executive Vice President, dated January 16, 2015

4. Consumer Federation of America: Letter from Micah Hauptman, Financial Services Counsel, dated January 20, 2015

5. DelphX LLC: Letter from Larry E. Fondren, President and CEO, dated January 7, 2015

6. Diamant Investment Corporation: Letter from Herbert Diamant, President, dated January 9, 2015

7. Fidelity Investments: Letter from Norman L. Ashkenas, Chief Compliance Officer, Fidelity Brokerage Services, LLC, and Richard J. O'Brien, Chief Compliance Officer, National Financial Services, LLC, dated January 20, 2015

8. Financial Information Forum: Letter from Darren Wasney, Program Manager, dated January 20, 2015

9. Financial Services Institute: Letter from David T. Bellaire, Executive Vice President and General Counsel, dated January 20, 2015

10. Financial Services Roundtable: Letter from Rich Foster, Vice President and Senior Counsel for Regulatory and Legal Affairs, dated January 20, 2015

11. Gerald Heilpern: E-mail dated December 9, 2014

12. Gerald Heilpern: E-mail dated December 18, 2014

13. Gerald Heilpern: E-mail dated January 8, 2015

14. Hilliard Lyons: Letter from Alexander I. Rorke, Senior Managing Director, Municipal Securities Group, dated January 20, 2015

15. Hutchinson Shockey Erley & Co.: Letter from Thomas E. Dannenberg, President and CEO, dated January 20, 2015

16. Interactive Data: Letter from Andrew Hausman, President, Pricing and Reference Data, dated January 20, 2015

17. John Smith: E-mail dated December 10, 2014

18. Jorge Rosso: E-mail dated November 24, 2014

19. Karin Tex: Letter dated January 12, 2015

20. McLiney and Company: Email from George J. McLiney, Jr. dated December 22, 2014

21. Morgan Stanley Smith Barney LLC: Letter from Vincent Lumia, Managing Director, dated January 20, 2015

22. Nathan Hale Capital, LLC: Letter from Peter G. Brandel, Senior Vice President, Municipal Bond Trading, and Kenneth T. Kerr, Senior Vice President, Municipal Bond Trading, dated January 20, 2015

23. Office of the Investor Advocate, U.S. Securities and Exchange Commission: Letter from Rick A. Fleming, Investor Advocate, dated January 20, 2015

24. Private Citizen: E-mail dated November 23, 2014

25. R. Seelaus & Co., Inc.: Letter from Richard Seelaus dated January 8, 2015

26. RW Smith & Associates, LLC: E-mail from Paige Pierce dated January 21, 2015

27. Securities Industry and Financial Markets Association: Letter from Sean Davy, Managing Director, Capital Markets Division, and David L. Cohen, Managing Director and Associate General Counsel, Municipal Securities Division, dated January 20, 2015

28. Standard & Poor's Securities Evaluations, Inc.: Letter from Gregory Carlin, Vice President, dated January 20, 2015

29. Thomson Reuters: Letter from Kyle C. Wootten, Deputy Director - Compliance and Regulatory, dated January 16, 2015

30. Wells Fargo Advisors, LLC: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated January 20, 2015

EXHIBIT 2c

BERNARDI SECURITIES INC.

MUNICIPAL BOND SPECIALISTS

Submitted Electronically

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

Re: Disclosure of Pricing Reference Information—Regulatory Notice 2014-20

December 26, 2014

Dear Mr. Smith:

Founded in 1984, Bernardi Securities, Inc. (BSI) is a municipal securities dealer providing underwriting, secondary market trading, brokerage, and portfolio management services to our institutional and retail customer base. We appreciate the opportunity to provide the Municipal Securities Rulemaking Board (MSRB) with comments related to the above referenced proposed rule.

BSI strongly supports appropriate transparency in our industry. We currently provide Pricing Reference Information upon request to customers wishing to know our markup or markdown for a trade executed in a principal capacity. Additionally, for customers selling bonds, we disclose the street bid for customer sales that BSI does not reoffer to customers. This is provided through supplemental reporting independent of the confirmation.

It is our understanding that EMMA was created to provide customers with prior trade information on bonds offered by broker-dealers. Dealer executions are disclosed in EMMA. These executions form the basis for the mark up/mark down. All customers should be aware of EMMA, as the EMMA website URL is disclosed on each customer confirmation. We believe that disclosing this information both in EMMA and on a customer confirmation is duplicative and possibly confusing.

BSI disagrees with the premise that all principal trades, where both sides of the market are executed in the same trading day, are "riskless." In fact, trades executed in this scenario can carry significant risk depending upon timing of the executions. Quite often BSI purchases positions without a customer order in hand. In this situation, the markup or markdown does not reflect "riskless" remuneration.

We believe dealers such as BSI provide valuable liquidity to the municipal marketplace. This liquidity is provided by placing our own capital at risk. Providing liquidity is especially important during periods of high volatility (i.e. fall 2008, fall 2010, spring 2013). During these time periods BSI provided liquidly to sellers of municipal bonds without holding a corresponding customer purchasing order. Some of these positions were reoffered during the same trading day, but none would be considered "riskless."

We recommend that the MSRB consider amending the proposed rules to require disclosure of Pricing Reference Information on trades where a customer order is obtained prior to the execution of trades for both sides of the market. This is a "near riskless" transaction.

We also wish to remind the MSRB that, while Pricing Reference Information may disclose the gross profit or loss on a firm trade, there are many other significant costs, both direct (technology, regulatory, clearance, financing) and indirect (personnel, occupancy, insurance) that a dealer has. Providing Pricing Reference Information without mention of these other costs provides an incomplete picture as to the remuneration that a dealer receives.

The rule proposal describes several disclosure formats and requests dealer input. For "riskless principal" trades described above, a number of disclosure formats are discussed. We believe that no specific or fixed format should be prescribed. We believe that the broker-dealer should have the option to disclose this information in the format that it determines is best (i.e. absolute dollar amount, execution price differential, percentage difference).

BSI believes that the final rules should be clear regarding customer trades that are executed versus multiple firm executions. It is possible that a dealer may purchase a position in a particular bond and at a later date purchase additional identical bonds. If a customer purchase is executed versus bonds acquired by the dealer on the customer's purchase date and date(s) prior to this trade date, it is not clear what methodology the dealer is required to use for potential disclosure.

Finally, BSI believes that significant modifications will need to be made to systems and procedures that process any final disclosure rules regarding Pricing Reference Information. These modifications will undoubtedly require a significant investment of time and resources. We hope that the MSRB will weigh the costs required with the liquidity benefits the marketplace receives from dealers such as BSI. We believe the marketplace needs dealers who stand ready to commit firm capital without a customer order in-hand. The marketplace may see the unintended consequences of fewer dealers standing ready to provide liquidity in turbulent markets.

BSI appreciates the opportunity to comment on this proposed rule and we look forward to providing additional feedback that will help the MSRB and the greater municipal bond marketplace.

Sincerely yours,

Eric Bederman
Chief Operating & Compliance Officer

BDA Bond Dealers of America

21 Dupont Circle, NW • Suite 750
Washington, DC 20036
202.204.7900
www.bdamerica.org

January 20, 2015

VIA ELECTRONIC MAIL

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

RE: **MSRB Regulatory Notice 2014-20: Request for Comment on Draft Rule to Provide Pricing Reference Information on Retail Customer Confirmations Fixed**

Dear Mr. Smith:

On behalf of the Bond Dealers of America ("BDA"), I am pleased to submit this letter in response to the Municipal Securities Rulemaking Board ("MSRB") Regulatory Notice 2014-20 (the "Notice"), requesting comment on a proposed rule to require the disclosure of pricing reference information on trade confirmations for certain 'retail-size' fixed-income securities transactions. BDA is the only DC based group representing the interests of 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 Notice.

BDA is concerned that regulators may move forward with this pricing reference disclosure rule without fully appreciating the complexity of the proposal from an operational and systems standpoint and without first engaging in a study that would inform regulators about the potential for this proposal to cause harm and confusion to investors, dealers, and the marketplace. Therefore, BDA urges regulators to engage in a feasibility study in order to begin to explore the inherent complexities of the proposed rule. Importantly, the feasibility study will create a valuable opportunity for regulators, dealers, and investors to explore enhancements to EMMA and TRACE that would serve as a cost-effective alternative to the disclosure described in the proposed rule.

BDA supports measures to increase pricing transparency for retail fixed-income investors. However, BDA is extremely concerned by the fact that the Notice lacks any discussion of how the proposed rule will actually function in the context of the systems currently used by dealers. While the description of the rationale that governs the disclosure methodology is clear what is not explored in the Notice is how difficult and

costly it will be for dealers to integrate this logic into their various trading and operational systems. Dealers will have to make alterations to operations, technology, clearing, and trading systems, in addition to third-party-vendor-provided services. The cost burdens associated with these changes will be significant for dealers, especially small-to-medium sized dealers. The Notice fails to fully contemplate these changes or their associated costs.

Without a full discovery of these complexities and the rule's possible negative investor impacts, preparing a comprehensive economic and operational analysis of the rule's impact is impossible. If, after completing a full discovery process, regulators chose to re-propose the pricing reference disclosure rule rather than working to create alternative solutions through enhancements to the functionality of EMMA and TRACE, regulators should allow for an additional comment period.

The proposed rule lacks a discussion of the various operational and technology obstacles for accurately capturing specific trade details for a specialized universe of trades, listing that information on a confirmation, and delivering that confirmation to the customer.

The Notice describes the logic that will be used to identify a universe of trades that will require a special confirmation disclosure. However, the rule does not discuss how FINRA and MSRB—based on their understanding of the trading, operational, and clearing systems currently used by dealers—believe it is feasible for dealers to seamlessly integrate the proposed rule's logic into their current systems in order to accomplish what is described in the Notice or what the associated cost burdens of doing so could be.

Listed below are some of the most significant and costly changes dealers will have to make in order to comply.

- Dealers will have to build new systems designed to capture the rule's required data elements in front and back-end systems.
- Dealers will be required to re-design front-end trading systems and back-office Service Bureau systems to operate with new matching logic. This system will need to be designed to run in real-time and will link dealer activity with customer trading activity. (This aspect of the rule will be especially problematic for firms, especially when applying the logic in real-time while executing significant buying and selling of securities at a variety of sizes and prices. For smaller firms, that may have to perform these types of tasks manually this could present a devastating technology and compliance burden. In some cases, smaller firms depend on vendors who may not even be willing to perform the tasks.)
- Dealers will have to design systems that work with batched trade files to identify—on a CUSIP-by-CUSIP basis—principal trades and associated retail trades. Then, at the end of the trading day, the system will have to apply the proper LIFO, closest in time, or average price methodology (based on FINRA's currently proposed rule) depending on how the principal position was accrued and the aggregate quantities of the retail-size trades. This is a system that does not

currently exist.

- Dealers may have to completely re-design their trade confirmations in order to comply with the rule's requirements. Trade confirmations have limited physical space to display the disclosures currently required under existing, applicable confirmation disclosure rules. Adding yet another required disclosure element will further challenge the finite confirm space availability, and at some point will yield diminishing returns to the investor as a disclosure piece due to the volume of information presented and the manner in which it must be presented to fit in the physical space.
- Trade files and reports will have to be enhanced in order to supervise compliance with the proposed rule change.
- Dealers will have to engage various third-party vendors to design solutions that will work in tandem with the various third-party-provided services and systems dealers currently use.

BDA believes that the proposed rule's universe of associated principal and retail trades is too broad and is not based on any empirical, market-based analysis.

BDA believes that, as currently designed, the rule would require disclosures that may not convey useful or complete information to retail investors. BDA believes that retail investors will ultimately ignore a disclosure that is confusing and applied without understandable consistency.

As Example 3 on page 4 of FINRA's Notice describes the reporting obligation for a firm that enters into a trade, in a principal capacity, to buy 500 bonds for 100 per bond. Then, on the same trading day, the dealer sells 30 of those bonds in a retail-sized transaction for 102.5 per bond. As the example states, the proposed rule would require a price differential disclosure of 2.50 on the retail trade confirmation.

This proposed disclosure requirement would inform the retail investor of the same-day price reference associated with the 30-bond purchase. But, this disclosure would not create a complete picture of the risks associated with this trade. The disclosure fails to provide the retail investor with a comprehensive disclosure because it does not adequately capture a holistic picture of the market risks and costs to the dealer for continuing to carry $469,250 of bonds in inventory for an undetermined period of time.

In this instance, if the retail customer scrutinized their dealer-provided trade confirm they would see the 2.50 ($750) pricing differential. However, the retail investor would be unaware that the dealer still held 94% of the original principal transaction in inventory. Carrying inventory carries significant risks. Profits are not guaranteed for the dealer. Dealers accept these risks in order to earn reasonable compensation in the service of their retail customers. BDA rejects the notion that principal trades entered into by dealers who chose to use their limited balance sheet capacity to service potential customer demand in the future are "riskless." These trades are not the functional equivalent of agency trades and should not be treated as such. BDA is concerned that this

disclosure could give investors the false impression that these trades are "riskless" thereby reducing investor confidence in the marketplace.

Furthermore, compensation, earned in compliance with the dealer's best execution responsibilities, helps to pay for the costs including but not limited to operations, sales, compliance, and trading personnel, credit analysts, providing retail investors with trade confirmations, monthly, quarterly, and annual statements, CUSIP fees, and the cost of trading technology services. These risks and costs are not disclosed to the retail investor, which creates an incomplete and misleading reference for the retail customer and the dealer, especially when the dealer holds inventory for any period of time.

As FINRA's rule states, "FINRA has observed that over 60 percent of retail-size trades had corresponding principal trades on the same trading day. In over 88 percent of these events, the principal and customer trades occurred within thirty minutes of each other." If this timescale captures the vast majority of the universe of trades that regulators seek an enhanced disclosure in relation to, BDA urges regulators to provide an empirical, market-based rationale for why designing the disclosure to apply in a full-day trading range is their preferred methodology.

BDA believes the proposed rule will provide a disclosure that may confuse investors and will not enhance investor understanding of the market generally.

The Overview to MSRB's rule states: *"This potential disclosure, made in connection with the investor's transaction, may be significantly beneficial for the purposes of the investor's understanding of the market for the traded security."*

The Background and Discussion of FINRA's rule states: *"FINRA has also observed that while many of these trades have apparent mark-ups within a close range, significant outliers exist, indicating customers in those trades paid considerably more than customers in other similar trades."*

The quotes above both allude to a comparative value analysis not between dealer cost basis and investor cost but, rather, between investor cost and the costs of other investors entering into "similar trades" in the market during a similar timeframe—"the market for the traded security."

Prices in the fixed income market are dynamic. A dealer may purchase bonds at 99 in a principal capacity prior to a market-moving event 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-size 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 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.

Furthermore, BDA notes, that if the disclosure were required to be based on LIFO, average price, or the closest in time standard depending on trade size and how the dealer accrues the principal position, three identical retail-size investor trades would receive three completely different pricing reference disclosures which adds an additional layer of potential confusion for investors.

BDA strongly recommends that FINRA and MSRB engage in a feasibility study to discover and evaluate the various practical challenges this highly complex rule presents.

Due to the fact that the proposed rule does not contain a discussion of what the proposed rule would entail from a technology and operational standpoint, BDA recommends FINRA and MSRB develop a feasibility study to explore what the optimal method for providing investors with greater market transparency could be. BDA is especially concerned with how this proposed rule will impact the competitive position of small-to-medium sized dealers. As stated above, BDA urges regulators to resubmit the pricing reference disclosure rule for comment after engaging in a comprehensive feasibility study.

Furthermore, as part of the study, BDA urges FINRA and MSRB to seek the input of the third-party vendors that dealers rely on to provide trading, technology, accounting, operations, and clearing services. While FINRA and MSRB are not required to perform outreach to these critical providers of services to dealers, the success of this rule will ultimately depend on the ability of these service providers to work with dealers and to configure their systems to allow efficient implementation and compliance to occur.

As BDA discussed above, FINRA and MSRB have not fully explored what this rule means for dealers on a practical day-to-day basis. The discovery process engendered by a feasibility study will allow for an assessment of what this rule would actually mean from an operational, technology, and trading systems standpoint. This will allow regulators to have greater insight into the systems on which they have proposed dealers make significant alterations. Additionally, BDA suggests FINRA and MSRB to actively seek the expertise of clearing firms and third party technology vendors to assess the feasibility of the rule and to discuss the operational and technological obstacles to expeditious dealer compliance.

This study should also provide an opportunity to explore ways to enhance TRACE and EMMA and explore why investors are not accessing these websites to evaluate the comparative value of their trades compared to similar-sized trades executed

in the market during similar timeframes. This study presents an opportunity for regulators to engage with investors and dealers in order to enhance EMMA and TRACE rather than requiring an additional disclosure prior to understanding why investors routinely ignore, or fail to seek, the market data that would naturally enhance their understanding of the market.

BDA suggests allowing dealers to employ whichever pricing disclosure methodology is the most efficient, least-cost method that fully complies with the dealer's responsibilities under the proposed rule.

If, after competing a comprehensive feasibility study, FINRA and MSRB present a detailed, market-based justification for why implementing a rule similar to the proposed rule is optimal for investors and the market, BDA recommends that FINRA allow dealers to choose the disclosure methodology of their choice. This will allow dealers to utilize the disclosure methodology that works most effectively with their existing systems. Dealers should be allowed to disclose the price differential in percentage spread, dollar terms, price differential, or yield terms. From a cost accounting standpoint, dealers should likewise be able to assess the functionality of their current systems and chose to make the reference disclosure using a weighted average, LIFO, FIFO, or closest in time proximity depending on what method works with their existing system capabilities.

The rule should contain some exclusions.

The rule should not apply to institutional investors. The rule operates to protect mainly retail investors through its application only to small trade sizes. The rule, though, should specifically exclude coverage to institutional investors so that dealers are able to categorically exclude those trades from coverage.

The rule should specifically exclude trades in connection with primary offerings. Distributions in connection with primary offerings benefit from offering memoranda that offer ample disclosure concerning the offering. Accordingly, trades by dealers in connection with distributions of securities in connection with primary offerings should be excluded from the coverage of the rule.

Thank you again for the opportunity to submit these comments.

Sincerely,

Michael Nicholas
Chief Executive Officer

January 16, 2015

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

Mr. Smith:

Thank you for the opportunity to comment on proposed amendments to Rule G-15 that would require mark-up disclosure for retail size transactions where the purchase and sale of a municipal security occur on the same day. Since the MSRB proposal is almost identical to that proposed by FINRA for transactions in agency and corporate debt securities, my comments here will be nearly identical to those made in response to the FINRA proposal.

Despite repeated denials and claims to the contrary, regulators truly believe that retail investors are paying too much for fixed income securities. Consequently, in an effort to provide investors information similar to that received on agency equity transactions, regulators have long sought a method of requiring disclosure related to what have heretofore been described as "riskless" principal transactions in fixed income securities. This desire usually manifested itself in proposals requiring markup disclosures for "riskless" principal transactions, which were always defined as transactions that clearly contained risk. The current proposal is an improvement in at least that regard as it does not attempt to define a lynchpin term as something it is not.

I would be tilting at windmills if I were to devote any more time to besmirching the idea of requiring dealers to disclose the price at which inventory was acquired. That ship has sailed. Nevertheless, there are still a number of issues with the current proposal that need to be addressed in order to ensure that the information provided to investors is accurate and educational, and does not represent a burden that falls unequally on certain broker-dealers.

First, the proposed amendments do not address issues raised by the sale of securities out of new issues at the public offering price. If a security is purchased at the public offering price on the day of issue, the amount of profit earned by the syndicate or selling group member should be irrelevant to the client acquiring the security. By rule, the public offering price is no respecter of the nature of a particular purchaser, unless the purchaser is a broker-dealer. Furthermore, calculating the exact amount of profit attributable to the sale is complicated by the nature of syndicate roles and the amount of the members' profits attributable to investment banking activity. Retail participation is particularly significant in municipal issuance. Yes, there are underwriters that will sell new municipal issues directly to retail clients at the public offering price. Requiring disclosure of mark-up on retail new issue transactions would have a chilling effect on retail sales of new issues that would not benefit investors and would stymie stated goals of many issuers that desire participation of their citizenry as investors in local bond offerings. The Board should consider including an exemption in the proposed amendments that would not require a broker-dealer to disclose "mark-up" on transactions in new municipal issues executed at the public offering price on the date of the issue's sale.

Also, in order to achieve the Board's stated intentions, the proposed amendments should address transactions that represent principal value of $100,000 or less in addition to those that involve 100 bonds or $100,000 par value or less. Transactions in zero coupon bonds with par value well in excess of $100,000 have principal amounts traded well below $100,000. A transaction involving $250,000 par

value of a zero coupon bond maturing in 30 years, priced to yield 6.00 percent would only involve about $42,000. I believe that the Board would consider this to be a retail size transaction. Far be it from me to advocate expansion of the applicability of an undesirable regulation; however, I believe that this was drafting oversight that the Board would want to correct. Additionally, if not corrected there would likely be a considerable increase in activity in zero coupon bonds in an effort to avoid the new requirements.

The proposal could result in an increase in prices paid by retail investors in general, since there will be more than a small chance that more than a few dealers will require that retail size sales to customers will not be permitted until the opening of business on the day following the purchase of the bonds. In instances where the dealer has acquired a block larger than "retail size", institutional clients will have access to inventory prior to the inventory being offered to retail clients. The result being that retail clients will only see inventory that did not represent value to institutional clients that were offered the security on the previous day. This might not be solely the result of larger dealers utilizing capital to avoid disclosure requirements. There will be some small dealers that may be forced to adopt this policy because they cannot afford the expense involved in programming the information necessary to accurately disclose the required information.

The request for comment inquires as to whether or not an alternate definition of reference price would be preferable to the definition proposed. Any definition of the reference price that would require a dealer to go outside the universe of its own trades would unnecessarily increase the cost associated with what will already be a burdensome task. Furthermore, the definition needs to be very clear in how price and mark-up are defined, so that an investor knows exactly what is represented by the amount of mark-up disclosed and can be confident that that amount is calculated in the same manner regardless of the client's counterparty. The idea of a *de minimis* exception holds promise, particularly if the *de minimis* amount is a flat dollar amount rather than a per bond figure.

Research has certainly revealed that the average retail customer is being charged fixed income mark-ups that regulators find unpalatable. It is difficult to determine which of a number of factors including investor apathy, which this proposal is designed to address, is centrally responsible. However, it is quite likely that firms that are charging mark-ups that regulators find generally unpalatable (although certainly not excessive) will not be deterred by the proposal. There are steps that could have been taken to improve investor education without requiring sellers to disclose the cost of their inventory on a confirmation.

I do not believe that the proposal will accomplish the goal that the Board has established. However, I am reminded of an old friend who would not eat mushrooms because he refused to eat anything the sun killed: it is difficult to oppose bringing sunlight to anything. Unfortunately, I do not believe that light of this nature will open many eyes, and will create unnecessary confusion and unintended consequences if some of the issues I have raised are not addressed.

Sincerely,

Chris Melton
Executive Vice President
Coastal Securities

Consumer Federation of America

January 20, 2015

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, Virginia 22314

Re: FINRA Regulatory Notice 14-52; MSRB Regulatory Notice 2014-20
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] to express our strong support for FINRA's and MSRB's proposed rules to require heightened confirmation disclosure of pricing information in fixed income securities transactions. By requiring firms to disclose on their customer confirmation the price to the customer, the price to the member of a transaction in the same security, and the differential between those two prices, the proposed rules will provide retail investors with critical cost information. This information will put them in a better position to assess whether they are paying fair prices and whether their dealers are fulfilling their best execution duties. As a result, this information will allow retail investors to make more informed investment decisions. These rules will also foster increased price competition in fixed income markets, which will ultimately lower investors' transaction costs.

The bond market plays a critical role in our nation's economy. The corporate bond market allows companies to finance their medium- and long-term capital investment and growth, and the municipal bond market allows cities, counties, and states to build schools, bridges, roads, sewer systems, hospitals, and other vital infrastructure. The bond market's significance is matched by its size. As of the fourth quarter of 2013, there was approximately $7.46 trillion

[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.

outstanding in corporate debt and $3.67 trillion outstanding in municipal debt, according to SIFMA.[2]

Retail investors provide corporations and municipalities with a significant amount of that capital by buying the bonds that corporations and municipalities offer. For example, as of March 2013, retail investors held directly or indirectly approximately 28 percent of the total outstanding principal value of the corporate bond market and approximately 75 percent of the total outstanding principal value of the municipal bond market.[3] Retail investors' participation in the municipal bond market is especially striking, as they held approximately 50 percent of outstanding municipal bonds directly.[4]

While retail investors are important participants in fixed income markets, they are disadvantaged in concrete ways when they transact in these markets. First, retail investors pay substantially more to trade in corporate and municipal bonds than they pay to trade in equities. Second, they pay substantially more to trade in corporate and municipal bond transactions than sophisticated traders. Theoretical and empirical evidence suggests that these price discrepancies are largely due to the fact that fixed income markets are opaque, and retail investors are not receiving information that would allow them to make better-informed decisions and pay lower transaction costs. In short, without essential price information, financial intermediaries are able to extract rents from their less well-informed retail customers by charging them higher transaction costs.

SEC Commissioner Michael Piwowar arguably has done more than anyone in recent years to highlight the ways in which retail investors have been harmed in fixed income markets. In 2007, Piwowar astutely observed: "Bond markets have been notoriously opaque….The lack of transparency in the bond markets has allowed market professionals – including sophisticated investors, brokers and dealers – to obtain vast sums of money from unsophisticated investors *and* taxpayers."[5]

Retail Investors' Trading Costs

Research on retail investors' trading costs for municipal and corporate bonds conducted by Piwowar, Lawrence Harris and Amy Edwards, has found that retail investors pay substantially more to trade municipal and corporate bonds than they pay to trade similar-size common stocks. In June 2006, Piwowar and Harris published a paper that examined municipal bond transactions through October 2000, and found, for example, that the average effective spread of a $20,000 municipal bond trade was almost 2 percent (1.98 percent) of the price. To put that cost in perspective, they pointed out that it is the equivalent of almost four months of the total annual return for a bond with a 6 percent yield to maturity. However, in today's low interest rate environment, that cost is even more pronounced; it is the equivalent of almost eight months of the total annual return for a bond with a 3 percent yield to maturity. In comparison to a

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[2] SIFMA Statistics, US Bond Market Issuance and Outstanding, http://bit.ly/1CL2CDz.
[3] *See* Luis Aguilar, **"**Keeping a Retail Investor Focus in Overseeing the Fixed Income Market**,"** Remarks at the Roundtable on Fixed Income Markets, Washington, D.C. April 16, 2013, http://1.usa.gov/1wnUjZr. (citing Federal Reserve Flow of Funds data).
[4] *Id.*
[5] Michael S. Piwowar, Corporate and Municipal Bonds, Securities Litigation and Consulting Group, Inc., 2007, http://bit.ly/1CwCN9V.

similar-sized equity trade of 500 shares of a $40 stock ($20,000), Piwowar and Harris found that this would be equivalent to an effective spread of 80 cents per share. Even the most illiquid stocks rarely have spreads that wide.[6]

A 2007 paper by Piwowar, Harris, and Edwards examined corporate bond transactions in 2003 and found that the average effective spread of a $20,000 corporate bond trade was 1.24 percent of the price, making it the equivalent of over two months of the total annual return for a bond with a 6 percent yield to maturity. Putting that cost in perspective relative to today's interest rates, it is equivalent to almost 5 months of the total annual return for a bond with a 3 percent yield to maturity. In comparison to a similar-sized equity trade, Piwowar, Harris, and Edwards found that this cost would be equivalent to an effective spread of 52 cents per share.[7]

In both studies, researchers found that trading costs decrease dramatically with trade size, meaning that retail investors generally pay substantially more than institutional investors to trade a bond. This is in stark contrast to equity markets, in which retail investors generally pay lower transaction costs than institutional investors to buy and sell stocks due to the lower price impact of trading smaller amounts. These results are consistent with the theory that dealers charge their less sophisticated, less well-informed customers much more than their more sophisticated, more well-informed customers.

Research by Erik Sirri on trading costs in the municipal securities market found a similar price impact based on trade size.[8] Sirri found that the average total price differential of moving municipal securities from one non-dealer investor to another dropped demonstrably as trade size increased. For example, Sirri found that trade sizes of up to $5,000 had an average total customer-to-customer differential of 246 bps (2.46 percent), whereas trade sizes of $25,000, which was the median trade size, had an average total customer-to-customer differential of 198 bps (1.98 percent). Larger trade sizes experienced even greater reductions in average total customer-to-customer differentials, with $100,000 trades resulting in a 28.7 percent lower average total customer-to-customer differential compared to $25,000 trades, and $1 million trades resulting in a 64.9 percent lower average total customer-to-customer differential compared to $100,000 trades.

In addition, Sirri found that 25 percent of all customer-to-customer transactions resulted in a total customer-to-customer differential of more than 288 bps (2.88 percent), and 10 percent resulted in a total customer-to-customer differential of more than 365 bps (3.65 percent). While these transaction chains did not factor in the number of dealers involved, the trade size, or the total length of time necessary to execute, these numbers suggest that it may not be out of the ordinary for many retail investors to pay extremely high transaction costs for their municipal bond transactions.

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[6] Lawrence Harris and Michael Piwowar, Secondary Trading Costs in the Municipal Bond Market, *Journal of Finance* 61, 1361-1397 (2006), http://bit.ly/1J3owpC.

[7] Amy Edwards, Lawrence Harris, and Michael Piwowar, "Corporate Bond Market Transaction Costs and Transparency," *Journal of Finance* 62, 1421-51 (2007), http://bit.ly/1Bb6y0y.

[8] Erik R Sirri, Report on Secondary Market Trading in the Municipal Securities Market, July 2014, http://bit.ly/1xuslwC.

Sirri also found that paired-trade differentials are noticeably higher when trades involve a customer, as opposed to another dealer. For example, the average customer-to-customer differential was 178 bps (1.78 percent), whereas the average differential of moving municipal securities from another dealer to a customer who bought municipal securities was 146 bps (1.46 percent), and the average differential of moving municipal securities from a customer who sold municipal securities to another dealer was 67 bps (0.67 percent). As expected, the average differential of moving securities from one dealer to another dealer was the lowest, at 50 bps (0.5 percent). This evidence supports the conclusion that dealers may be taking advantage of less-informed customers by charging them higher transaction costs, while charging each other minimal costs to trade securities.

Bond Market Opacity

For all the recent attention U.S. equity market structure has received recently, there is much greater price transparency in our equity markets than there is in our fixed income markets. For example, retail stock investors can see a continuous stream of publicly available information about the prices at which other market participants may be willing to buy or sell stocks. No publicly available pre-trade price information exists in the bond market.

In addition, firms are required to provide on their customer's confirmation the transaction costs the customer paid for all stock transactions, regardless of whether the firms executed the transaction in an agency or principal capacity. In bond transactions, firms are only required to provide on their customer's confirmation the customer's transaction costs if the firm executed the transaction in an agency capacity. Thus, if an intermediary arranges a trade for a customer on an agency basis, the intermediary must disclose on the customer's trade confirmation the transaction costs he or she paid, reflected as a commission. However, if an intermediary arranges a trade for a customer on a principal basis, the intermediary has no duty to disclose on the customer's trade confirmation the transaction costs he or she paid, reflected as a markup or markdown. This is essentially a regulatory loophole that allows bond intermediaries to treat functionally equivalent transactions differently for disclosure purposes, based on how they choose to characterize their transactions.

Given this regulatory inconsistency, which allows firms to choose whether their clients receive confirmation disclosure of the costs they are paying, it is hardly surprising that firms execute virtually all customer transactions in a principal capacity. This allows firms to effectively withhold information from their clients that their clients would find useful. As a result, firms are able to charge more than they otherwise would if they provided that cost information to their clients. Ironically, because customers do not see any transaction costs on their confirmations, they may mistakenly believe that they aren't paying any trading costs on their bond transactions. In reality, they are likely paying some of the highest trading costs in the market.

We recognize that there have been notable efforts to increase post-trade transparency in the bond market in recent years. In July 2002, Transaction Reporting and Compliance Engine (TRACE) began requiring bond dealers to report transaction data in U.S. corporate bonds in near real-time to what was then the National Association of Security Dealers (now FINRA), which made that transaction data available to the public for free. Similarly, in January 2005, the MSRB

began disseminating U.S. municipal bond pricing data to the public in real-time and for free. Market information was first posted on the Bond Market Association's investor education website, but was relocated in March 2008 to MSRB's Electronic Municipal Market Access (EMMA) website. There is evidence that overall transaction costs have decreased, both for corporate and municipal bond transactions, since transaction data has been made available.[9]

However, while overall bond trading costs have fallen as a result of increased price transparency, the evidence suggests that those benefits have not been noticeable for all investors. According to Commissioner Piwowar, for example, while institutional and sophisticated investors have seen their bond trading costs fall, retail investors' trading costs remain high. This is likely because institutional and sophisticated investors know that TRACE and EMMA exist, know how to access the information on those sites, and know how to interpret the transaction information that they find in order to gauge whether they are paying fair prices. Most retail investors, on the other hand, likely do not know the websites exist and, even if they did, are not in a position to use those websites with any reasonable degree of expertise. As a result, they likely are not able to realize the benefits that these websites can offer.

Unrealistic Expectations of Retail Investors

It's not realistic to expect retail investors to use TRACE and EMMA with any reasonable degree of expertise. In order to use TRACE and EMMA, one has to know each website exists and what specifically each website offers. It would likely confuse an investor that he or she has to go to different websites to see different types of recent bond transactions. Even assuming that a retail investor knows that those websites exist, one would have to know the precise information one is looking for; then, one would have to actually find that information. Finally, assuming that a retail investor knows what information to look for and finds it, one would need to be able to understand and make use of that information for one's benefit.

Assuming an investor Googles "FINRA TRACE" and clicks on the first option, the investor would somehow need to know—or find through trial and error—that out of the roughly seventeen options, he or she should click on "corporate bond data." Then the investor would have to click on www.finra.org/marketdata to find information on individual bonds, then enter relevant search terms, followed by agreeing to the user agreement, before coming to the relevant recent trade data. Once an investor finally navigated to the relevant data, he or she would have to make sense of it all. That would require an understanding of what all of the different columns mean (trade quantity, price, yield, coupon, maturity, time of execution, trade data), what the various rows mean in relation to one another, and how the rows and columns relate to the price the investor paid. Expecting an unsophisticated retail investor to navigate through this burdensome maze and then understand all of the data presented so that it is useful is too tall an order.

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[9] Bessembinder, Maxwell, and Venkataraman (2006), Edwards, Harris, and Piwowar (2007), and Goldstein, Hotchkiss, and Sirri (2007) conclude that the increased transparency associated with TRACE transaction reporting was associated with a decline in investors' average trading costs in corporate bonds. *See* Hendrik Bessembinder and William Maxwell, Markets, Transparency and the Corporate Bond Market, Journal of Economic Perspectives, Volume 22, Number 2, Spring 2008. Deng (2013) and Sirri (2014) conclude that the MSRB's Real Time Reporting System and EMMA were associated with a decline in investors' average trading costs in municipal bonds. *See* Gene Deng, Using Emma to Assess Municipal Bond Markups, Securities Litigation Group, 2013.

EMMA is significantly easier to use than TRACE, with video tutorials and visual depictions of recent trade information. However, even EMMA requires a certain amount of sophistication to make use of the data that is presented. Despite EMMA's more user-friendly design, it is unrealistic to expect an unsophisticated retail investor to understand all of the data that is presented, and then to make productive use of that data.

To understand why it is unrealistic to expect retail investors to use TRACE and EMMA productively, one must consider a typical retail investor's financial literacy. Extensive research has documented the disturbingly low levels of financial literacy among American investors. For example, the SEC's August 2012 study regarding financial literacy among investors found that retail investors "do not possess basic knowledge of interest rates, inflation or risk, all of which are essential to making well-informed investment decisions."[10] More specifically, they are essential to making well-informed bond transaction decisions. If retail investors do not possess these basis levels of knowledge, there is little likelihood they will be able to use TRACE and EMMA with any degree of skill or expertise or even that they will know of their existence.

It may be particularly unrealistic to expect fixed income retail investors to use TRACE and EMMA. Fixed income markets are generally tilted to the elderly, and the elderly have been shown to use the internet in lower percentages than the general population. For example, while roughly 80 percent of American adults use the internet, only 54 percent above the age of 65 use the internet.[11] Thus, the retail investors who would most benefit from certain pricing information may not have access to it.

Method of Delivery Matters

The only way to ensure that retail investors are receiving necessary cost information is to provide it directly to them. Research shows that the method that information is delivered matters. Information must be provided in an easily accessible manner, with as few barriers as possible, to have the highest impact and be most effective. Just because the information is available somewhere does not mean that it will be accessed. And, in fact, when CFA surveyed investors for a report on internet disclosures, investors were very skeptical of disclosures being made available but not being provided directly.[12]

Therefore, for bond price disclosures to be the most effective and to fulfill investor preferences, we strongly support directly providing retail investors on their confirmations the costs they are paying, the costs their dealers are paying, and the differentials between those two prices. Directly providing retail investors with this information rather than requiring them to search it out on their own will lower the barriers to access that retail investors currently confront, increasing the likelihood that they see and understand the transaction costs they are paying. With this information presented to them, they will be in a better position to assess whether they are

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[10] Study Regarding Financial Literacy Among Investors, As Required by Section 917 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Staff of the Office of Investor Education and Advocacy of the U.S. Securities and Exchange Commission, at vii-viii, August 2012, http://1.usa.gov/1fMABVZ.

[11] *See* Barbara Roper, Can the Internet Transform Disclosures for the Better?, Consumer Federation of America, January 2014, http://bit.ly/1CwEbJS.

[12] *Id.*

receiving a fair deal and whether their dealers are fulfilling their best execution duties. As a result, this information will allow retail investors to make more informed investment decisions.

With regard to the specific proposal, we believe FINRA and MSRB have done a sensible job in crafting a workable rule that is likely to benefit retail investors significantly. Regarding a few specific points:

- Defining "qualifying size" as a purchase or sale transaction of 100 bonds or less or bonds with a face value of $100,000 or less strikes us as a reasonable attempt to capture those trades that are retail in nature. According to Sirri's research in the municipal securities market, 14.7 percent of all trades were in par amounts over $100,000. Assuming those numbers are similar in the corporate context, it is likely that those trades are being undertaken by more sophisticated, wealthier investors, possibly even small institutions. However, it is still possible for unsophisticated retail investors to be trading more than what is considered a qualifying size under the rule. Moreover, it might be possible for dealers to game the system by conducting transactions that fall just outside the size limits of the rule. Therefore, we urge FINRA and MRSB to continue to monitor the costs of transactions that fall outside the definition. If it appears that certain investors are transacting in larger quantities and par amounts and are being taken advantage of by paying excessively high transaction costs, and FINRA and MSRB believe that they are paying those costs because the definition of qualifying size is too narrow or too rigid, FINRA and MSRB should seek to expand the definition of the rule.
- Limiting the proposal to same trading day appears to be a reasonable constraint on the application of the rule. FINRA has observed that over 60 percent of retail-size customer trades recently had corresponding principal trades on the same trading day. In over 88 percent of these trades, the principal and the customer trades occurred within thirty minutes of each other. Similarly, Sirri found that 57.7 percent of the total number of trade pairs occurred on the same day, and that almost 85 percent of same day pair trades occurred within thirty minutes of each other. If current trading patterns continue, these trades will be captured under the rule. However, it is possible that dealers' trading patterns might change to avoid having to comply with the rule. For example, they could hold positions overnight to avoid being subject to the disclosure requirements of the rule. While we don't think firms are likely to subject themselves to substantial increases in risk merely to avoid complying with the rule, we cannot rule out the possibility that they would view this as a reasonable risk. We therefore urge FINRA and MSRB to continue to monitor trading activities to ensure that the intent of the rule is being fulfilled to the maximum extent possible.
- 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 transactions. We agree that it will allow for a more mechanical approach by firms than a riskless principal approach, which may require firms to conduct a trade-by-trade analysis to determine whether a specific trade was "riskless." This approach will also allow for a

more mechanical regulatory review for compliance by FINRA and MSRB. Toward this end, we are pleased that vague and difficult to apply terms such as "essentially riskless" and "nearly contemporaneous" were not included in the rules' language.

- One clarification in the proposal is absolutely necessary regarding disclosure of the difference between the customer's price and the intermediary's price. We strongly urge FINRA and MSRB to require dealers to disclose the amount of the price differential BOTH as a percentage of the total amount AND as a total dollar amount based on the number of bonds purchased or sold. Ample research shows that retail investors have trouble comparing percentages and total amounts in costs, and that total dollar amounts are far more compelling to investors than percentages.[13] Furthermore, as question 5 in FINRA's proposal demonstrates, even in the simplest of transactions, several steps would be required for an investor to compute the total dollar amount differential. The likelihood of human error is extremely high. And, if retail investors do in fact make computational errors, the utility of this entire proposal will be seriously diluted. Therefore, it is imperative that this information be provided to retail investors in the clearest way possible.

Countering Industry's Arguments

We expect extensive industry opposition to this proposal, given that dealers have a vested interest in maintaining a certain level of opacity in this market so they can continue to extract rents from less-informed customers. This proposal is likely to threaten dealers because fostering increased price awareness and competition will ultimately lower investors' transaction costs, thereby lowering dealers' profits. We would like to address several industry arguments we have already seen:

- "Investors may see the prices and price differentials they are paying, but not understand them in the context in which dealers operate. Those prices don't reflect all the work dealers undertake to arrange customer transactions." That may be true. Dealers are entitled to reasonable compensation for their services, and if certain services, such as locating and arranging transactions in illiquid securities, are more labor intensive, dealers should be paid accordingly. However, that does not mean their customers should not be provided necessary cost information. What it means is dealers should be able to justify the costs that they charge their customers.
- "Investors will be annoyed and confused to see the costs they are paying." The implication of this argument is that investors are not aware of the costs they are paying now, and letting them in on the truth of what they're actually paying will make them upset. Perhaps they should be upset to learn the amount of transaction costs they've been paying. As a result of providing customers cost information directly, it may create an environment in which they are able to be more cost sensitive.
- "More price transparency will harm bond market liquidity." This is the same argument the Bond Market Association, the trade organization for bond dealers, made when

[13] *Id.*

TRACE became operational. While industry claimed that corporate bond trading would be more difficult, several studies found that trading costs decreased, and liquidity and trading activity increased. There is no reason that providing much of the same information through a more effective transmission channel will have any deleterious effect on liquidity.

Conclusion

While we do not believe that disclosure alone can address the many issues that affect retail investors, disclosure is an essential investor protection tool that, if done properly, can increase the likelihood that investors make more informed choices. Even minor improvements to the content and delivery of the disclosures that retail investors receive can influence investors' understanding of information and the choices they make as a result.

Retail investors in fixed income markets currently are paying extremely high transaction costs, and evidence suggests that they are paying those costs because they are not being provided essential cost information. These proposals will put retail investors in a better position to understand the costs they are paying and to assess whether those costs are reasonable. The information that is provided will also foster increased price competition in fixed income markets, which experience suggests will ultimately lower investors' transaction costs. We therefore strongly support FINRA's and MSRB's proposals to enhance fixed income market transparency for retail investors.

Respectfully submitted,

Micah Hauptman
Financial Services Counsel

Via PDF filed at: http://www.msrb.org/CommentForm.aspx

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

January 7, 2015

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"

Dear Mr. Smith:

The members and management of DelphX LLC [1] ("DelphX") appreciate this opportunity to respond to the request for comment issued by the Municipal Securities Rulemaking Board ("MSRB") in Regulatory Notice 2014-20 (November 17, 2014) ("Regulatory Notice"). We are pleased to submit the following comments regarding MSRB's important and timely proposal to increase transparency relating to transactions involving municipal securities ("Proposal"). Specifically, the Proposal would require that a broker, dealer, or municipal securities dealer (collectively, "dealer") for same-day, retail-size principal transactions, "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."

As reflected in many recent commentaries, pre-trade pricing and transaction costs in the vast fixed income market continue to be opaque.[2] This lack of transparency materially limits the ability of

[1] DelphX is an unbiased pricing-service provider dedicated to promoting efficiency, liquidity and broad pre-trade price transparency for corporate bonds and other fixed income securities by delivering validated continuous forecasts of the price at which each such security would currently trade. The undersigned, Larry Fondren, is the founder and CEO of DelphX. For more information about Larry Fondren, please visit http://en.wikipedia.org/wiki/Larry_Fondren. For more information about DelphX, please visit www.delphx.com.

[2] See, e.g., Securities and Exchange Commission ("SEC") Chair Mary Jo White, "Intermediation in the modern securities markets: putting technology and competition to work for investors" (June 20, 2014), 5-6; SEC Commissioner Daniel M. Gallagher, "Remarks to the Georgetown University Center for Financial Markets and Policy Conference on Financial Markets Quality" (September 16, 2014), at 5-6; SEC Commissioner Michael S. Piwowar, "Remarks at the 2014 Municipal Finance Conference presented by The Bond Buyer and Brandeis International Business School" (August 1, 2014), at 4-5; Director of the SEC Division of Trading and Markets, Stephen Luparello, "Testimony on 'oversight of the SEC's Division of Trading and Markets'" (June 26, 2014), 6-7; Remarks of FINRA Chairman and CEO Richard G. Ketchum, FINRA Fixed Income Conference (March 9, 2010); Legislation: Mark R. Warner (D-VA) and Thomas A. Coburn (R-OK) sponsorship of "Bond Transparency Act of 2014," S. 2114, 113th Cong. § 3.

investors to discern the remuneration retained by their dealers in fixed income trades,[3] and investors' ability to determine if their dealers fulfilled their obligation to seek the "best execution" of such trades.

Based upon our experience and the insights received from an array of market participants, we believe there is a critical need for increased pre-trade price transparency in relation to transactions involving fixed income securities, particularly those issues that are traded infrequently. We, therefore, applaud MSRB's initiative to enhance municipal bond market transparency for investors.[4]

A. Scope. The comments contained herein are principally focused on MSRB's request regarding "alternatives that could similarly increase price transparency, particularly for retail customers" or otherwise achieve or serve to better facilitate the objectives of the Proposal.

B. Summary of Comments. As discussed below, we believe the Proposal could provide useful information to investors that would enable them to make more informed investment decisions and be better equipped to assess the quality of their trade executions by dealers. Moreover, in response to MSRB's request for comments regarding potential "viable alternatives to the proposal" and "more principles-based approach that would achieve the objectives of the proposal" [5] we believe that an alternative means of providing pricing reference information, namely, the recognition of "**Accredited-Benchmark**" prices that accurately forecast the current market price ("Market-Price") of a municipal security continuously throughout each trading day, would provide timely and relevant pre-trade pricing reference information to investors. That contemporaneous pricing information could be used by investors to assess the remuneration retained by dealers when effecting their trades, and to evaluate the performance of dealers in seeking "best execution" of those transactions. We also believe that this approach of employing transparently-validated Market-Price forecasts would provide a comprehensive and cost-efficient means of expanding the scope of the Proposal to include customer transactions for which there is no same-day or recent reference transaction involving the subject security.

C. The Proposal. MSRB states that its goal is to better inform investors, particularly retail investors, with relevant pricing reference information, to provide valuable insight into the market in the context of their securities transactions. Additionally, such pricing reference information may also enable investors to more easily evaluate their transaction costs and the fairness of the price they paid or received for securities they bought or sold.[6] Accordingly, MSRB is proposing an amendment to Rule G-15, with respect to transactions with customers, that would require a dealer to disclose on the customer confirmation its trade price for a defined "reference transaction" as

[3] Because fixed income securities transactions are commonly executed by dealers which act as a principal in the transaction, their remuneration is generally secured in the form of a markup or markdown from the "prevailing market price." The Proposal is intended to address the fact that, currently, the amount of that markup or markdown is not required to be disclosed on the confirmation for fixed income trades executed by a dealer as principal.

[4] As the Regulatory Notice notes, MSRB has coordinated with the Financial Industry Regulatory Authority ("FINRA") which issued a similar proposal relating to transactions in corporate bonds and agency debt securities: FINRA Regulatory Notice 14-52, "Pricing Disclosure in the Fixed Income Markets " (November, 2014).

[5] See, e.g., Regulatory Notice, Request for Comments, No.5.

[6] Regulatory Notice, at 8.

well as the difference in that price and the customer trade price. A reference transaction is defined in the Notice as "generally one in which the dealer, as principal, purchases or sells the same security that is the subject of the confirmation on the same date as the customer trade."

Specifically, "The proposal would require 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. Thus, for example, if a dealer purchases 50 bonds in XYZ securities at a price of 100 for $50,000 and, on the same day, sells 50 bonds in those same securities to a customer at a price of 102 for $51,000, the dealer would be required to disclose on the customer's confirmation both the price of the reference transaction (100), which is currently available to the customer on EMMA, as well as the differential between the price of each trade (2)." [7]

While this additional disclosure could enable investors to "gain valuable insight into the market for the securities they trade,"[8] it has a variety of limitations. Because many of these considerations are recognized and discussed in the Regulatory Notice, we touch upon them only briefly in our comments below.

D. Response to Selected Request-Questions.

We refer to specific requests for comment as numbered in the Regulatory Notice.

Question 1. Would the proposed disclosures provide investors with greater transparency into the compensation of their brokers or the costs associated with the execution of their municipal securities trades?

Response: Economic studies have shown that investors benefit from increased price transparency through material reductions in their transaction costs.[9] Currently, dealers are not required to disclose their markups or markdowns to investors on fixed income trade confirmations when the dealer acts as a principal in the transaction.[10] Therefore, we believe additional relevant and meaningful reference information about current Market-Prices would assist investors in understanding the remuneration retained by their dealers, and help investors evaluate the services they receive. Providing pricing reference information relating to similar same-day trades, as the Proposal contemplates, could assist investors in assessing the quality of a dealer's transaction services. However we believe that same-day prices are less informative than relevant prices that are contemporaneous with the dealer's trade for

[7] Regulatory Notice, at 8-9.
[8] Regulatory Notice, at 8.
[9] *See* Hendrik Bessembinder and William Maxwell, "Transparency and the corporate bond market," J. Econ. Perspectives, v.22, no.2 (Spring 2008), 217, 227 ("Overall, the statistical and anecdotal evidence indicates that the introduction of post-trade transparency in the corporate bond markets has significantly reduced the costs that investors pay to dealer firms for executing their trades in corporate bonds."); Amy K. Edwards, Lawrence E. Harris, and Michael S. Piwowar, "Corporate bond market transaction costs and transparency," J. Fin., v.LXII, no.3 (June 2007), at 2. "If transactions costs are a deterrent to retail interest, we would expect retail interest to increase with the lower transaction costs associated with transparency." Id. at 31.
[10] Regulatory Notice, at 3 (discussing SEC Rule 10b-10).

the investor (i.e., pre-trade pricing) that the alternative Market-Price reference information described in Section E below would provide.

Question 4. For which transactions should pricing reference disclosures be made?

Response: Useful and meaningful price reference disclosure should be made available, where feasible, for all forms and sizes of transactions, rather than be limited to retail-sized or "riskless principal" trades.[11] Without meaningful pre-trade price reference disclosure, institutional investors can be as uncertain as individual investors as to the current Market-Price of municipal securities they are considering buying or selling.[12] While it is possible that increased price-transparency may diminish the levels of traditional dealer-sourced liquidity, increasing the ability of investors of all sizes to more confidently assess the current pricing levels of securities will potentially increase investor-sourced liquidity and the ability of dealers to more-readily facilitate "matching" or "pairing" of contra-trades among investors – further promoting increased liquidity.

Question 5. What are the viable alternatives to the proposal?

Response: We believe that, by creating an environment in which independent pricing-service providers are incentivized to develop and continuously publish precise forecasts of the current Market-Price of outstanding municipal securities in real-time, investors would gain access to a transparent and demonstrably accurate pricing reference for assessing the current Market-Price of securities they are considering buying or selling. Such a transparent environment, as described more fully in Section E below, would also enable investors to independently assess the remuneration retained by their dealers, and more efficiently determine the quality of executions they receive from their dealers.

The SEC's 2012 "Report on the Municipal Securities Market" ("SEC Report") recommended that the MSRB "consider encouraging or requiring municipal bond dealers to provide retail customers relevant pricing reference information" in connection with their trades.[13] The SEC Report suggested that the information might include recent transactions in the same or comparable securities, and current market information, such as quotations.[14]

The Accredited-Benchmark utility described in Section E below would help investors realize many aspirations of the SEC Report, by providing accurate to-the-second forecasts of the current Market-Price of thousands of municipal issues, including those for which no contemporaneous transaction pricing is available. It also would benefit investors by fostering a transparent market facility through which independent pricing-service providers are incentivized to publish the most accurate Market-Price

[11] According to the Regulatory Notice, only approximately 21.32% of retail-sized trades during a recent one-year period had relevant same-day trades by the dealer that would require disclosure under the Proposal. Regulatory Notice at 10 n.22. That means that nearly 80% of retail trades would not benefit from the Proposal's pricing information.

[12] Accordingly, we do not believe that it would be beneficial to exclude "sophisticated municipal market professionals" from receiving reference price information, as suggested in the Regulatory Notice at 10.

[13] SEC Report at 147.

[14] Id.

forecasts possible, and to continually strive to improve the scope and cost-efficiency of their pre-trade pricing utilities.

The idea of providing investors with current Market-Price forecasts and other benchmark prices is not a new one. The need for investors to receive relevant information immediately prior to buying or selling a bond was recognized by the Corporate Debt Market Panel ("Panel") established by FINRA's predecessor.[15] The Panel stated that an important part of increasing investors' ability to "understand the detail of their investment choices, risks and return" is the "ability to link aspects of recent improvements in transparency with actual transactions so that individual investors can determine the quality of execution they receive from their brokers." [16] The recommended pre-trade information included "[w]here the customer can get information on recent transactions in this or similar bonds." [17] The Panel also observed that "it would be very helpful for investors to be able to compare the price and yield they receive for a bond against industry benchmarks." [18]

We believe it would be appropriate to allow dealers to establish their own methodology, consistent with the objectives of the Proposal, provided that methodology is developed employing an objective rationale acceptable to MSRB, is clearly described to investors, and is consistently applied in all transactions. For example, should a firm choose to display Accredited-Benchmark pricing in its confirmations, it would be required to implement written policies and procedures to: (a) identify the Accredited-Benchmark as defined by criteria in a MSRB rule; (b) use a consistent methodology to disclose the Accredited-Benchmark's Market-Price forecasts to customers; (c) periodically review the performance of the Accredited-Benchmark to verify that it continues to satisfy the accreditation criteria specified by MSRB and provides meaningful information to customers; and (d) retain all documentation and data required to demonstrate the foregoing. Dealers could thus optionally disclose on customer confirmations the price to the customer, the Accredited-Benchmark price of the subject security at the time of the trade, and the differential between those two prices.

Question 8. When a firm executes multiple municipal securities transactions as principal, what should be the appropriate methodology or methodologies to use in determining the reference transaction price and differential to be disclosed on the confirmation? Are there other methodologies that may be more appropriate?

Response: As noted above, we believe a firm should be allowed to use an Accredited-Benchmark as the determinant of Market-Price at the time of each trade, and to consistently include such reference pricing in its confirmations. Given the transparency, validation and documentation of every Accredited-Benchmark price, the firm would have ready access to all documentation required to justify its use of Accredited-Benchmark prices. Use of objectively-derived Accredited-Benchmark prices would thus avoid the subjective pricing difficulty described in this question.

[15] National Association of Securities Dealers, "Report of the Corporate Debt Market Panel", at 2, 9 (September 2004) ("Debt Market Panel Report").
[16] Debt Market Panel Report, at 9.
[17] Debt Market Panel Report, at 12.
[18] Debt Market Panel Report, at 3.

Question 11. What information should be required to be disclosed on the customer confirmation?

Response: While some firms currently provide markup (markdown) information to their customers, we believe investors would materially benefit from dealers using a consistent standard to include information regarding the current Market-Price forecasts of one or more Accredited-Benchmarks for the subject security. Accordingly, we believe that Rule G-15 should permit the disclosure of Accredited-Benchmark pricing as an acceptable alternative to the reference pricing disclosures discussed in the Proposal, particularly where same-day transaction pricing for the security is not available. To provide additional transparency, we believe firms should be required to provide customers with an explanation of all pricing information they use (including Accredited-Benchmark prices) on trade confirmations, customer statements, and/or the firm's website.

Question 13. Would a requirement to disclose pricing reference information on the confirmation cause any problematic delays in sending the confirmation to a customer?

Response: We believe that electronically-delivered real-time Accredited-Benchmark prices could be integrated readily into a dealer's system that generates confirmations. We also suspect that incorporating Accredited-Benchmark reference prices would be technologically simpler than retrieving and recording a dealer's same-day prices pursuant to the Proposal.

E. Enhancing Pre-trade Price Transparency Through "Accredited-Benchmarks".

DelphX agrees with MSRB that investors in fixed income securities are currently limited in their ability to understand and compare transaction costs. However, we believe "understanding" and "comparing" are separate, but related, challenges. The Proposal would help with the former, but have limited impact on addressing the latter - as investors' comparative-pricing information would be limited to only the prices of same-day transactions executed by their dealer.

Because the vast majority of outstanding municipal bond issues will likely not be traded on any given day, the transparency fostered by the Proposal will apply to only a small portion of the total universe of such securities. We believe MSRB's recognition of an additional form of pre-trade price transparency, which also encompasses the larger group of securities for which no readily-observable current transaction pricing is available, would expand the utility and benefit of the confirmation disclosure contemplated in the Proposal.

To provide that additional comparative-pricing information to investors, we propose that MSRB foster the development and ongoing refinement of historically-accurate, continuously-updating forecasts of the current Market-Prices for a broad array of municipal bond issues, including those for which no recent transaction information is available. Specifically, we encourage MSRB to:

1) Establish an environment in which independent pricing-service providers are encouraged to calculate, validate and publish in real-time continuously-updating forecasts of the Market-Price at which each of a broad universe of outstanding municipal securities would currently trade;

2) Prescribe a standard protocol for measuring the accuracy of such forecasts, and definitive qualification parameters, that all pricing-service providers could employ to uniformly

determine the accuracy with which their Market-Price forecast for a subject security predicted the actual price at which that security traded ("Trade-Price");

3) Specify the minimum acceptable level of historical accuracy that the Market-Price forecasts published by a pricing-service provider must continually meet to qualify as an "Accredited-Benchmark"; and

4) Amend Rule G-15 to provide guidance to dealers, that the price of an Accredited-Benchmark is an acceptable reference source of the current Market-Price of the subject security for disclosure on customer confirmations.[19]

By establishing a standard protocol for calculating the accuracy of security-specific, time-specific Market-Price forecasts published by independent pricing-service providers, MSRB could provide a compelling incentive to current and future pricing-service providers to publish demonstrably accurate Market-Price forecasts. Moreover, competitive pressures would likely also encourage those providers to continually strive to increase the accuracy of their forecasts and to deliver those forecasts on increasingly competitive terms.

It is anticipated that the cost of accessing Accredited-Benchmark pricing references would be based upon the number of subject securities, timing of updates (real-time or delayed), frequency of updates (end-of-day or intra-day) and other factors. It is also possible that an Accredited-Benchmark pricing service provider, like DelphX, would provide free public access to Accredited-Benchmark prices for limited-use, time-delayed queries.

EMMA-Enabled Validation. We believe MSRB's Electronic Municipal Market Access system ("EMMA") provides a valuable source of timely post-trade pricing information that could be employed to measure and validate the forecasting accuracy of continuous pre-trade Market-Price forecasts published by pricing-service providers. By comparing a given provider's Market-Price forecasts for a subject security current at the time of each transaction in that security, as reported to EMMA, the accuracy of that provider's pre-trade Market-Price forecasts can be definitively determined on a security-specific and aggregate basis for use in the benchmark-accreditation process.

Thus, each time a transaction involving a subject security is reported to EMMA, the degree to which the forecasted Market-Price published at the time the transaction was executed deviated from the transaction's Trade-Price can be definitively measured, recorded and transparently reported to validate the accuracy of the Market-Price forecasts.

Therefore, to provide greater price transparency and facilitate more definitive compliance, we recommend that, in addition to the Proposal's same-day transaction price, dealers alternatively be permitted to disclose as a pricing reference on confirmations the current Market-Price forecast of an Accredited-Benchmark for the subject security at the time of the transaction with or for the investor.

[19] As we discuss below, the Accredited-Benchmark pricing references used in customer confirmations would also be useful for best execution and other price-related compliance purposes.

Investors and all other market participants and regulators would thus gain an informed and transparent basis upon which to assess the current pre-trade pricing levels of most outstanding fixed income issues.

Minimum Accuracy Standard.

It is suggested that to qualify as an Accredited-Benchmark, MSRB would require a municipal securities pricing service to:

1) Publish prices for municipal securities and update them continually, or at least as frequently as MSRB specifies, throughout each trading day;

2) Continually meet the acceptable Accuracy-Score levels specified by MSRB (e.g., at least 80.0% of published Market-Price forecasts must possess Accuracy Scores of 98.0% or higher); and

3) Continually report the benchmark's current Accuracy-Score, and transparently publish all information required to independently audit the accuracy of its current and prior Accuracy-Scores and its Market-Price forecasts current at each time the issue has been traded.

One approach for determining the accuracy of prior Market-Price forecasts of a municipal securities pricing service is to compare its Market-Price forecast at the time each trade of the security occurred in the past (using the "Execution" date/time of the trade reported to the EMMA system as the trade-time determinant), as DelphX currently does for calculating the Accuracy "Scores" of its MAV≡n® (Market-Adjusted Value per congruent nexus) Market-Pricing forecasts. Specifically, the current Accuracy-Score of the Market-Price forecasts generated by MAV≡n is determined by:

1) Calculating the Absolute Deviation (without regard for the direction of each deviation to avoid distortions due to "netting" of groups of deviations) of each Market-Price forecast from the actual Trade-Price at which the applicable transaction involving the security occurred;

2) Adding the Absolute Deviations of a specified number (e.g., 5) of the most recent transactions involving the subject security;

3) Adding the Trade-Prices of the transactions described above;

4) Dividing the Total Sum of the Absolute Deviations by the Total Sum of the Trade-Prices, to determine the Absolute Deviation-Quotient of the Market-Price forecasts in the analyzed transactions; and

5) Subtracting that Absolute Deviation-Quotient from 100% to determine the Accuracy- Quotient (Score) of the Market-Price forecasts of the subject benchmark.

For example, the Accuracy-Score of the continually-updating benchmark pricing of security A would be calculated as follows:

Calculating Accuracy-Score of Market-Price Forecasts for Security A

Transaction Sequence	Forecasted Market-Price	Actual Trade-Price	Absolute Deviation
Most Recent	112.045	112.392	0.347
2nd Most	109.255	109.641	0.386
3rd Most	110.340	110.950	0.610
4th Most	110.654	109.894	0.760
5th Most	110.873	111.055	0.182
		553.932	2.285

Absolute Deviation Quotient = 0.413% (2.285 ÷ 553.932 = 0.413%)

Accuracy-Score = 99.587% [20] (100% - 0.413% = 99.587%)

Employing Accredited-Benchmarks. We believe that permitting dealers to display an Accredited-Benchmark price on a trade confirmation would be an excellent example of "principles-based regulation" - rather than specifying a solitary method to provide pricing information to achieve its regulatory objective, the rule would allow firms to decide which acceptable method best fits their business model and customer base. Under this approach, a firm would be required to have written policies and procedures reasonably designed to identify an Accredited-Benchmark, provide contemporaneous Accredited-Benchmark pricing information to customers, and periodically review the performance of the Accredited-Benchmark to verify that it continues to satisfy the required criteria and provides meaningful information to its customers.

Accordingly, we recommend that MSRB amend Rule G-15 to permit dealers to disclose as a pricing reference on customer confirmations the Accredited-Benchmark price published for the subject security at the time of the transaction. By including Accredited-Benchmark prices as pricing references on customer confirmations, dealers could thus provide meaningful and useful information to investors.

Recognition by MSRB of Accredited-Benchmarks may also tend to increase the frequency with which currently-illiquid issues trade as, by informing investors of the likely current Market-Price of each of a broad range of securities they may have interest in buying or selling, those investors may be more inclined to trade attractively-priced securities with greater confidence and frequency.

Best Execution and Fair Prices. MSRB recognizes that retail investors "may not be able to effectively evaluate the market for their securities or the transaction costs associated with their securities." [21]

[20] More than 94.0% of MAV≡n forecasts published by DelphX currently possess Accuracy-Scores higher than 98.0%.

Similarly, SEC Commissioner Gallagher has stated: "Notwithstanding these recent initiatives in post-trade price transparency [22] retail investors continue to face significant market headwinds. They simply cannot be sure that they receive best execution and a fair price." [23] There is a growing consensus that "meaningful pre-trade pricing information" is key to addressing concerns about best execution and markup and markdown disclosure in the fixed income markets.[24]

As described below, there is a close association between the objectives of the Proposal and a dealer's obligations to seek "best execution" in executing customer orders, and to charge reasonable markups and markdowns on customer trades. Providing investors with Accredited-Benchmark Market-Pricing could enhance best execution and markup/markdown information and compliance.

Best execution. MSRB Rule G-18 will require a dealer to "use reasonable diligence to ascertain the best market for the subject security and buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions," and indicates that an essential element in assessing the "character of the market for the security" is price.[25] In the fixed income markets, where many if not most securities trade infrequently, determining whether a price offered in the market is reasonable can be difficult and time-consuming. However, a price generated by an Accredited-Benchmark could greatly assist the dealer in assessing whether an offered price is fair. That, in turn, can be incorporated into the other prevailing market factors in satisfying the dealer's best execution obligation. In addition, if the Accredited-Benchmark price were included on the customer's confirmation, the customer would have highly relevant, accurate and reliable information to use in evaluating the dealer's satisfaction of its best execution responsibilities.[26]

The use of Accredited-Benchmark prices could be used by a dealer to fulfill its obligations under Supplementary Material .06 of Rule G-18. For securities where there is limited pricing information, the dealer must have written policies and procedures to show how it fulfilled its best execution responsibilities. Among other things, the dealer should "analyze other data to which it reasonably has access." We believe that Accredited-Benchmark data that is available on reasonable terms would be highly relevant in this context.

Markup policy. MSRB Rule G-30, among other things, requires that a dealer trade as principal with a customer at "an aggregate price (including any mark-up or mark-down) that is fair and reasonable." Supplementary Material .01 discusses MSRB's policy on dealer compensation, and provides that the mark-up or mark-down is computed from "the inter-dealer market price prevailing at the time of the

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[21] Regulatory Notice 2014-20, at 13.
[22] Referring to FINRA's Transaction Reporting and Compliance Engine and the Municipal Securities Rulemaking Board's Electronic Municipal Market Access system.
[23] Remarks by Commissioner Gallagher, supra n.2, at 4.
[24] *See, e.g.*, Speech by Chair White, supra n.2, at 6; Remarks by Commissioner Piwowar, supra n.2 at 4-5; Remarks by Commissioner Gallagher, supra n.2, at 4.
[25] MSRB Rule G-18(a)(1). Rule G-18 becomes effective on December 7, 2015. See MSRB Regulatory Notice 2014-22 (December 2014).
[26] We note that MSRB Rule G-48 disapplies the best execution obligations of MSRB Rule G-18 to dealer transactions with "sophisticated municipal market professionals."

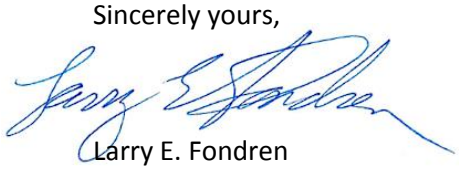
customer transaction." Fair pricing requires the dealer to "assess the market value" of the security, and may not pass on the dealer's cost if the dealer paid a price well above market value.

We believe that Market-Prices generated by Accredited-Benchmarks could substantially contribute to the dealer's assessment of market value at the time of its trade with or for a customer. Accredited-Benchmark prices could be used by a dealer in evaluating one or more dealer prices, or in determining the prevailing market price for a sale out of the dealer's inventory. If disclosed on the confirmation, the customer would have useful and meaningful information to assess the price obtained by the dealer and the remuneration retained by the dealer on the trade.

As stated above, we believe that all customers, retail and institutional, would benefit from the timely and historically-accurate Market-Price information provided by Accredited-Benchmarks.[27]

Conclusion. DelphX applauds MSRB for its initiative and is grateful for the opportunity to present an ancillary means of increasing pre-trade price transparency and enhancing achievement of the proposal's objective. We would be pleased to meet with MSRB Staff to provide additional information or answer questions regarding the Accredited-Benchmark utility. Please contact me at (610) 640-7546 (lef@delphx.com).

Sincerely yours,



Larry E. Fondren
President and CEO

cc: Marcia E. Asquith, Office of the Corporate Secretary, Financial Industry Regulatory Authority
Larry E. Bergmann, Murphy & McGonigle PC

[27] *Cf.* Hendrik Bessembinder, William Maxwell, and Kumar Venkataraman, "Market transparency, liquidity externalities, and institutional trading costs in corporate bonds," Initial Draft: November 2004, Current Draft: October 2005, J. Fin. Econ., forthcoming, at Abstract, 2, 35-36 (study of the "effect of transaction reporting on trade execution costs … using a sample of institutional trades in corporate bonds, before and after the initiation of public transaction reporting through the TRACE system. … These results reinforce that market design [i.e., decisions as to whether to make the market transparent to the public] can have first-order effects [a reduction of approximately 50% in trade execution costs for bonds eligible for TRACE reporting], even for sophisticated institutional customers."]

DIAMANT
INVESTMENT CORPORATION

Comprehensive Portfolio Management

January 9, 2015

Ronald W. Smith
Corporate Secretary
MSRB
1900 Duke Street, Ste 600
Alexandria, VA 22314

RE: MSRB Notice 2014-20

Dear Mr. Smith,

Diamant Investment Corporation (Diamant) is making the below constructive comments regarding the above proposed ruling detailed in the MSRB Notice 2014-20 (Proposal). The reason for making these comments is that is after reading the text of this proposed amendment, it became clear the MSRB, a regulatory authority charged with creating rules for the municipal bond industry, has little if any understanding of the way municipal bonds trade, or of the harmful consequences such a Proposal will have for the very retail customer they are claiming to help.

The Municipal Bond Business

Diamant is a small, self-clearing, municipal 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 municipal bond business, having worked full time at Diamant, our family owned business, for over 36 years. Although the Proposal was clearly written by articulate policy makers and lawyers, I suggest they pay close attention my comments, as they are from a seasoned municipal bond investment professional who has spent an entire career working in the municipal bond marketplace.

In the fixed income marketplace, business is conducted in very large, but imperfect auction market. It is an auction marketplace that is dependent not on computer listings of bonds, but on bids and offers from a diverse group of bond dealers that position bonds for future sale. As the Securities and Exchange Commission (SEC) has described in its July 31, 2012 Report on the Municipal Securities Market, there are over 1,000,000 bond CUSIPs outstanding, with a principal amount of more than $3.7 trillion. Note these bonds are not fungible, many CUSIPS trade infrequently, and there are different characteristics between bond issues even within the same municipality. 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. Bonds simply do not work this way. This is all pretty basic stuff, but apparently this point was missed when someone thought it would be novel idea to effectively treat municipal bond trading just like a riskless agency transaction.

In the auction marketplace of bonds, at times Diamant is the only bond dealer in the United States that has a position in a particular bond. This bond will be offered exclusively to Diamant clients. Months may pass before this bond trades again. Diamant takes on risk of capital to buy or sell bonds for future purchase or sale. Diamant conducts a nationwide business, trading bonds in certain segments of the market it has expertise in. For many decades, customers have placed their trust in Diamant's expertise and capability to locate safe, predominantly low risk, municipal bonds for them. Bond transactions are not about moving merchandise at a discount, as occurs in a commodity type of business. Instead, bond transactions are completed by finding the appropriate investment that fits the needs and objectives of each customer. That is why a customer remains loyal to Diamant. I must point out many other bond dealers participate in this auction marketplace in a similar way.

Diamant predominantly conducts a risk business in the fixed income sector, and does not employ a sales force to sell bonds. I must admit admiration of bond dealers that have a sales force that enables the trading of bonds in the same day they are purchased. This happens when a trading desk acquires an attractively valued bond, and the sales force is immediately able to locate customers to buy this bond. It happens frequently in the bond industry, yet the tone of this Proposal is that it is now bad that salespersons are pouncing on investment opportunities for their customers.

Although it is possible certain bond dealers may have a customer order in hand and are executing it in what seems like a riskless manner, it is also possible that most trades are occurring in a normal auction place, where a trader has built a bond position in their firm inventory, and the sales force are able to quickly locate customers to purchase the bond, perhaps within a very short time frame. A short time frame does not suggest such a trade is riskless, but rather that the sales team is very good at their job of selling bonds.

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. At times when large bond dealers are unable to bid bonds, the smaller bond dealers fill the void. And with other equally savvy traders actively engaged in the markets, this auction marketplace remains surprisingly competitive in the buying and selling of bonds. Just because this industry remains an auction market does not mean the current system is broken, or needs further regulatory interference in the guise of helping the customer.

EMMA

For those who want trade information, EMMA always remains available. There is nothing wrong with the regulatory finding that EMMA is not widely used. This simply means such information is not deemed important by most customers. Yet if over time such available disclosure information has not been considered important by most customers, then there is no merit to move forward with this Proposal to further disclose this unimportant information. The underlying problem with this regulatory Proposal is there really is no problem to be solved.

Distinguishing Between Institutional and Retail Customers

In the municipal bond market, both institutional and retail investors participate in this auction market. There is no marker that distinguishes institutional from retail investors. The MSRB Proposal incorrectly assumes the existence of a specific threshold, where transactions above a 100,000 par value are all institutional customers, and trades below this threshold are all retail customers. This is a very simplistic and arbitrary threshold that does not apply in this complex marketplace. Certain retail customers may buy or sell bonds above a 100,000 par value. And certain institutional customers may buy or sell bonds below a 100,000 par value, perhaps to add or reduce an existing position. At times a retail customer may buy a bond, and the seller is an institution. At other times an institutional customer may buy a bond, and the seller is a retail customer. The important takeaway is that retail and institutional customer trades are intertwined together in the auction marketplace, and there is no bright line of a 100,000 par value to separate the two. Thus this Proposal will impact both institutional and retail investors. To use the proposed threshold of a 100,000 par value, or any other artificial device to separate or identify a reference transaction size in such a complex market, is totally inaccurate. And as there is no bona fide threshold in the market, the negative impacts to retail investors from this Proposal will also spread to institutional investors.

Recent Comments By The SEC

On page 148 of the July 31, 2012 Report on the Municipal Securities Market by the SEC, there is a recommendation that the MSRB should consider requiring disclosure to customers of any markup or markdown. This report does not require the MSRB to mandate disclosure, which is what the Proposal represents, but to simply "consider" requiring disclosure. If the MSRB left the comfort of their desks to visit and engage numerous municipal bond dealers throughout the United States as part of a listening tour to see firsthand how municipal bond trades occur, enough information would have been collected to complete the consideration of such disclosure, the consequences to the retail investor, and the industry infrastructure that runs the fixed income marketplace. Then the municipal bond industry would not be faced with such a short sighted Proposal that now lies before us.

The impetus behind this MSRB rule Proposal seems to focus on a June 20, 2014 speech that Commissioner White made where she referenced the need for markup disclosure. This speech had a laundry list of many topics. Although I admire the Commissioner, the particular topic that triggered this Proposal was not well thought out. Her intent was to probe overcharging in some trades, but I firmly believe she was looking for a way to improve, not destroy, the retail municipal bond industry. Her comments on this issue were:

> "This information should help customers assess the reasonableness of their dealer's compensation and should deter overcharging. The need for markup disclosure is increasingly important as riskless principal transactions become more common in the fixed income markets."

The immediate question raised is whether overcharging is actually occurring. The MSRB has many years of data on every municipal bond trade that occurs, and FINRA conducts substantial audit work on the reasonableness of bond dealers compensation. By now it would seem reasonable to conclude that these regulators know if overcharging is commonplace. And if so, which bond dealers have a pattern of what may seem like overcharging, and what the circumstances are behind each trade.

It would seem rather straightforward to focus regulatory efforts on questionable trades and further review instances where overcharging may occur. Given the detail that went into preparing this Proposal, rest assured such statistics would have prominently displayed as overwhelming proof of this allegation and the reason for such a Proposal. Yet I have not seen news coverage on this issue for many decades. Although the topic of avoiding rampant overcharging is a noble cause, it is not an issue in the municipal bond market place.

My personal belief is it is wrong to overcharge, as the objective of this business is to provide quality bonds to valued retail clients at competitive yields so they return to buy more bonds. This simple philosophy has worked for many bond dealers like us for decades, and we really do not need a regulator to remind us of the need to take care of our customer.

Another important question raised is whether riskless principal trading is actually occurring. It is very easy to view historical data and make the arbitrary assumption that a same day trade between a dealer and a customer had no risk. However, at the point of the day when the bonds were not yet sold to a customer, the perspective of risk is different, as the bond dealer may not know for certainty whether a customer trade will occur. This introduces risk into the equation. Yet such trades are all being deemed riskless solely because it is easier for data compilation purposes. This means senior regulators are provided what may be inaccurate data from which to create policy statements that in turn attempt dramatic changes to the fixed income securities industry. It is both bad policy and dangerous to have regulators promulgate changes to an entire industry based on fundamentally inaccurate data.

A Very Bizarre Line Of Reasoning

The tone of the Proposal is that markups are somehow bad. This presumption has little to do with "helping" the customer with confusing partial disclosure. 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 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 municipal 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. 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.

In the municipal bond business, the retail customer needs the assistance of a professional to navigate the selection of available fixed income products. When a client buys 25,000 in bonds as in the example in Table 1, their most important decision points may include: the income stream (coupon); years until their principal is returned (maturity date); after tax return on the investment (a 3.9% 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 is the after tax return after state taxation; what other alternatives are available; whether this investment be should 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 makes this Proposal so bizarre is that the MSRB 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 is really not terribly relevant to the overall decision to purchase a bond. Finding out that the bond dealer in Table 1 had a gross trade profit of $494.75 is meaningless information in a decision whether to commit ~$25,000 to purchase a particular bond.

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 the gross profit was $494.75 instead or $394.75, or even $294.75? 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.

Of course the regulatory reader will counter by saying the disclosure may force the dealer to cut its gross profit and therefore the customer is better served. One would expect this perspective from regulators who apparently have not purchased a portfolio of bonds or have not worked in the industry they regulate. The gross profit is what is used to pay for all the components that keep a bond dealer in business. It is important to understand the difference between the gross profit and the net profit. Despite seeing a gross profit, it is possible there may be little net profit in a trade. 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.

In the example of Table 1, the dealer could have made a lower gross profit. The salesperson would be compensated less to communicate with their customer, the firm would not bother holding inventory it is unlikely to earn a net profit on, and the trader will not bother wasting time reviewing the marketplace. Reducing time spent on a trade and the associated customer service beyond the trade will all have to be reduced if the gross profit is the new focus of how to buy a municipal bond.

For those trades that occur with a disclosure requirement, the MSRB should expect that the customer will no longer receive the needed attention to the above critical decision points inherent in a trade, as the MSRB disclosure may reduce or eliminate the gross compensation of a dealer to provide these tasks. Then both the customer and the regulators can focus on the least relevant decision point in a transaction. In this game, the regulator now believes the trade is better for the customer, even though the customer may now own the wrong bonds without knowing it. Of course suitability comes into play, but one should not expect much effort on this beyond papering a file, as the important parts of the bond purchase decision are removed in order to display a lower gross profit. When one takes a hard look at this Proposal, it will actually harm a retail customer's ability to navigate the bond market and build a good portfolio for their hard earned money.

No Need For The Proposed Rule

In item 1 on page 13 of the Proposal, the assertion is made that the need for this Proposal is because the MSRB needs to ensure customer transactions are transacted at a fair and reasonable price. This is a stunning admission that the MSRB believes transactions are not occurring at a fair and reasonable price. If this true, then the MRSB has failed as regulator and should be disbanded.

The reality in the bond marketplace is different. The requirement to ensure customer transactions are transacted at a fair and reasonable price, pursuant to MSRB Rule G-30, has been in place for decades. Municipal bond dealers understand the rule, and make every attempt to comply with it. For many years the MSRB has received near real time trade information (15 minutes after every trade). On any given day it can review customer trades to ensure customer transactions are transacted at a fair and reasonable price.

In an imperfect auction market, where trades in a CUSIP may occur at different prices during the day, trades will happen at differing prices for differing quantity sizes, that may be higher or lower than other trades. To the extent the trade price seems way out of line, an outlier, one would presume the MSRB would have a mechanism in place to request further information on the trade. Presumably a regulator who is familiar with the working of the industry it regulates would be in a position to understand the level of effort a firm went through to complete a particular trade, or understand when a firm has no justification of what may be a pattern of outlier trades. This is what regulatory oversight is in the securities industry.

It is very misleading for the MSRB to allege that after decades of regulatory oversight, that it now believes the entire municipal bond industry is not effecting customer transactions at a fair and reasonable price, which therefore justifies the need for this Proposal. In my experience with decades of very comprehensive audits from regulatory examiners, it would be difficult for a municipal bond firm to remain in business if their intent was to transact their business in a manner other than to comply with MSRB Rule-30.

Evaluate The Market For Securities

In item 1 on page 13 of the Proposal, the MSRB now believes customers may not be able to evaluate the market for their securities. The only way one can make assertion is to assume that all retail customers are stupid, as they must have absolutely no idea what is going on in the world. And that those types of customers will finally be able to evaluate the municipal bond marketplace by knowing what the gross profit was on some confirmations.

In the last four decades in this industry, I have yet to meet a stupid customer. Every customer I have dealt with understands much more than the MSRB gives them credit for. Whether having a high school education or a doctorate degree, they all display good judgment, and they appreciate assistance in navigating the municipal bond marketplace. Most important, the current confirmation disclosure rules provide a sufficient description of exactly what they are buying.

Also, like many other bond dealers, Diamant provides customers with periodic portfolio appraisals that use an independent pricing source that illustrates the market for each of their securities. So when making the assertion that customers are unable to evaluate the market and therefore would benefit from more regulation and disclosure, the MSRB is simply insulting the intelligence of retail customers.

While the MSRB is questioning whether customers may not be able to evaluate the market for their securities, why stop with municipal bonds? In today's security marketplace, customers may not be able to evaluate the market for any of their securities or other investments.

Start with stocks. What makes a regulator think the price paid for a stock properly reflects the market for this security? High volume traders now dominate the trading activity, with their computers moving stock prices based on the parsing of text in the news flow. Customers do not actually know company sales and earnings when reviewing a company between earning releases. Recent price moves may not reflect earnings potential. And institutional investors may have access to better information than retail investors. Shouldn't there be a much greater concern by regulators of whether customers are able to evaluate the market for any of their stocks?

What about investments in annuities? What makes a regulator think the price paid for an annuity properly reflects the market for this security? Customers do not actually know how their complex annuity investment will work in the future. And they may have purchased this tax deferred investment within a tax sheltered vehicle such as their IRA, making the tax deferred benefit very difficult to understand. Shouldn't there be a much greater concern by regulators of whether customers are able to evaluate the market for any of their annuities?

What about investments in commodities such as oil? What about the price of home heating oil? Or the price of gasoline paid to drive a car? What makes a regulator think the price paid for any oil based commodity properly reflects the current market for this security? Customers do not actually know the real prices for a commodity when reviewing such purchases. Recent price moves may not reflect the underlying markets. Shouldn't there be a much greater concern by regulators of whether

customers are able to evaluate the market for any of their commodity related purchases, such as their gasoline and home heating oil?

In the United States, individuals are making reasonable decisions every day without being able to conduct a complete evaluation of every facet of information that may or may not pertain to their decision. This applies to securities investments, as well as every other economic decision they need to make. The fact that transactions continue to occur suggest that customers are able to evaluate the market using existing information for their securities. Thus another underlying premise of this Proposal, of customers now being unable to evaluate the market for their securities, is incorrect.

Unintended Consequences

Any securities firm forced to report gross markups on some bond trade confirmations will certainly harm their customer relationships. The anger and confusion from retail customers' who receive this partial information on some bond trades but not others, without understanding how the fixed income auction market works, or the level of effort that went into the locating and acquisition of a specific bond, will boil over throughout the municipal bond industry. Human nature being what it is; customers will consider any markup number disclosed pursuant to this Proposal to be too large. Everyone should expect customers who are given disclosure of a gross profit number on a trade to be upset the number is not smaller.

Before the regulatory reader gets a smug sense of satisfaction, one needs to understand what happens next. If a confirmation disclosure from a municipal bond transaction is perceived to harm a customer relationship, most securities bond dealers will simply stop trading municipal bonds. Wall Street is full of smart people who will find some other way to service their customers tax exempt income needs without dealing in specific municipal bonds.

It is laughable to think that the effect of this Proposal will be to enhance competition between bond dealers. Most bond dealers enjoy their own client base that has been cultivated over time. Because of the complexities of buying bonds which are not fungible and may not available at other bond dealers, these purchases are not shopped between bond dealers. Each firm provides an investment experience that its clients seek, at a service level which may differ from other bond dealers. Under this Proposal, a low volume firm with a small sales force will likely have few, if any, disclosures to make on their confirmations, as they may not trade the same CUSIP within a day. Bond dealers with high trading volumes may trade the same CUSIP within a day, and will have disclosures on many of their confirmations. Thus some bond dealers are forced to disclose, while others are not. From a pure economic perspective, the firm making disclosures is at a competitive disadvantage to the firm that does not need to make disclosures.

Under this perspective, a firm like Diamant would benefit from this Proposal. Yet the municipal bond business is such that Diamant also needs other bond dealers, both large and small, to remain viable in order for the auction marketplace to work. Therefore Diamant is opposed to this type of regulatory interference that places another bond dealer at an artificial competitive disadvantage to another.

Given retail trading represents nearly 70% of the trades in the municipal bond business, the cessation of retail trading in response to this MSRB Proposal will destroy the market for retail trades in municipal bonds. And as many small and mid sized municipal bond dealers are active in niche sectors within this retail market, they will be greatly harmed regardless whether the disclosure Proposal even applies to their type of business.

Even though this disclosure requirement would not apply, Diamant would be part of the collateral damage as the marketplace stops functioning without the inclusion of other bond dealers with retail clients. And this avalanche of unintended consequences creates a major liquidity problem for retail investors who need to either buy or sell municipal bonds as bond dealers exit the bond business.

How To Harm Retail Customers And Damage The Municipal Bond Industry Infrastructure

The best way for the MSRB to harm retail customers and damage the municipal bond industry infrastructure is to proceed exactly with this Proposal. The MSRB will celebrate achieving disclosure not seen in other industries, and then will wonder why the bond dealer community stopped handling retail customer trades. What a brilliant disaster.

How can the retail customer be harmed with this disclosure? First of all, municipal bonds will stop trading at many if not all bond dealers. Why would any bond dealer want to effect trades that antagonize their relationship with their customer, and create unknown liabilities of future trade cancellations, regardless whether such trades provide great value to their clients? If this Proposal is implemented, my immediate response will be to prohibit trading any municipal bonds from or to retail customers, for any bond that meets the disclosure definition under this Proposal. Not only would customer relationships be harmed, but the additional compliance costs would be excessive for just these specific types of trades. Many other bond dealers may arrive at the same conclusion. The harm is that the retail investor will be denied liquidity in what remains of the municipal bond marketplace.

Secondly, many entrepreneurial bond dealers like Diamant, are a part of the municipal bond auction marketplace that will become part of collateral damage from this proposed ruling. I take great offense that the MSRB is acknowledging the destruction of capitalism in the bond marketplace, by accepting the collateral damage to many bond dealers and brokers. In the section of the Proposal titled "Effect on Competition, Efficiency and Capital Formation", the MSRB proclaims the likely effect is competition between bond dealers will be enhanced. Yet in the very next paragraph the MSRB contradicts itself by acknowledging the costs could lead small bond dealers to exit the market. Somehow there is supposed to be more competition with fewer industry participants. This makes no sense.

Third, it is hard to imagine that this Proposal will achieve fair and reasonable prices for any customer after this collateral damage occurs. Bond dealers collectively provide necessary components to the maintenance of liquid markets. Our absence will harm retail, institutional investors, and any remaining bond dealers. It is important to remind the MSRB that the complex fixed income marketplace does not and cannot operate on some computer program. It runs on the efforts of numerous talented individuals employed at numerous bond dealers, without whom the market simply stops. I have been around long enough to see a temporary stop in municipal bond trading, and it is frightening.

Fourth, from an operational perspective, the MSRB must understand that bond dealers are unable to comply with identifying reference transactions without incurring substantial costs to back office operations. It will be easier to create a firm wide immediate stop trading system on a CUSIP before or just after a retail customer trade occurs, than to monitor all trade volume before or after the retail trade occurs. Even if a firm does not expect to have to make disclosure, they will have to have both a back office and compliance system in place to identify transactions that meet this Proposal and then process such trades in a manner completely different than other trades. Who thought this was a good idea?

It is completely naive to think that every firm just waves a magic wand to achieve instant compliance with a rule that will be very difficult to comply with, even at a low volume dealer. Compliance costs will be very significant to create a separate purchase and sales module to existing back office systems to identify applicable trades and then create a substantive, unique disclosure document on selected confirmations. This process will delay the sending of such trade confirmations as there will have to be a completeness check on all impacted confirmations prior to mailing, and an internal audit function to assure that every bond transaction that meets certain eligibility is part of this exception processing. These additional processes and reviews will likely delay the batch production and mailing of all securities confirmations for that trade date until the broker dealer is confident the confirms that need disclosure have been properly prepared.

As this has never been done before, we do not have a hard data processing quoted cost to achieve this. If we were to create a new automated separate purchase and sales module to integrate within our legacy back office system, we would likely have to start with a budget at $100,000. For our size firm, it would take several years of diverting trading all net profits from municipal bonds to cover this cost. As this is an unworkable solution, the person who ultimately must pay for the additional per trade compliance costs for this Proposal is the customer. This additional cost will have to be added to each transaction. Most clairvoyant readers will understand the increased operational and compliance costs added to each transaction actually is harming the very customer this Proposal is claiming to "help".

Alternatives To This Absurd Proposal #1- Internal Regulatory Rules

If the MSRB is fixated on bond reference disclosure, then let the bond dealers create their own sets of rules on how to handle trading in manner that avoids all disclosure. The way to achieve this is to make sure the bond dealer only completes one principal trade to a retail client in any particular CUSIP for any particular trading day. Should a firm trade a CUSIP in the morning to a retail client, they would have to stop bidding or trading this bond throughout the remainder of the day. Conversely, if that CUSIP had traded somewhere else in their firm during that day, the firm would also need to modify its systems to refuse to sell these bonds to a customer by creating an internal stop trading system. In this manner, even though the customer may want to purchase a particular bond which really fits the customer's investment needs, they may not be able to buy the bond due to a regulatory time delay. And if a customer needs to raise cash immediately, in this environment they will have to understand there is now a regulatory time delay in their sale. This regulatory time delay is the direct result of such a naive Proposal, but it is a workable solution for the dealer community.

Aside from a regulatory time delay, what happens to the auction marketplace as bond dealers create their own sets of trading rules to comply with this Proposal? After this Proposal is implemented, the last thing a bond dealer will want is to inadvertently buy bonds in the same day a customer purchased bonds. So bond dealers will need to change all their Street bids as being subject to being pulled at any time. Instead of firm bids that are good for the day, municipal bond brokers and other participants (such as bond dealers representing other retail and institutional customers) will be working with un-firm bids from the Street that really just are indications of where bond dealers might want to buy a bond if no other trades occur in the bond that day at their firm.

With un-firm bids, the auction market in municipal bonds ceases to function properly. As an illustration of un-firm markets, I will always remember how the stock market quotes were un-firm when the equity markets were having difficulty functioning during the stock exchange market crashes of 1987, 1998, 2002, and 2008. One does not need a vivid imagination to understand what happens in an auction marketplace when rates move and the bidding bond dealers who understand the bonds refrain from bidding due to this new rule. Large, ten point spreads would be commonplace, assuming a bona fide bid materializes. This substantial market impact will be a direct result of this Proposal.

Alternatives To This Absurd Proposal #2- Time Period

If the MSRB has already decided to proceed with this Proposal prior to reading industry comment letters, then modify the time period for disclosure between offsetting trades in a CUSIP to be within 15 minutes of the first trade. This will enable back office operations to identify adjacent trades that would need disclosure, while permitting municipal bond dealers to continue to operate in the marketplace during the rest of the day without triggering inadvertent disclosure. Moreover, back office enhancements can be designed in a much more cost effective manner if they focus on adjacent transactions within 15 minutes instead of the entire trading day. In this scenario, bond dealers may actually be able to afford the additional compliance costs. As important, the reference trade can be identified and then reported in the same 15 minute time frame using the same system as RTRS. This will provide near real time reporting of "riskless" trades for regulatory review, and provide for accurate manual procedures of identifying in back office operations the specific confirmations that need special handling and processing.

Alternatives To This Absurd Proposal #3 - Exclusions

If the MSRB has already decided to proceed with this Proposal prior to reading industry comment letters, it would be prudent to include exclusions for certain types of transactions notwithstanding the fact they are retail sized transactions. In addition to excluding institutional investors, the Proposal should also exclude entities that act with institutional type knowledge. This should include banks, trust companies, and registered investment advisors that are employed by individual and institutional customers to invest their portfolios and make transaction decisions on behalf of their customers.

Alternatives To This Absurd Proposal #4- Listed Exchange

Maybe the real intent of the MSRB, under the guise of selected confirmation disclosures, is to completely change the marketplace which it regulates. If so, then instead of half measures like this Proposal, perhaps the MSRB should complete the destruction of the auction marketplace as we know it. There may be no further need of having skilled trading professionals at numerous bond dealers acting as an auction marketplace. Instead the MSRB could mandate to change the entire municipal bond business from an auction marketplace to one where the MSRB acts as a listed exchange to simultaneously make the entire market for over 1,000,000 different CUSIPS. This would be reminiscent of the New York Bond Exchange back in the 1980's, that had occasional markets, in some corporate bonds, with bid and ask sizes of around 2,000 to 3,000 in face value. But in this case the MSRB would create a riskless marketplace that would always maintain deep markets for all CUSIPS, of at least 100,000 par value in both bid and ask sizes.

Because the market would now be riskless with only one exchange controlling the entire market, pricing efficiencies would be attained. All market participants would expect very small spreads between bid and ask from the MSRB listed exchange, perhaps as little as a tenth of a basis point. To achieve this grandeur, the MSRB would simply have to initially commit several trillion dollars of their capital in order to maintain sufficient market depth in every bond CUSIPS that come to their marketplace.

This way our municipal bond industry would remove capitalism from the marketplace and let the government regulators make the entire market. In this concept, bond dealers would be able to always sell blocks of bonds to the MSRB listed exchange at the market. Most importantly, when yields move higher, the same bond dealers then would be able to buy these blocks of bonds back as the MSRB computer algorithms would of course have marked down the positions to reflect much lower market prices.

This concept would create the riskless market to participants that the MSRB currently believes exists. This fantasyland type of idea would be a boon to the municipal bond dealers as they could remove the market risk from their inventory positions. And by permitting bond dealers to establish either short or long positions on bonds traded on the MSRB listed exchange, they could profitably employ traders. Also the customers would enjoy riskless trading, as long as the MSRB listed exchange, as a systemically important financial institution, continues to engage in this non-profit business without filing for bankruptcy.

This scenario is the alternative to an auction marketplace. When the Proposal destroys the auction market place, the MSRB should have a plan in place similar to this one to avoid harming the retail customer while maintaining liquidity for the remaining participants.

Alternatives To This Absurd Proposal #5- No Action

After reviewing the Proposal and alternatives, the MSRB 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.

The auction marketplace has many intertwined industry participants that include retail customers; institutional customers; large municipal bond dealers; mid-size municipal bond dealers; smaller municipal bond dealers; municipal bond dealers that trade mainly with other municipal bond dealers; municipal bond dealers that trade mainly with their customers; and bond brokers that facilitate trades between all types of municipal bond dealers. All these participants within this very large auction market will be adversely impacted. The noteworthy harm will occur to retail customers that will be unable to trade bonds on days that their bond dealer decides not trade their CUSIP, in order to avoid disclosure of this Proposal. The larger harm will come from the auction marketplace no longer having liquidity. This occurs from the absence of firm bids as bond dealers stop trading bonds that would trigger the disclosure in this Proposal. These are terrible, yet very realistic outcomes from this Proposal.

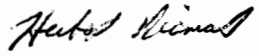
Harming the relationship between the customer and the bond dealer, and having bond dealers reduce or eliminate retail trades, all for the sake of this misguided Proposal, simply does not add any benefit to the retail customer.

In this reasonable alternative, the MSRB must simply recognize the complexity within the entire fixed income marketplace, review the alternatives, and commit to taking no action on the entire Proposal.

Conclusion

While on the very surface the Proposal seems a noble idea, as shown throughout my response, it actually opens up a Pandora's Box that is uncontrollable in terms of damage to the fixed income auction markets. Moreover, the Proposal is trying to solve problems that do not exist. Most customers are being treated fairly by the markets. So there is no reason to run a regulatory wrecking ball through a working auction marketplace in a manner that destroys capitalism, impairs retail customer access to markets, and impairs or shuts down bond firms. The conclusion must be that the MSRB thoroughly reviewed the matter in a meaningful way, but after careful consideration of the unintended collateral damage to the marketplace, decided to take no action in order to continue maintaining an orderly and regulatory compliant market in municipal bonds.

Yours truly,



Herbert Diamant
President

January 20, 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 14-52,
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2014-20,
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:

Fidelity Investments[1] ("Fidelity") appreciates the opportunity to respond to the Financial Industry Regulatory Authority's ("FINRA's") Regulatory Notice 14-52 and the Municipal Securities Rulemaking Board's ("MSRB's") Regulatory Notice 2014-20 (together the "Proposals").[2] The Proposals seek to provide retail investors greater information on fixed income pricing by requiring brokers, dealers and municipal security dealers ("broker-dealers") to disclose, on customer confirmation statements, the price to the customer, the price to the broker-dealer, and the differential between those two prices for same-day, retail-size principal transactions in corporate, agency and municipal securities.

[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. Fidelity generally agrees with the views expressed by the Securities Industry and Financial Markets Association ("SIFMA") in their comment letter to FINRA and we submit this letter to supplement the SIFMA letter on specific issues.

[2]*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. ("FINRA Proposal") *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 ("MSRB Proposal") Unless otherwise defined in this letter, capitalized terms have the meanings ascribed to them in the Proposals.

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.

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 investor choice.

Fidelity's fixed income pricing for its self-directed retail brokerage customers is transparent, simple and low for the brokerage industry. 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 bond offerings from unaffiliated third-party sources. When FCM is not the offering dealer, Fidelity's compensation is limited to a $1 per bond transaction fee for most fixed income securities. We disclose this fee 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 $1 per 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. A 2013 study found that Fidelity was less expensive 98.6 percent of the time versus "mark-up based" brokers that bundle transaction fees with the price of the bond.[3]

Although we fully support regulatory efforts to enhance fixed income price transparency, we do not support the Proposals as currently written and believe they should be withdrawn. While well intentioned, we believe the Proposals will confuse rather than clarify fixed income pricing for retail investors because 1) they apply to a wider spectrum of trades than simply riskless principal transactions; 2) they apply to some, but not all, retail fixed income transactions; and 3) they use different terminology and disclosures to meet the same regulatory goal. The Proposals also present serious operational and logistical challenges that render them unworkable for many market participants. In place of the Proposals, we urge FINRA and the MSRB to consider alternatives that meet the same policy goals, such as further enhancements to existing fixed income price discovery tools for retail investors, *i.e.* FINRA's Trade Reporting and Compliance Engine ("TRACE") and the MSRB's Electronic Municipal Market Access ("EMMA") system.

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[3]For further information regarding this study, see *Fidelity's Message for Retail Bond Investors: Comparison Shop — it Can Make a Big Difference* (September 20, 2013) *available at*: https://www.fidelity.com/about-fidelity/individual-investing/fidelitys-message-retail-bond-investors

The Proposals Will Not Help Retail Investors

For some time, regulators have considered requiring broker-dealers to disclose markups in "riskless principal" transactions.[4] Although "riskless principal" transactions are not defined in the Proposals, they are generally understood to mean purchases and sales done with a contemporaneous, offsetting customer order in hand, so there is little or no chance that the market could move against the broker-dealer.

The Proposals seek to ensure fairness and transparency around mark-ups in riskless principal transactions by requiring broker-dealers to provide mark-up disclosure on a subset of retail customer fixed income transactions that 1) match one or more same day principal orders and 2) meet certain size requirements.[5] We believe that the over- and under-inclusive scope of the Proposals will do little to clarify fixed income pricing for retail investors.

The Proposals require broker-dealers to identify all possible principal and customer matching scenarios for certain fixed income transactions over the course of a day and provide retail investors mark-up disclosure on these transactions, some of which may be "riskless principal" transactions, others not. In identifying matched trades, broker-dealers must navigate an overly complicated – and at times conflicting – matching methodology. For example, under certain circumstances, the Proposals specify a "last in first out" methodology for matching trades and under other circumstances, the Proposals specify a "weighted average price" methodology for matching trades. A potential result of this matching methodology is that a retail customer may receive pricing information on a composite of principal trades that simply happened to occur on the same day as his or her trade, but that are unrelated to their actual trade.

Moreover, the Proposals do not apply to all retail customer fixed income transactions. Retail customers will receive the proposed disclosure only on select transactions meeting established size and time criteria. Other fixed income transactions, not meeting size and time

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[4] *See* for example, Report on the Municipal Securities Market, U.S. Securities and Exchange Commission (July 31, 2012) and Speech by SEC Chair Mary Jo White *Intermediation in the Modern Securities Markets: Putting Technology and Competition to Work for Investors* (June 20, 2014).

[5] The FINRA Proposal would require confirmation disclosure where a broker-dealer 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). This disclosure would include (i) the price to the customer; (ii) the price to the broker-dealer of the same-day trade; and (iii) the difference between those two prices. The rule would define "qualifying size" as a purchase or sale transaction of 100 bonds or less or bonds with a face value of $100,000 or less, based on reported quantity. The MSRB Proposal would require a dealer to disclose on the customer confirmation its trade price for a defined "reference transaction" as well as the difference in price between the reference transaction and the customer trade. A reference transaction is defined in the MSRB Proposal as one in which the dealer, as principal, purchases or sells the same security that is the subject of the confirmation on the same date as the customer trade. The disclosure requirement would be triggered only where the dealer is on the same side of the transaction as the customer (as purchaser or seller) and the size of such dealer transaction(s), in total, would equal or exceed the size of the customer transaction.

parameters, will not receive this disclosure. In the end, we fail to see how the Proposals will help retail investors who may, at best, be confused as to why this disclosure appears on some -- but not all -- of their fixed income transactions and at worst, receive broker-dealer pricing information on securities unrelated to their actual trade.

We also note that the Proposals use different terms, phrases and structures for initiatives designed to work together to meet the same regulatory goal. For example, FINRA's Proposal would require broker-dealers to disclose (i) the price to the customer; (ii) the price to the broker-dealer of the same-day trade; and (iii) the difference between those two prices, while the MSRB's Proposal would require a municipal securities dealer to disclose its trade price for a defined "reference transaction" as well as the difference in price between the reference transaction and the customer trade. These differences are likely to confuse retail investors who purchase a variety of fixed income products as well as impact implementation efforts at broker-dealers.

The Proposals Are Not Workable For Market Participants

The Proposals would add significant operational challenges and risks to the confirmation statement process by adding new layers and requirements onto already complex systems.

The Proposals would require broker-dealers to build a significant new system, at considerable cost, to match trades that meet an artificial definition of a riskless principal transaction.[6] By necessity, this system will need to identify all possible matching scenarios for all principal fixed income transactions over the course of the day 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.[7]

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.

[6]At present, we believe that it would be a sizable effort simply to understand the costs of building a new system to identify "matched trades" under the various methodologies that FINRA and the MSRB have proposed.

[7]For example, at many financial services firms, a single broker-dealer is shared across multiple business units, complicating the matching of trades under the Proposals. Similarly, the Proposals do not address fairly common situations in which a dealers' institutional, retail, and proprietary trading desks operate independently, complicating whether and how transactions would or should be disclosed and/or matched across affiliated desks. It is also not clear how computations would be made, and what disclosure added, to customer confirmation in certain situations, *i.e.* if the customer trade was executed in partial fills, in the event of a cancelation or re-billing of a transaction, or in the case of an investment adviser block size purchase of bonds that was subsequently allocated to retail customer accounts.

Fully-disclosed clearing broker-dealers clear and settle millions of securities transactions each day for thousands of introducing broker-dealers.[8] 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, and 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.

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. Industry standard processing of retail customer trade confirmations involves batching and pricing during the day, processing immediately after market close, overnight composition, with printing and mailing the next business day.[9] 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.

[8]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).

[9]Trade confirmations to institutional customers are sent on a real-time basis through the DTCC system for trade affirmation. To the extent an institutional customer's fixed income trade met the size and dollar parameters of the Proposals, this process would require significant changes.

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 determine (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.

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.

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 bonds, and unit investment trusts ("UITs") from T+3 (trade date plus three days) to T+2 (trade date plus two days).[10] Once achieved, DTCC has recommended a pause and further assessment of industry readiness and appetite for a future move to T+1.[11] 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.

[10]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).

[11]*Id* at 2.

Proposed Alternatives

We believe that the Proposals' efforts to improve the transparency of fixed income pricing information for retail investors while well intentioned fall short in a number of areas and should be withdrawn. In place of the Proposals, we recommend FINRA and the MSRB consider the following alternatives and modifications that we believe meet the same policy goals as put forth in the Proposals.

TRACE and EMMA. Retail customers can currently use TRACE to determine pricing information for a fixed income security that is eligible for TRACE reporting, including the last trade price, execution time and execution quantity, using either the issuer's name or the CUSIP number. The MSRB's Proposal would provide investors with information generally already publicly available on the MSRB's EMMA website but would provide it directly to investors in connection with their transactions. Given the significant amount of data already available to investors on TRACE and EMMA, FINRA and the MSRB should explore further using these existing price transparency sites as viable alternatives to the Proposals.

For example, we support greater opportunities for direct access to TRACE and EMMA by retail customers through their online brokerage account platforms, as well as through retail investor education efforts more generally. We believe that investors are more likely to use this information if it is readily available to them. For this reason, Fidelity already makes real-time trade reporting from FINRA TRACE and MSRB RTRS available on *Fidelity.com*.

We also believe that it would be fairly easy to provide CUSIP-specific links to EMMA and TRACE historical transaction data on customer confirmation statements. Currently, EMMA uses intuitive, retail customer-friendly hyperlinks to information on its website. For example, to obtain trade activity history for Massachusetts State GO Bonds Series 2009A, 4%, 3/1/2015 (CUSIP 57582PPT1), a retail customer could simply type the following hyperlink into their internet browser: emma.msrb.org/SecurityDetails/TradeActivity/57582PPT1. The only variable portion of the hyperlink text is the CUSIP number. FINRA could adopt a similar hyperlink protocol to allow retail customers to obtain TRACE trade activity for a particular security on its website. These hyperlinks could be printed on trade confirmation statements with a brief description of the information that can be found on the respective sites. We believe that this alternative approach would provide retail investors with far more price reference information than a single trade could provide, and can also help drive increased adoption of TRACE and EMMA by retail investors.

Shorten Time Horizon. FINRA notes that it "has observed that over 60 percent of retail-size customer trades had corresponding principal trades on the same trading day. In over 88 percent of these events, the principal and the customer trades occurred within thirty minutes of each other."[12] Despite this data, the Proposals would apply to all retail-size principal trades executed on the same day as a customer trade. We believe that the Proposal's full day time

[12]FINRA Proposal at page 2

horizon is unnecessarily long and fails to consider that market conditions can significantly change over the course of a day that could impact pricing, *e.g.* severe market moves, increased volatility and limited liquidity.

If a new confirmation disclosure obligation with specific price references must use a "matched trade" concept, we believe the time horizon for this disclosure should be reduced. We believe that a majority of riskless principal transactions occur well within 15 minutes of each other. To better address the regulatory goal of increased price transparency in riskless principal transactions, if a "matched trade" concept must be used, FINRA and the MSRB should reduce the time window for matched trades from a full business day to 15 minutes.

Certain Aspects of the Proposals Must be Clarified

Although we believe that the Proposals should be withdrawn, if FINRA and the MSRB ultimately go forward with the Proposals, we recommend that certain aspects are clarified prior to final rulemaking.

Allocations

FINRA and MSRB should clarify that the determination of whether specific transactions are subject to the Proposals' disclosure requirements should be applied at the parent account level, not at the sub account level. Transactions with investment advisers in amounts exceeding any qualifying size or allocated to retail customers of the investment adviser, should not be subject to the proposed confirmation disclosure obligations. It would be enormously complex and potentially impossible for broker-dealers to allocate various portions of an institutional block trade into retail customers' respective components, particularly since investment adviser direction for allocations does not typically come to the clearing broker-dealer until the end of the business day. For example, a purchase of $500,000 face amount of a bond by an investment manager on behalf of advisory clients will be booked as allocated and confirmed at the sub account/end customer level, potentially as ten, $50,000 transactions at the end of the day. We believe that disclosures aimed at retail investors should not be required in this case because the investment adviser or other institution making the transaction decision has access to pricing information.

Affiliated Desks

FINRA and the MSRB should also clarify that trading by separate desks and affiliates is not subject to the disclosure requirements. Many broker-dealers employ a separate, specialized trading desk structure, where for example, one desk or group covers the firm's intermediary client trading, another is designated coverage for institutional accounts, and another trades solely on behalf of the firm's retail client accounts (or similarly, transactions for the intermediary, institutional, or retail accounts of a member firm's affiliate).

We believe that trading activity by separate trading desks and affiliates should not be matched. We do not believe that the disclosure of unrelated reference transactions by affiliates

and/or affiliated desks will be helpful to retail customers. Moreover, matching trading activity by separate trading desks and affiliates will significantly increase the complexity of implementation efforts for many broker-dealers who, by design, currently segregate or block this transactional information between desks/businesses.

* * * * *

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
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Via Electronic Delivery

January 20, 2015

Ronald W. Smith
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Municipal Securities Rulemaking Board
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Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: MSRB Notice 2014-20 - Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations; FINRA Notice 14-52 - Pricing Disclosure in the Fixed Income Markets

Dear Mr. Smith and Ms. Asquith,

The Financial Information Forum (FIF)[1] would like to take this opportunity to comment on MSRB Notice 2014-20 - Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations and FINRA Notice 14-52 - Pricing Disclosure in the Fixed Income Markets ("Requests for Comment"). We appreciate the willingness of the MSRB and FINRA to seek feedback on these important issues in a coordinated manner and will respond to both notices in this comment letter.

With respect to the Requests for Comment, FIF respectfully makes the following recommendations:

1. Fully align efforts of MSRB and FINRA regarding these proposals
2. In order to minimize implementation challenges, consider the alternative approach of leveraging existing EMMA and TRACE data
    a. Add a link to EMMA and TRACE data on the customer confirmation
    b. Aggregate EMMA and TRACE data into a single website
    c. Perform a survey of retail investors to identify enhancements to EMMA and TRACE
    d. Further educate retail investors on EMMA and TRACE functionalities

FIF's perspectives on the proposals in the Requests for Comment are discussed in more detail below.

[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.

Aligning Efforts of MSRB and FINRA Imperative

FIF members appreciate that the MSRB and FINRA have taken a coordinated approach in proposals to require dealers to provide pricing reference information on retail customer confirmations. While the Requests for Comment issued by MSRB and FINRA are similar, there are differences in some of the details. For instance, in Example 7 of the Proposed Disclosure Requirement section of the FINRA Notice, the example requires the weighted average price of the firm's trades to be disclosed on the customer confirmation. In Example 9 of the same section, FINRA expects that the firm would consistently apply a last in, first out (LIFO) methodology that would refer to the last principal trade(s) that preceded the customer trade. These scenarios are not defined in the MSRB proposal and it remains unclear if the MSRB would mirror the FINRA requirements. We believe costs to dealers would increase exponentially if there are any variations between the FINRA and MSRB rules. FIF members urge MSRB and FINRA to be fully harmonized in any resulting regulations.

Significant Implementation Challenges as Proposed

These proposals will lead to operational and technological challenges that will increase costs to dealers as outlined below.

- Capturing trades to make sure dealers are tying principal trades to customer trades will be challenging. The process will be even more challenging for batch trades. Programming systems to match principal batch trades with customer trades would be a very complex process involving trade by trade matching. Enhanced audit trails will need to be built to validate system processes. Larger firms may have order management systems that can be modified to comply but smaller firms may end up having to do this manually. Matching principal and customer trades will be further complicated by trade cancels and rebills. This trade capture piece alone will lead to significant costs.
- Customer confirmations are currently produced at the time of the trade. All customer confirmations would need to be produced at the end of day in the proposed rule in case a corresponding principal trade is executed. Programming trading systems to wait until the end of the day to see if a corresponding trade is executed and adding information retroactively to the confirmation will be a costly, time-consuming task.
- Another programming challenge would be crafting systems to suppress resubmission of trades to regulators if a confirmation needs to be modified with pricing reference information at the end of the day. Systems would need to be able to recognize that this is a trade information modification affecting customer confirmations that does not require resubmission of the trade.
- The MSRB and FINRA proposals both apply to retail-sized transactions of 100 bonds or fewer or bonds in a par amount of $100,000 or less. Since the proposals are not limited to transactions of actual retail customers, institutional trades may fall within the parameters of these proposals. For the majority of FIF members, institutional trades flow through Omgeo's TradeSuite Institutional Delivery (ID)[2] via DTCC's ID System. Each transaction is confirmed and affirmed/matched through Omgeo's TradeSuite system, which distributes the affirmed confirmation to appropriate parties of the trade. If this rule applies to retail-sized institutional trades, the ID System may be required to add additional fields to the confirmations it generates to comply with the rule. The costs associated with implementing these fields at DTCC and Omgeo should be evaluated in the cost-benefit analysis for these proposals. To address this concern, FIF recommends limiting the parameters of these proposals to transactions of 99 bonds or fewer or bonds in a par amount of $99,000 or less. Doing so would eliminate potential

[2] TradeSuite ID is a 10b-10-compliant solution which automates messaging and settlement for equity and fixed income securities. It provides seamless connectivity from execution to settlement on domestic and cross-border trades of U.S. securities.

institutional trades or DVP/RVP transactions and therefore focus more on retail customer trades. This would make trading systems' programming logic to determine when pricing reference information should be on a customer confirmation much less complex. The best way to ensure that only retail trades are impacted is to clearly articulate in the proposal that the requirements only apply to accounts of natural persons.

Other Considerations

FIF members understand that the MSRB and FINRA would like to better inform retail investors. However, it is not certain that providing pricing reference information on retail customer confirmations will achieve this goal. Providing the price of the corresponding principal trade in comparison to the customer trade may be misleading. Overhead costs, such as compliance and technology, need to be factored into pricing securities in customer transactions. Additional information may need to be provided to customers explaining what their price represents and that there are other costs to broker dealers that are not strictly represented in the execution of the principal and customer trades. Providing this additional information to customers will continue to increase implementation costs. Furthermore, pricing reference information on customer confirmations could lead to some irrelevant data being reported to customers at the end of the day. While the fixed income markets fluctuate daily, customers could be receiving confirmations that show stale pricing as a result of intraday market movement. Overall, FIF members believe additional information on the confirmation may actually confuse customers as they will be seeing multiple prices listed. Customers may also wonder why they see additional information on only some of their trade confirmations and not on others.

FIF members would also like clarification on how to treat customer allocations of institutional-sized trades in the current proposals. If a broker dealer buys 500 bonds early in the day and sells 400 of those bonds to a customer later in the day, we understand that no pricing reference information would be required on the customer confirmation. If that client now requests separate allocations to sub accounts of 80 bonds to five different accounts, each of those allocation transactions would get a confirmation for the purchase of 80 bonds. Under these proposals, would those transactions require pricing reference information to be disclosed on the customer confirmations? There will always be a distinction between institutional and retail-sized pricing. Disclosing these markups to customers on confirmations may mislead customers as they won't be provided the context that the principal trade was an institutional-sized lot. FIF members request clarification on this scenario.

Recommendations

If the MSRB and FINRA decide to proceed with the proposals in the Requests for Comment, FIF members have the following recommendations:

- As mentioned above, ensure the MSRB and FINRA align efforts in any final regulations
- Eliminate institutional trades from the scope of these proposals
    - Add the definition of natural persons when determining which investors this rule will apply to. This will ensure the rules apply to retail customers only and will eliminate institutional trades from these regulations.
    - Apply the rule to retail customer trades of 99 bonds or fewer or bonds in a par amount of $99,000 or less, instead of the proposed 100 bonds or fewer or bonds in a par amount of $100,000 or less.

FIF members believe the MSRB and FINRA should consider alternate approaches to achieve their goal.

One step MSRB and FINRA could take is to require that broker dealers provide links or reference to EMMA and TRACE on customer confirmations. This would leverage the work that the MSRB and FINRA have already done to provide pricing reference information to retail investors and may expand the

awareness of these sources of data. Retail investors can utilize EMMA and TRACE data to acquire market information and evaluate the costs associated with their transactions. The MSRB and FINRA currently provide the ability for retail investors to identify same-day principal trades of the same security as their individual trades. We don't believe investors that utilize this information and actively seek it out would benefit from similar information on their customer confirmations. Realistically, customers would benefit much greater by using EMMA and TRACE in real-time compared to pricing reference on confirmations as they can obtain reference pricing information prior to submitting their trade. In this manner, we believe a link on customer confirmations to EMMA and TRACE data would satisfy the same goal as these proposals to better inform retail investors with much less implementation impact.

Additionally, MSRB or FINRA could aggregate all trade data available on EMMA and TRACE to provide a single website so customers can visit one place for all of this information. Dealers could then put a single link on customer confirmations further simplifying implementation.

The MSRB and FINRA could also survey retail investors to gauge their knowledge and usage of EMMA and TRACE. This could serve to inform retail investors of EMMA and TRACE benefits and functionalities, and bring to light ways to improve upon the accessibility of the data.

Finally, the MSRB and FINRA could further educate retail investors on EMMA and TRACE functionalities. Pricing reference information is already available on EMMA and TRACE. Creating summary documents or holding webinars that detail how to access information in EMMA and TRACE would allow for broader customer usage. Education combined with a survey and references to EMMA and TRACE on customer confirmations would lead to better informed retail investors.

In conclusion, FIF would like to thank the MSRB and FINRA for providing the opportunity to comment on the proposed changes. We look forward to a future meeting with DTCC, MSRB and FINRA in order to discuss the issues raised in the letter.

Regards,

Darren Wasney
Program Manager
Financial Information Forum

FINANCIAL SERVICES INSTITUTE

VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS AND INDEPENDENT FINANCIAL ADVISORS

VIA ELECTRONIC MAIL

January 20, 2015

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

Re: **Regulatory Notice 2014-20: Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations**

Dear Mr. Smith:

On November 17, 2014, the Municipal Securities Rulemaking Board (MSRB) published its request for public comment on proposed recommendations to require additional pricing disclosure on customer confirmations for retail municipal securities transactions (Proposed Rule).[1] The Proposed Rule requires broker-dealers to include on customer confirmations for retail size municipal securities transactions: (i) the price to the customer; (ii) the price to the dealer of the same-day principal trade; and (iii) the difference between those two prices. The Proposed Rule would only apply in circumstances where the firm has executed a same-day principal transaction offsetting the customer's transaction. MSRB stated that it believes increasing pricing disclosure for municipal securities transactions will allow investors to better evaluate their transaction costs and the fairness of the price they paid or received.

The Financial Services Institute (FSI)[2] appreciates the opportunity to comment on this important proposal. FSI welcomes regulatory initiatives to help improve investor education and disclosure in the municipal securities market. As such, we support the principle that retail investors should have access to timely and complete information to make informed investment decisions. FSI is also supportive of increasing pricing transparency in the secondary municipal securities market. However, FSI is concerned that the Proposed Rule may not strike an appropriate balance between potential benefits to investors and potential costs such as operational difficulties, detrimental market impacts, and increased customer confusion. FSI requests that MSRB consider several suggested alternatives in light of these concerns.

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[1] 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) *available at*, http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-20.ashx?n=1.

[2] 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.

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

FSI appreciates the opportunity to comment on the Proposed Rule. We support efforts to increase price transparency and investor education. However, we have several concerns with the proposed approach to achieve these goals. The Proposed Rule presents significant operational difficulties, creates the potential for unintended consequences, and risks confusing investors. As such, FSI proposes several alternatives that achieve a balance between costs and benefits, leverage existing investor education resources, and ensure customers receive access to increased information concerning the execution of their municipal securities transactions. These concerns and potential alternatives are discussed in greater detail below.

I. Unintended Consequences

A. Imprudent Investment Decisions

FSI believes that it is important to consider a variety of factors in evaluating the execution quality of a municipal securities transaction. Placing a disproportionate emphasis on price may not best serve investors. Customer transactions are currently subject to suitability,[3] fair pricing[4] and best execution requirements.[5] Each of these rules serves a vital investor protection purpose and together ensure that customers receive fair prices for investments that are appropriate to their financial condition and investment needs. As such, it is unclear why pricing disclosure on a confirmation is necessary to protect investors. If each of these three requirements has been satisfactorily met in the opinion of regulators, it is unclear to FSI why there should be an implication that customers are being excessively charged for municipal securities transactions. Furthermore, if MSRB has evidence of excessive mark-ups, the execution quality mandates should provide adequate authority to address these situations.

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[3] See MSRB Rule G-19.
[4] See MSRB Rule G-30.
[5] See MSRB Rule G-18 (effective as of Dec. 7, 2015).

Furthermore, FSI cautions that instructing investors to use this additional disclosure to search for the financial firm that offers the lowest mark-ups is misguided and potentially not in investors' best interests. 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. Additionally, customers should receive education that ensures they are making investment decisions consistent with their needs and objectives. While pricing may be a factor that aids such an analysis it is certainly not the only one and, perhaps, not the most important one. Rather, it is important to encourage investors to seek out the financial advisor that best understands their investment needs and has the requisite expertise. Encouraging investors to seek out the broker-dealer offering the lowest price may not be consistent with investor protection goals.

B. Flight to Packaged Products

The additional disclosures imposed by the Proposed Rule may have the unintended consequence of limiting investor access to municipal securities products. As a result of the increased compliance burden imposed by the Proposed Rule firms may steer investors interested in a fixed return toward packaged products, to the detriment of investors. Individual municipal securities offer greater transparency concerning the anticipated return as compared to packaged products. Furthermore, in a rising interest rate environment an investment with a stated maturity may be a more appropriate investment for customers. FSI suggests MSRB consider amending the Proposed Rule to create a proposal that is neutral in the face of changing economic conditions.

C. Negative Impact on Liquidity

The Proposed Rule may also have a detrimental impact on liquidity in the secondary municipal securities markets. Mandating additional disclosures might disincentivize participants from engaging in retail-size transactions.[6] This potentiality is all the more significant in light of the negative impact that enhanced capital rules and other regulatory requirements have had on bond market liquidity.[7] A further erosion of liquidity in the bond markets may significantly inhibit FSI members' ability to adequately service their customers. The secondary debt markets are innately opaque. Oftentimes, trading for a particular municipal issuance could require significant time and effort on the part of the broker-dealer as there is a vast amount of bespoke municipal issuances outstanding. Ensuring the existence of as many market participants as possible is critical to aiding broker-dealers in their efforts to facilitate transactions in illiquid securities for their customers. Furthermore, there are currently other regulatory requirements that can be used to ensure that the actions of a firm in municipal securities trading for customers are fair and reasonable. As such, FSI does not believe that the benefits of the Proposed Rule are outweighed by these potential negative market impacts.

D. Eroding Yield

FSI also suggests MSRB consider the potential that securities industry participants may convert customer brokerage accounts to fee-based advisory accounts, to avoid the Proposed Rules'

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[6] Proposed MSRB Rule G-15(a)(i)(F) defines a retail size transaction as "100 bonds or fewer or bonds in a par amount of $100,000 or less." *See* Regulatory Notice 2014-20, *supra* note 1.

[7] Tom Braithwaite and Vivianne Rodrigues, *Banks Blame Bond Volatility on Tighter Regulation*, Financial Times (Oct. 16, 2014), *available at* http://www.ft.com/cms/s/0/1a456bc6-54d9-11e4-bac2-00144feab7de.html#axzz3NxcBFf5Y.

disclosure obligations. These unintended activities may harm the integrity of the secondary municipal securities markets and harm investors. Advisory accounts would avoid the additional disclosure requirements consistent with prior SEC No-Action Letters. While the advisors would maintain a fiduciary duty to the customers, maintaining debt securities, particularly those with low yields, in an advisory account will inappropriately erode that already small yield. FSI requests MSRB consider this potentiality and act accordingly to ensure that investors do not suffer the consequences of eroding yield.

II. Customer Confusion

A. Purpose and Use of Confirmation

Prior to pursuing the Proposed Rule, FSI suggests that MSRB poll investors to understand how, and to what extent, they use trade confirmations. The SEC has previously stated that customer confirmations serve "basic investor protection functions by conveying information allowing investors to verify the terms of their transactions; alerting investors to potential conflicts of interest with their broker-dealers; and providing investors the means to evaluate the costs of their transactions and the quality of their broker-dealer's execution."[8] The SEC further acknowledged that a firm may use a confirmation as a customer invoice while it finances positions when payment is received after settlement date. Additionally, confirmations may simply serve as "written evidence of a contract between the customer and broker-dealer," consistent with Uniform Commercial Code requirements. FSI believes it is worthwhile for MSRB to understand whether investors and firms use confirmations consistent with the SEC's stated intent for their issuance.

It is important for MSRB to ensure that any effort to increase pricing transparency and investor education is undertaken in a manner that will in fact achieve these goals. Online and mobile access to account holdings and transaction information is an important and widely used tool where investors may review all of the information that is included on a confirmation. Additionally the information is available to investors sooner than a confirmation is delivered. In light of these new and innovative ways for investors to interact with their brokerage accounts, FSI suggests MSRB evaluate the impact of further technological development on the purpose and use of customer confirmations.

B. Solicitation of Feedback from Investor Focus Groups

FSI also suggests that MSRB consider the potential for customer confusion and the desire for increased information at the time of trade. Currently, customers receive a significant amount of information and disclosures from their financial advisors. As specifically concerns municipal securities transactions, customers receive a large amount of information pursuant to the Rule G-47 requirement to provide all material information on the security at or before the time of trade.[9] Confirmations already contain a significant amount of information, some transaction-specific and some generic disclosures. Supplying a customer with a document containing too much information may cause the customer, already the recipient of multiple documents, disclosures and prospectuses to ignore the additional pricing information included on a confirmation. Furthermore, supplying additional pricing information without any explanation of methodology behind such pricing may create additional customer confusion.

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[8] Confirmation of Transactions, SEC Release 34-34962, 59 Fed. Reg. 59612, 59613 (Nov. 17, 1994).
[9] MSRB Rule G-47.

In an effort to ensure that industry and regulatory resources are channeled efficiently FSI suggests MSRB commission investor surveys and focus groups to learn from investors exactly what information they are interested in and the particular method in which they would like to receive it. While FSI members agree with MSRB's intention to further educate investors on the nuances of municipal securities markets, we ask that MSRB first ensure that its Proposed Rule is in fact desired by investors. FSI stands willing to work with MSRB to increase investor understanding of market operations and functions in a way that will capture investors' attention. The significant operational and system implications associated with adding this pricing information to a confirmation suggests that it would be appropriate for MSRB to evaluate whether the Proposed Rule is truly in line with investor desires.

III. Operational Implications

A. System Modifications

The additional disclosures mandated by the Proposed Rule will require substantial modifications and upgrades to current trading and back-office systems. Many FSI member firms are fully-disclosed introducing brokers that execute their customer transactions through their clearing firm or through other executing brokers. Alternatively, FSI members may execute their customers' transactions while relying on a clearing firm for clearing and custodial services, including sending confirmations. In either case, all of these firms will be required to work with their clearing firms and other third-party providers to modify their interfaces to ensure that not only the customer trade but also the appropriate reference transaction is captured and transmitted to the clearing firm. Additionally, FSI member firms will be required to work with these providers to create oversight mechanisms to ensure that the correct information is included on the confirmations. In the event a mistake is printed and sent to a customer, FSI members will be required to work with these providers to amend and resend the confirmation.[10]

These enhancements necessitate the establishment of additional processes that are both automated and manual in nature. Particularly for smaller firms without the requisite resources to build and maintain fully automated systems, the Proposed Rule will require the creation of multiple additional manual processes. The manual nature of these additions presents a high level of operational risk such that these smaller firms may no longer be able to offer fixed income products to their customers. Firms will be required to hire additional personnel to track and log both customer and same-day reference transactions, input and transmit each pair of transactions along with the price differential to the clearing firm for inclusion on the confirmation and review customer confirmations to validate the accuracy of the information provided to the customer. These additional processes create multiple opportunities for errors that will result in increased costs for firms to correct, inaccurate information provided to customers and increased customer confusion following the receipt of multiple confirmations for a particular transaction.

FSI requests that MSRB strongly consider the impacts of these necessary system enhancements in evaluating the costs and benefits of the Proposed Rule. The Securities and Exchange Commission has previously acknowledged the importance of considering these practical implications in evaluating the merits of additional confirmation disclosure:

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[10] FSI also requests MSRB detail whether there will be a penalty imposed on firms that send amended confirmations due to an error in the original confirmation. There is a high potential for errors due to the manual nature of new systems. FSI does not believe firms should be penalized when there were good faith efforts to comply with a rule.

> "In amending Rule 10b-10, the Commission must balance the increased cost to broker-dealers, and ultimately to investors, of compliance against the benefits that added disclosures would provide investors. In some instances, the Commission has declined to adopt proposed amendments to its confirmation requirements because they were considered too costly, or would have been too difficult to apply on a uniform basis."[11]

FSI requests that MSRB undertake a similar analysis of the impact of the Proposed Rule and determine if the benefits outweigh these increased costs.

B. Implementation Period

Should MSRB proceed with the Proposed Rule, FSI suggests that it provide a minimum of a 12 month implementation period in light of the significant technological and operational enhancements the proposal demands. Broker-dealers are currently engaged in many significant technological initiatives. These include the Consolidated Audit Trail and potentially the Comprehensive Automated Risk Data System. The same personnel that are necessary to build systems to comply with these regulatory mandates will also be responsible for system enhancements to comply with additional pricing disclosures. Each of these initiatives is labor intensive. Some FSI members worked with their providers to estimate that the Proposed Rule could require a minimum of five thousand hours to build the necessary system enhancements. In an effort to provide the industry with adequate time to comply with the Proposed Rule and the bevy of additional technological initiatives currently underway, FSI requests MSRB adopt a 12 month implementation period.

IV. Alternative Disclosure Options

A. Leveraging EMMA

FSI suggests MSRB undertake an analysis of potential enhancements to promotion efforts to retail investors regarding EMMA and the pricing information it offers. Currently, investors may view pricing information including last trade price, execution time, execution quantity, and the nature of the transaction on EMMA. As such, EMMA provides a significant amount of the information that would be provided to customers pursuant to the Proposed Rule. In light of the amount of time and resources expended to build and continually develop EMMA, FSI asks MSRB to consider initiatives to greater publicize to investors how they can use EMMA to find relevant pricing information.

EMMA represents an easily accessible, important market data tool. To further facilitate customer use of EMMA, FSI suggests FINRA seek public comment on a proposal to mandate the inclusion of a statement on the confirmation directing customers to the EMMA website to view pricing information. For electronically delivered confirmations, the statement could also include a hyperlink to the EMMA website. Alternatively, we recommend that MSRB consider exploring additional options that would require broker-dealers to direct investors to EMMA to view pricing information. In concert, these small additions should significantly raise the profile of EMMA such that retail investors would consult EMMA data more frequently. Hopefully, investors will eventually consult this data prior to executing a transaction. Consulting pricing data at the time they are making their investment decisions will better serve customers than after-the-fact disclosure.

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[11] SEC Release 34-33743, 59 Fed. Reg. 12767, 12772 (Mar. 17, 1994).

B. Broker-Dealer Websites

A second potential alternative would be to require pricing disclosure on broker-dealer websites. The disclosures would be made directly to a customer that is logged in and viewing their personal account holding. Alternatively, MSRB could mandate broker-dealers provide a link to EMMA so customers can access information on their holdings. FSI suggests MSRB explore opportunities to provide increased pricing information to customers on firm websites. Investors are increasingly accessing account information through online and mobile means. FSI believes that it is vitally important for MSRB to consider this behavior in selecting the best method for providing increased disclosures. Password protected customer pages on broker-dealer websites may be the best place to provide disclosures and educate customers on pricing information.

C. Municipal Securities Market Education

FSI also suggests MSRB consider requirements to increase customer knowledge of the operations of the secondary municipal securities markets. FSI believes that regardless of whether customers receive specific pricing information it is important for them to understand how prices for municipal securities are determined. It is not clear that investors currently appreciate the degree of opacity present in the municipal securities market. Educating investors on the roles that broker-dealers play in executing municipal securities transactions and the steps that must be undertaken to fairly and reasonably fill a customer order are as essential as pricing information.

These educational materials could be required to be delivered to an investor prior to the first execution of a municipal securities transaction with that particular financial advisor. Additionally, the disclosure materials could be included on broker-dealer websites so customers can continue to access them. Furthermore, FSI suggests that MSRB pursue additional customer education on the operations of secondary municipal securities markets, such as mandating a generic disclosure on confirmations directing customers to consult the disclosure documents available on the broker-dealer's website.

Alternatively, MSRB could require firms to disclose on confirmations the potential existence of a mark-up/mark-down and a point of contact at the firm a client could contact with questions about fixed income pricing. Such a disclosure could read: "On principal fixed income transactions, there may a mark-up/mark-down built into the purchase/sale price. Please contact [Insert Name and Contact Information Here] if you would like additional information about pricing." This disclosure would educate investors about the basics of fixed income pricing, would be relatively easy to understand, and would not present firms with significant operational challenges.[12] Should a customer desire to better understand municipal security pricing, this disclosure would direct them to a point of contact that could provide the customer with more detailed information about the firm's pricing schedule and municipal security market structure generally.

[12] A disclosure of this sort would be consistent with disclosure requirements for payment for order flow pursuant to Rule 10b-10(a)(2)(i)(C).

D. Centralized Marketplace

FSI also suggests that MSRB commit to exploring ways to establish a centralized marketplace for municipal securities. True pricing transparency will only be established once the structures of the fixed income markets are altered. Market participants and regulators have recently addressed the possibility of facilitating increased electronic and on-exchange trading of fixed income securities.[13] These proposals recognize the significant difficulties posed by the inherent nuances of fixed income markets. This is especially true of municipal securities, which rarely trade after initial issuance.[14] However, the proposals represent first steps in addressing a systemically important issue. Centralized marketplaces would reduce transaction costs, increase transparency and efficiency, and facilitate greater investor protection. FSI believes MSRB should engage the industry, the public and other regulatory authorities in developing a proposal to develop a centralized marketplace and introduce true price transparency. Centralized marketplaces are all the more important if market makers and broker-dealers decrease the extent of their involvement in fixed income markets. Investors may suffer unintended consequences that will result in higher transaction costs and increased inefficiency.

Conclusion

We are committed to constructive engagement in the regulatory process and welcome the opportunity to work with MSRB on this and other important regulatory efforts

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

Respectfully submitted,

David T. Bellaire, Esq.
Executive Vice President & General Counsel

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[13] See e.g. Remarks of Commissioner Daniel Gallagher, Sept. 16, 2014, *available at* http://www.sec.gov/News/Speech/Detail/Speech/1370542966151#.VKRQrivF_ws; BlackRock, *Corporate Bond Market Structure: The Time for Reform is Now* (Sept. 2014), available at http://www.blackrock.com/corporate/en-ae/literature/whitepaper/viewpoint-corporate-bond-market-structure-september-2014.pdf.

[14] See e.g. Sec. & Exch. Comm'n, *Report on the Municipal Securities Market* (July 31, 2012), p. 113, available at http://www.sec.gov/news/studies/2012/munireport073112.pdf.

Submitted electronically

January 20, 2015

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

Re: **MSRB Regulatory Notice 2014-20, Request for Comment on Draft MSRB Rule G-15 Amendments, on Same-Day Pricing Information for Municipal Securities Transactions**

Dear Mr. Smith:

The Financial Services Roundtable[1] ("FSR") appreciates the opportunity to comment on the Municipal Securities Rulemaking Board's ("MSRB") proposed amendments to MSRB Rule G-15 ("Proposed Amendments"), as set forth in Regulatory Notice 2014-20 ("Regulatory Notice"), which would require disclosure on retail customer confirmations of pricing information for same-day transactions in municipal securities. The confirmation disclosure requirement would apply whenever a municipal securities dealer executes transactions in municipal securities as principal and also effects one or more transactions with a customer in the same security on the same day, provided that the transactions are "retail-size."[2]

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[1] *As advocates for a strong financial future*™, the Financial Services Roundtable represents the largest integrated financial services companies providing banking, insurance, payment, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. FSR member companies provide fuel for America's economic engine, accounting directly for $ 92.7 trillion in managed assets, $1.2 trillion in revenue, and 2.3 million jobs. Learn more at FSRoundtable.org.

[2] *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, at 9 [hereinafter "Regulatory Notice 2014-20"].

The stated purpose of the Proposed Amendments is to increase transparency by providing customers with "meaningful and useful information" about the price differential between what a municipal securities dealer pays for a security and what it charges the customer for that same security.[3] Specifically, it responds to concerns raised in 2012 by the Securities and Exchange Commission ("SEC") regarding firms' mark-ups and mark-downs on securities.[4] We note that the Financial Industry Regulatory Authority ("FINRA") is proposing similar amendments to its Rule 2232,[5] and that the MSRB and FINRA are coordinating their respective rulemaking initiatives. Given the nature of the proposed amendments to confirmation disclosures, FSR believes regulatory coordination is essential, and we commend the MSRB and FINRA for these efforts.

FSR's members greatly appreciate efforts to create meaningful transparency in the municipal securities markets; however, they do not believe that the Proposed Amendments are likely to achieve that objective. Rather, the Proposed Amendments would provide retail customers with information that is at best confusing and at worst misleading. In the process, the Proposed Amendments would impose significant and unwarranted costs on municipal securities dealers, which would be required to reprogram their confirmation and trading systems, redesign their confirmation forms to squeeze the proposed new disclosure onto trade confirmation forms that lack—as a practical matter—sufficient space to incorporate the proposed disclosure, and undertake costly accounting measures. Many of the costs might be passed along to retail customers, who would face higher fees without any real corresponding benefit. As a result, FSR urges the MSRB to abandon the Proposed Amendments.

I. Executive Summary

FSR urges the MSRB to abandon the Proposed Amendments for the following reasons:

- Implementation of the Proposed Amendments would not provide retail customers with meaningful and useful information about transaction costs for municipal securities.
- The Proposed Amendments would impose an unworkable burden on firms to sort through thousands of transactions in real-time to capture, analyze, and report information that, in many cases, would provide retail customers with an inaccurate picture concerning execution costs for municipal securities.
- There is a significant risk that the proposed disclosure, absent extensive disclosure, would mislead retail customers about their municipal securities dealers' mark-ups or mark-downs on their specific municipal securities trades, because the proposed disclosure would not reflect a complete and accurate picture of all of the factors (including market events) that go into the price paid or received by the retail customer.

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3 *Id.* at 13.

4 *Id*. at 4.

5 *See* FINRA Regulatory Notice 14-52, Pricing Disclosure in the Fixed Income Markets.

- FSR urges the SEC, the MSRB, and FINRA to work with the industry and consumer advocates to develop effective educational tools for retail customers that would be designed to increase the retail customers' understanding of the way that municipal securities transactions are effected.
- Reprogramming customer confirmation forms to implement the disclosures required by the Proposed Amendments would entail substantial costs for municipal securities dealers that may ultimately be passed along to retail customers, thereby increasing retail customers' fees without any corresponding increase in meaningful disclosure to retail customers.
- The Proposed Amendments are overly inclusive and would apply regardless of whether the firm makes or loses money on transactions it executes as principal and even if the principal and retail customer transactions are executed at exactly the same price.
- Although FSR believes the MSRB should abandon its Proposed Amendments, if the MSRB and FINRA proceed to implement these or similar initiative, FSR urges the MSRB and FINRA to coordinate their efforts to ensure the uniformity and consistency of the rules (and their interpretative guidance) in order to minimize disruption.

II. Introduction

FSR's members have a number of concerns relating to the feasibility of capturing the information that would be required to be disclosed under the Proposed Amendments, the usefulness of such information to customers, the overinclusiveness of the Proposed Amendments, and the costs that would be imposed on firms without any corresponding benefits for retail customers.

i. Difficulty capturing the information. It is not uncommon for firms to engage in multiple principal transactions and multiple customer transactions in the same municipal security on the same day. The Proposed Amendments themselves do not provide any guidance or standardization that would take into account these realities. Rather, they merely suggest as possibilities "disclosing the trade that is closest in time proximity to the customer trade; disclosing the last principal trade that preceded the customer trade (a last in, first out (LIFO) methodology); or disclosing the weighted average price of multiple trades."[6] Capturing this information in real time is impractical and overly burdensome.

ii. Confusion. Because of the difficulty in capturing the relevant information, there is a high likelihood that the reference prices that would be disclosed would be inaccurate or misleading. Even setting aside the difficulty of capturing the appropriate reference prices, there is also a significant risk that retail customers would conflate price differentials with mark-ups and mark-downs. For instance,

[6] Regulatory Notice 2014-20 at 11.

if the principal transaction occurs at the beginning of the trading day and the customer transaction occurs at the end of the day, any number of unrelated market events could be responsible for the price differential. However, the Proposed Amendments do not provide retail customers with any basis for evaluating that possibility. Finally, the Proposed Amendments would require the disclosure of the reference pricing information too late in time for it to be useful and would not provide any basis for retail customers to evaluate or contextualize the information.

iii. Cost. As the MSRB is aware, reprogramming customer confirmation systems and redesigning the confirmations themselves is a time-consuming and expensive process. This large financial burden is not offset by any meaningful benefit to retail customers in light of the likelihood of retail customer confusion that would result from the somewhat *ad hoc* disclosure requirements.

iv. Overinclusiveness. The Proposed Amendments would apply regardless of whether the firm makes or loses money on retail customer transactions it executes as principal; they would even apply if the principal and retail customer transactions were executed at exactly the same price. Moreover, they would apply whether the principal and customer transactions are seconds or hours apart and without regard to whether they are "riskless." Such overbreadth imposes unnecessary costs.

v. Uniformity. If the MSRB and FINRA ultimately adopt the respective proposals, we urge the MSRB and FINRA to ensure the uniformity and consistency of the rules (and their interpretative guidance) in order to minimize disruption.

II. Difficulty Capturing the Information

The Proposed Amendments would impose an unworkable burden on firms to sort through thousands of transactions in real time to capture, analyze, and report information that, in many cases, would provide retail customers with an inaccurate picture concerning execution costs for municipal securities. The premise of the Proposed Amendments is that there should be a way for retail customers to determine the difference between what they paid for municipal securities and what their municipal securities dealer paid for those same securities.

The Proposed Amendments might make sense in a market where the standard practice worked along the following lines: Firm buys X ABC bonds from a dealer and immediately sells X ABC bonds to a customer; Firm then buys Y DCE bonds from a dealer and immediately sells Y DCE bonds to a customer; and so on. However, the realities of the markets are far more complicated. Firms do not build and sell positions in municipal securities on a paired transaction basis. There is simply no meaningful way for a firm to match in an efficient and price-effective manner the securities sold to customers with particular securities that it has in its inventory or to match securities purchased from customers with securities that it sells in principal transactions.

The Proposed Amendments are silent about the calculation methods that firms should use in order to ensure compliance. Although the Regulatory Notice suggests as possibilities a patchwork of weighted averages, LIFO accounting, and other approximations, these methods, apart from being confusing and costly to implement, only begin to capture the potential permutations that can exist in a market involving multiple customers and multiple transactions. For example, what would happen in a scenario where a municipal securities dealer purchases bonds from multiple dealers at the same time at different prices, and sells bonds to multiple customers at the same price at the same time. While municipal securities dealers could perhaps extrapolate from the suggested methodologies for deriving a reference price to include on a customer's confirmation, the information provided would be somewhat of an arbitrary estimate and could mislead investors as to how their municipal securities dealers actually trade and derive the price to their customers.

Additionally, capturing the information and incorporating it into the confirmation process would make it difficult for municipal securities dealers to deliver confirmations in a timely manner. For example, municipal securities dealers will need processes for identifying the relevant principal transaction or transactions for each retail municipal securities trade in accordance with the MSRB's methodology, tagging each principal trade to prevent duplicative matches, calculating the price differential, and submitting the data to their confirmation systems (which in many cases are third-party service providers) for inclusion on each retail customer's written trade confirmation. FSR believes that this process will take hundreds of hours and be impossible to complete in order to deliver confirmations to retail customers prior to trade settlement. Even if the MSRB continues to believe that reference pricing information should be available to retail customers, FSR submits that requiring this disclosure on trade confirmations is not the appropriate vehicle.[7]

III. Confusion

The objectives of the Proposed Amendments are only served if investors receive useful information. However, the Proposed Amendments are not reasonably calculated to achieve that goal. Indeed, there is a significant risk that the information provided to retail customers would mislead them about their municipal securities dealers' mark-ups or mark-downs on their specific transactions because it would not—and could not in a timely and cost-effective way—provide a complete and accurate picture of all of the factors, including market events, that go into the price paid or received by a retail customer.

For instance, other factors, including market events, might be responsible for price differentials. Nonetheless, the Regulatory Notice characterizes the Proposed Amendments as disclosure regarding mark-ups and mark-downs, which could mislead retail customers into thinking that a particular municipal securities dealer's mark-up or mark-down is the primary factor in determining a customer's transaction price for a specific municipal security. For instance, mark-ups and mark-downs will be shown in a vacuum without reference to whether it

[7] Some possible alternatives are discussed in Part III of this letter.

took the municipal securities dealer five seconds or five hours to execute the trade. Nor will the Proposed Amendments facilitate accurate comparisons of transaction costs for municipal securities across firms.

A more useful alternative would be for the SEC, the MSRB, FINRA, the industry, and consumer advocates to develop effective educational tools for retail customers that would be designed to increase retail customers' understanding of the way that municipal securities transactions are effected. This could include efforts to increase retail customers' awareness of tools that already exist to determine much of the information that would be disclosed under the Proposed Amendments. For instance, the Regulatory Notice observes that under the status quo, "[w]ith the use of information disseminated through these [free online] platforms, investors can make a more informed evaluation of the price paid or received for their municipal securities."[8] Indeed, the promise of such publicly available information was the very reason the SEC decided not to move forward with proposals to increase confirmation disclosure requirements for municipal and other fixed income securities the last time it considered the issue, which was in 1994.[9] Since then, EMMA (along with FINRA's tool TRACE) has made dramatic strides in increasing transparency. To the extent that the MSRB is concerned that not enough retail customers are aware of these resources, this can be solved through increased education. To the extent that the concern is that more information should be available online, that can be corrected as well without requiring municipal securities dealers to undertake the burdensome process of updating confirmation disclosures in the way that would be required under the Proposed Amendments.

Municipal securities dealers could supplement these efforts by providing a toll-free telephone number that their retail customers can use to obtain information about how their municipal securities dealer handles municipal securities trades generally, including the mark-up or mark-down charged on any particular transaction. Alternatively, if the MSRB believes that it is necessary for additional information to appear on confirmations, it could require firms to disclose the maximum mark-up/mark-down percentage that the firm permits and direct customers to the toll-free number if they have any additional questions.

IV. Cost

FSR estimates that the cost of implementing the Proposed Amendments would be significant. The most significant cost would be reprogramming confirmation forms. As the MSRB is aware, this is a time-consuming and expensive process. For instance, as part of a 2010 proposal to change mutual fund disclosures, the SEC estimated that the changes to the confirmation forms alone would take in excess of a million hours and would cost upwards of

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[8] Regulatory Notice 2014-20 at 6.

[9] *See* Confirmation of Transactions, Securities Exchange Act Rel. No. 34962, 1994 SEC LEXIS 3503, at *4-5 (Nov. 10, 1994) (basing decision to defer consideration of proposals based on MSRB's commitment to develop "significant new ways of making pricing information more widely available to investors").

$250 million.[10] These are substantial costs that may ultimately be passed along to retail customers, thereby increasing their fees without providing meaningful disclosure. The alternatives proposed here would be far less costly, but would still achieve the goal of making more information about municipal securities available to retail investors.

V. Overinclusiveness

The Proposed Amendments are overly inclusive in a number of ways. For instance, they would apply regardless of whether the firm makes or loses money on transactions it executes as principal; they would even apply if the principal and retail customer transactions are executed at exactly the same price. This approach subjects firms to the burdens of the Proposed Amendments without any analysis of whether the information disclosed is likely to be of any utility to the customer.

The SEC's 2012 report only recommended disclosure for "riskless principal" trades.[11] However, the Proposed Amendments go beyond that recommendation and encompass all trades that occur within the same day. Even if the MSRB ultimately requires greater confirmation disclosure, such an expansive approach is not necessary.

VI. Uniformity

If the MSRB and FINRA ultimately move forward with their respective proposals, FSR urges the MSRB and FINRA to ensure the uniformity and consistency of the rules (and their interpretative guidance) in order to minimize disruption.

For instance, both regulators should use the same terminology to refer to third-party transactions. Currently, the MSRB uses the term "reference transactions." It would be helpful for FINRA to adopt the same term, or for both regulators to agree on some alternative that would be the same for both of them.

More importantly, the regulators should work together to ensure that the standards are the same for when disclosure is required and that the methodologies and accounting methods are standard and consistent. A failure to ensure uniformity would impose even greater costs on firms by requiring them to reprogram their confirmations according to two separate protocols.

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[10] *See* Mutual Fund Distribution Fees; Confirmations, 75 Fed. Reg. 47064, 47126 (Aug. 4, 2010).

[11] *See* Regulatory Notice 2014-20 at 4.

FSR appreciates the opportunity to comment on the MSRB's Proposed Amendments. If it would be helpful to discuss FSR's specific comments or general views on this issue, please contact Richard Foster at Richard.Foster@FSRoundtable.org or Felicia Smith at Felicia.Smith@FSRoundtable.org.

Sincerely yours,

Vice President and Senior Counsel for
Regulatory and Legal Affairs
Financial Services Roundtable

With a copy to:

Municipal Securities Rulemaking Board
Michael L. Post, Deputy General Counsel
Saliha Olgun, Counsel

Financial Industry Regulatory Authority
Robert L.D. Colby, Chief Legal Officer
Patrick Geraghty, Vice President, Market Regulation
Cynthia Friedlander, Director, Fixed Income Regulation, Regulatory Operations
Andrew Madar, Associate General Counsel

Comment on Notice 2014-20

from Gerald Heilpern,

on Tuesday, December 9, 2014

Comment:

Questions/thoughts re the new disclosure rule:

If this is adopted the customer might think that he/she is better off. Unfortunately the opposite is true. Right now firms can search the whole country for the best bond to satisfy the clients need and then mark it up one or two points for their efforts. Obviously, if this markup is shown the client is not going to be happy. Under the new procedure there will three classes of brokers:
1. Small firms that do not carry inventory. - these firms will be out of the bond business and all the diversity that they provide will be lost.
2. Small firms that carry inventory – these firms will ONLY show bonds in their inventory. This will result in a very narrow choice for their customers.
3. Large firms that carry inventory – these firms will benefit greatly from the change. The customer will have a larger choice than the small firm can provide but no matter how large the firm is, it will never equal the choices now available by any firm being able to check for the best bond and the best price.

Capitalism is based on competition. By eliminating whole classes of competitors the customers will suffer as to choice and price. Right now I am the manager of a small firm the does not keep inventory. I have spent 38 of my 46 year career at small firms. I and my RR's have NEVER lost out to a large form on an order based on competing with large firm's inventory, We offer the inventory of every trading firm in the country and by careful shopping and using judicial mark ups we are always competitive. The only winners under the proposed plan will be the large firms.

One additional thought. There is a sense among regulators that profits on individual trades is basically unfair. Instead of commissions/mark ups there is pressure to create managed accounts using an annual fee of 1% or more on the value of the account. Under past practices the client who buys 100m bonds might incur a markup of one to two thousand dollars. Under managed accounts, the customer would pay one thousand dollars PER YEAR for as long as the position is kept. I can't see how this benefits the customer.

Sincerely yours,

Gerald Heilpern 845-357-5044

Comment on Notice 2014-20

from Gerald Heilpern,

on Thursday, December 18, 2014

Comment:

on 12/9 I submitted some thoughts. This is an addition.

If the disclosure rule is not set in stone, I think that the whole subject should be re-evaluated. I previously submitted comments on 12/9. I would also like to add one more item. Right now there are firms that seem to fit your end desires perfectly. The discount houses generally charge $ 2.50 per bond and the cust. gets to choose from a national inventory. Unfortunately the inventory in presented on an electronic bulletin board. The average retail client is not equipped to ascertain all the facts about the bond, even if it disclosed on page 2 or 3. How many will know what an extra ordinary redemption is? when a client sees a rating is he/she aware of problems in nearby communities? Will he/she know the difference between an unlimited GO and a limited GO. To cover themselves these houses have lengthy hedge clauses in their new account docs. This protects them but not the client. This is akin to having patients self- prescribing medicines using an on line PDR. Every regular brokerage must have Muni Bond Principals and Government Bond Principals on staff. This is more important than price disclosure

Comment on Notice 2014-20

from Gerald Heilpern,

on Thursday, January 8, 2015

Comment:

This is my third comment on this issue. I feel that opposing the rule (as I have in my 2 previous emails) is not enough. As a substitute, I would like to recommend the following: A hard and fast markup/down rule of one percent. This would allow small firms to remain in the business without creating bad feelings as the disclosure rule would effect. Also, all prospectus items should be exempt from any changes

HILLIARD LYONS 500 West Jefferson Street | Louisville, KY 40202
502-588-8400 | toll free 800-444-1854

January 20, 2015

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

Mr. Ronald W. Smith, Corporate Secretary
MSRB
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Response to the Requests for Comment from FINRA and the MSRB on Proposed Rules to Require Confirmation Disclosure of Pricing Information in Fixed Income Securities Transactions (Regulatory Notices 14-52 and 2014-20).

Dear Ms. Asquith and Mr. Smith:

Hilliard Lyons welcomes the opportunity to comment on the rule proposed by FINRA outlined in Regulatory Notice 14-52 and the MSRB outlined in Regulatory Notice 2014-20, proposing disclosure of price information on "Matched Trades" directly to customers on trade confirmations. We are a member firm of relatively small size, with 1,100 employees and approximately 400 registered representatives, which offers a unique perspective for commentary on the proposed changes. We feel very strongly that these proposals will unfairly burden small dealer firms with extremely costly revisions to fixed income trading and back office processing systems. Significant resources will be required to provide systems coding changes to both capture the suggested data comparisons and correctly communicate it on customer confirmations in real time.

Changes should be uniform in content and language across all firms. Although they will also face a burden implementing regulations of this nature, larger firms with greater IT resources will be in a position of tremendous advantage compared to small firms in this effort.

If you examine the impact of all the regulatory initiatives that have been implemented over the last year, clearly a proportionately greater burden has been placed on smaller/regional firms. This was not the intent of Dodd/Frank. Certainly the smaller firms did not precipitate the financial crises. The unexpected consequence of actions like the proposed rules is to stifle competition and lessen market liquidity.

Comments from several market regulators early in this process seemed to focus primarily on disclosure of markups for "riskless principal" trades. However, that appears to have morphed into any buy vs. sell trade comparisons under a certain par value that occur on the same CUSIP within a specified amount of time. Many proprietary positions of risk (long positions) have customer buy trades and additional firm purchase trades that follow within the same day that are unforeseen or anticipated at the original time of position purchase. Extremely high costs would be incurred by small firms to code back office systems for position accounting reporting, either at the time of trade or at the end of day to determine average cost.

To focus on "riskless principal" trades, none of this risk position accounting is necessary. Member firms should individually designate which "Matched Trades" represent actual "riskless principal" trades. We agree with SIFMA that institutional trades of any size should be exempt from the process. Retail purchases from the street with a customer order in hand would qualify, retail sells to the street with a customer order in hand would qualify, and crosses between retail customers with both sides executed together (within seconds or minutes) would qualify. None of the proprietary position examples would qualify, regardless of the trade time frame. Allow each firm to make those designations under specific regulatory guidelines, eliminating the need for computer search programs for reference trades.

We anticipate that you will shortly receive technical/operational analysis of the proposal that shows the extraordinary difficulty, in terms of time and cost, of implementing the proposals as currently drafted.

There is an alternative.

The MSRB EMMA website continues to provide the municipal market with increased transparency and has a growing audience with both member firm traders, underwriters, public finance personnel and sales people and, most importantly, municipal investors. Continued periodic enhancements could provide investors with even more detailed trade information on individual CUSIP numbers than we are discussing with the "Matched Trade" proposals. We have several suggestions as to how that information could be presented on EMMA to enhance the present disclosures:

- Color code individual trades from each dealer participating in a market for a specific CUSIP. That would greatly aid the investor in seeing how many different firms might be transacting in the market on one CUSIP. The customer could easily identify personal trades as well as any offsetting matched trades by that same dealer. At the same time, the customer could see other dealers' prices distinguished by different colors to determine if others might be offering a more favorable price. The color coding could revert to standard black type after seven days (or another time frame) to evidence older trade data.
- If member firms are required to designate "Matched Trades", a special type (italics) could be used on those two trades for instant recognition by the viewer.
- Offer a more interactive Price Discovery tool on the Trade Activity page to make it easier to compare trades on similar actively traded securities. Logic could be created to have direct links underneath the Price Discovery icon to Activity pages for specific comparable securities that meet at least 3 criteria: state, maturity, rating (either service), coupon, call features, or credit enhancement.

We feel the MSRB EMMA website is just scratching the surface of possible price/yield comparison disclosures. An informational disclosure could be required for all municipal product confirmations referencing the MSRB EMMA website address. Member firms should provide additional education information about the EMMA features on both their internal and external websites. That information could be standard language developed by an industry panel or left to each firm individually. The marketplace should leverage this useful technology instead of requiring member firms to implement very costly trade detail disclosures on each customer confirmation.

Anecdotally, we are aware of a substantial increase in the use of EMMA by our retail clients. Our guess is that this level of usage is growing exponentially and will continue to do so. Prior to spending extraordinary amounts of money and time to develop a system that may not achieve your intended goals, it makes much more sense to study EMMA's effectiveness with retail investors and put resources into expanding its reach to those investors.

Hilliard Lyons appreciates the opportunity to provide our views on the rule proposal. We would welcome any opportunity to participate in further discussions with FINRA, MSRB, and other member firms about these proposals or other marketplace issues.

Sincerely,

Alexander I. Rorke
Senior Managing Director
Municipal Securities Group

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January 20, 2015

VIA ELECTRONIC MAIL

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

Re: **MSRB Regulatory Notice 2014-20, Pricing Reference Information on Retail Customer Confirmations**

Dear Mr. Smith:

Thank you for the opportunity to submit comments on the draft rule amendments requiring the disclosure of a "reference transaction" price on customer confirmations for retail-size principal transactions. Hutchinson, Shockey, Erley & Co. (HSE) is an investment bank and broker-dealer that specializes exclusively in municipal securities, and has done so since the firm's establishment in 1957. As such, we believe we are well-positioned to provide comments on the draft rule amendments and we are pleased to do so.

As a general principal, HSE supports increased price transparency for retail investors in the municipal securities market. Our firm transacts municipal securities business only with Sophisticated Municipal Market Professionals, however, and therefore our comments will focus specifically upon the following question for which the MSRB has sought feedback:

Is it appropriate to provide that a dealer is only obligated to disclose pricing reference information when the customer trade is likely to be a retail trade? If so, should retail be defined by reference to the trade size, as in the proposal, or by some other standard?

HSE feels strongly that any obligation to provide pricing reference information should be limited to retail trades. It would be unnecessary for broker-dealers to disclose the pricing of "reference transactions" on trade confirmations for Sophisticated Municipal Market Professionals, as SMMPs have access to the same sources of pricing information as broker-dealers do. Moreover,

SMMPs have the knowledge of how to use these information sources, and the timeliness of the SMMP's access is on par with that of the broker-dealer. Indeed, in our experience, an SMMP's decision to execute a transaction is typically based upon his awareness and understanding of contemporaneous transactions in the same or similar municipal securities.

Because the SMMP has timely access to the same sources of pricing information as the broker-dealer, and because the SMMP has the specialized knowledge and experience to understand the meaning of that pricing information, it is unnecessary for the pricing of "reference transactions" to be disclosed on trade confirmations for SMMPs. Therefore, for purposes of the draft rule amendments, "retail" should not be defined by trade size, but rather on the basis of whether or not the customer meets the definition of SMMP. The somewhat arbitrary, though oft-cited, transaction size of 100 bonds as the defining line between retail and professional is inappropriate here. Using trade size as the standard for application of the draft rule will certainly result in less-than-complete coverage of retail market participants; it will also result in the capture of a significant number of transactions with SMMPs.

By way of example: in December 2014, HSE – which, again, conducts its business exclusively with SMMPs – wrote 1,999 trade tickets in transactions involving 728,565,000 bonds. The average trade size was 365 bonds. The smallest trade size was 5 bonds; the largest was 8,080,000 bonds. **Of the 1,999 trade tickets, 959 of them represented trades of 100 or fewer bonds.** Fully 48% of our transactions in the month – all of which were executed with SMMPs – would be subject to reference pricing disclosure under the retail standard proposed in the draft rule amendments. To conform to the stated purpose of providing increased transparency to retail investors, the standard by which retail is defined in the draft rule amendments must be changed; if it is not, the result will be considerable unnecessary reporting and additional unwarranted burdens on the broker-dealer community. The MSRB already employs a standard by which retail is separated from non-retail, and that standard is the SMMP.

On behalf of Hutchinson, Shockey, Erley & Co., I thank you for your consideration of these comments.

Sincerely,

Thomas E. Dannenberg
President & CEO

cc: Marcia Asquith, Office of the Corporate Secretary, Financial Industry Regulatory Authority

Interactive Data
Pricing and Reference Data LLC

32 Crosby Drive
Bedford, MA 01730

Tel: +1 781 687 8800
Fax: +1 781 687 8005

www.interactivedata.com

January 20th, 2015

SENT VIA ELECTRONIC SUBMISSION

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 14-52 and MSRB Regulatory Notice 2014-20

Dear Mr. Smith and Ms. Asquith:

Interactive Data appreciates the opportunity to comment on the coordinated rule proposals FINRA 14-52 and MSRB 2014-20, concerning the disclosure of pricing information on retail fixed income transactions published November 17, 2014. We support the overarching goal of increased transparency for fixed income investors and the commitment of the Financial Industry Regulatory Authority (FINRA) and the Municipal Securities Rulemaking Board (MSRB) in this area. The goal of increased transparency should balance the costs to the industry with the utility of the proposed disclosures to investors, while minimizing any deleterious effects to the fixed income markets.

Interactive Data is not a broker/dealer, and therefore is not well positioned to comment on many of the questions posed in the releases, such as those concerning the mechanics of confirmation statement generation. Rather, our comments focus on our observations regarding transaction costs in fixed income markets and the usability of the proposed disclosures to retail investors. We find that while the proposals would generate additional information for retail investors, these investors would continue to lack the necessary context or insight to be able to interpret that

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information. As a result, we suggest alternative disclosures and methods of communication with retail investors be explored.

Interactive Data provides independent evaluations to over 5,000 global organizations, including banks, brokers, insurance firms, hedge funds and mutual funds. These evaluations underpin many facets of the fixed income investment lifecycle, ranging from trading, OMS and portfolio analytics platforms (such as our own BondEdge analytics solutions), to performance, risk and compliance systems, as well as portfolio accounting and NAV calculation processes. The foundation of our approach to evaluating 2.7 million instruments lies in the combination of our extensive set of market data (including FINRA's TRACE® and the MSRB Real-time Transaction Reporting System, along with additional pre-trade information sourced from both the sell side and buy side), our rich set of models, and the expert oversight provided by an Evaluated Services team of approximately 200 professionals. More recently, Interactive Data has developed Continuous Fixed Income Evaluations, producing an intraday streaming fixed income evaluation service that can assist with pre-trade price discovery and post-trade performance analysis among other applications.

Interactive Data's immersive evaluations approach makes us a keen observer of fixed income market trends, including shifting patterns in trade size and frequency. To help communicate our perspective based on these market surveillance activities, we have recently undertaken a 2010-2014 update to our previous, external transaction costs white paper from 2010. Both papers are available on the Interactive Data website[1] and will be referenced throughout this letter. Our comments in this letter derive from our role as an independent market observer and our associated understanding of the expertise that is required to assess and translate such transaction cost data.

As noted above, the recent paper "Transaction Costs in the Corporate, Municipal and Agency Bond Markets, 2010-14" updates Interactive Data's prior white paper "Corporate and Municipal Bond Trading Costs During the Financial Crisis" published in 2010. The 2014 paper examines patterns of transaction costs over time, for both paired and unpaired trades, by employing three different measurement approaches. The paper concludes that:

[1] See "Corporate and Municipal Bond Trading Costs During the Financial Crisis" by Ciampi and Zitzewitz, 2010 and "Transaction Costs in the Corporate, Municipal and Agency Bond Markets, 2010-14 by Zitzewitz, 2014. http://go.interactivedata.com/rs/idglobalcrm/images/Corporate-and-Municipal-Bond-Trading-Costs-During-the-Financial-Crisis-Aug-2010.pdf
http://go.interactivedata.com/Transaction-Costs-Jan-2015-Web-WPR.html

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- Transaction costs for the period of 2010-14 were both relatively stable[2] and generally lower than they were during the credit crisis[3].
- Small, intra-period increases in transaction costs were also noted during periods of volatility for particular asset classes, such as in late 2011 for corporate bonds.[4]
- Paired-bond activity, suggesting riskless principal transactions, was also prevalent, although transaction costs for both paired and unpaired dealer-client transactions were similar.[5] However, an examination of the distribution of transaction costs within size bands illustrates clear asymmetry with a larger 90^{th}-50^{th} percentile difference for client buys and a larger 50^{th}-10^{th} percentile difference for client sells.[6]
- Interdealer trades that are paired with client trades reflect transaction costs that are about half of those paid by clients.[7]
- Transaction costs exhibit a direct relationship with length to maturity and an inverse relationship with credit quality.
- Average transaction costs for smaller trades continue to be higher than for larger trades. However, it was noted that transaction costs for very small trades (less than $10,000) are no larger than those in the $10k-50k range.
- The 2014 paper also compares the differences in transaction costs observed when using Continuous Fixed Income Evaluations[8] (updated on a streaming basis throughout the trading day) and finds that by eliminating the 'noise' introduced by overnight bond movements, the measurement error is reduced significantly and the length of the tails decrease. In other words, transaction costs, when measured against a valuation benchmark on an intraday basis, tend to exhibit a tighter distribution[9].

[2] See figures 11 and 12 from the 2014 paper.
[3] Although the methodologies are not exactly the same, these patterns can be generally observed by comparing 2010 with 2008-9 in Tables 3A and 3B of the 2010 paper and comparing 2010 with 2011-14 in Figures 5A and 5B of the 2014 paper
[4] See page 8, and Figures 11 and 12 of the 2014 paper.
[5] See Tables 2A, 2B and 2C as well as Figures 2A, 2B and 2C of the 2014 paper.
[6] See Tables 4A-4D and Figures 4A-4D of the 2014 paper.
[7] See Tables 2A-2C of the 2014 paper.
[8] Interactive Data launched Continuous Fixed Income Evaluations in 2014. For additional information, please refer to http://www.interactivedata.com/Assets/DevIDSite/PDF/InteractiveData_Continuous-Evaluated-Pricing.pdf
[9] This reduction in distribution can be seen by comparing Figures 4A and 4D as well as Tables 4A and 4D from the 2014 paper.

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Taken together, we believe the findings outlined above highlight the compound nature of fixed income transaction cost variability. These costs tend to differ not only according to the size of the trade, but by bond characteristic (distance to maturity, credit quality, recency of issuance, relative liquidity), by market conditions (especially volatility) as well as by trading partner and execution method.

The rule changes detailed in FINRA release 14-52 and MSRB release 2014-20 generally propose that for certain retail-sized trades (mainly $100k or less), additional information concerning same-day offsetting trades be provided to the client as part of the confirmation statement. The underlying rationale is that having this information will enable the retail investor to understand the effective mark-up or mark-down realized by their broker/dealer, allowing the client to discern the reasonableness of the transaction cost and execution price. However, given the complexities of the bond market and the variability of transaction costs described above, it seems unlikely that the average retail investor (who does not trade frequently and is not expert in fixed income markets) will be able to interpret the new mark-up or mark-down information. For example, on a $50,000 transaction, an effective one point mark-up might be a very low transaction cost for the purchase of a 15 year, high-yield corporate, but the same one point mark-up would be relatively expensive for the purchase of a 5 year, high-grade municipal. It is hard to imagine, absent some form of additional market context, that a casual retail investor would have the baseline knowledge necessary to understand this transaction cost data.

We believe alternative approaches should be considered that offer meaningful context and therefore permit the retail investor to better understand the transaction cost and execution price. As proffered in both the MSRB[10] and FINRA[11] releases, we believe that third-party prices can be leveraged to better inform retail investors. In particular, an accepted, intra-day benchmark valuation for a specific security, displayed with an illustration of the likely range of expected variation in trades (factoring in size of transaction), would offer the retail client meaningful information about their trade. With these additional details, the aforementioned investor in a15 year, high-yield corporate bond would be able to observe that their execution was clearly within

[10] See page 15 of MSRB's 2014-20 release - "The MSRB could also require the inclusion of other market information (e.g., prices provided by external pricing services) on the confirmation. The MSRB seeks comments on whether any of these alternatives provide customers with more meaningful and useful information, whether that value of additional information can be quantified, and the degree to which any of these alternatives would be more or less costly to implement."

[11] See page 12 of FINRA's 14-52 release - "Rather than using the price to the firm, would the best available representation of current market price be more useful… If so, given the infrequent trading in many bonds, what would be an acceptable reference price to use to measure the current price?"

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the expected range of prices, while the investor in a 5 year, high-grade municipal bond could see that their execution fell outside of the expected range. Furthermore, it is possible that such an approach – if available as an alternative to the proposed display of offsetting trades - could be less costly for firms to implement, particularly if industry participants were to provide the information via a website link.

Further detail on information that could be made available for retail clients as part of an alternative approach is included as an appendix. These screens are not meant to specifically represent investor-ready information, but are included to help illustrate the possible direction that such an approach could take. The underlying data and delivery mechanisms necessary to deliver such clarifications exist now and could be rolled out to broker/dealers.

Interactive Data appreciates the opportunity to comment on these rule proposals and welcomes further discussion concerning the information provided.

Sincerely,

Andrew Hausman

President, Pricing & Reference Data

Interactive Data

Appendix:

Figure 1

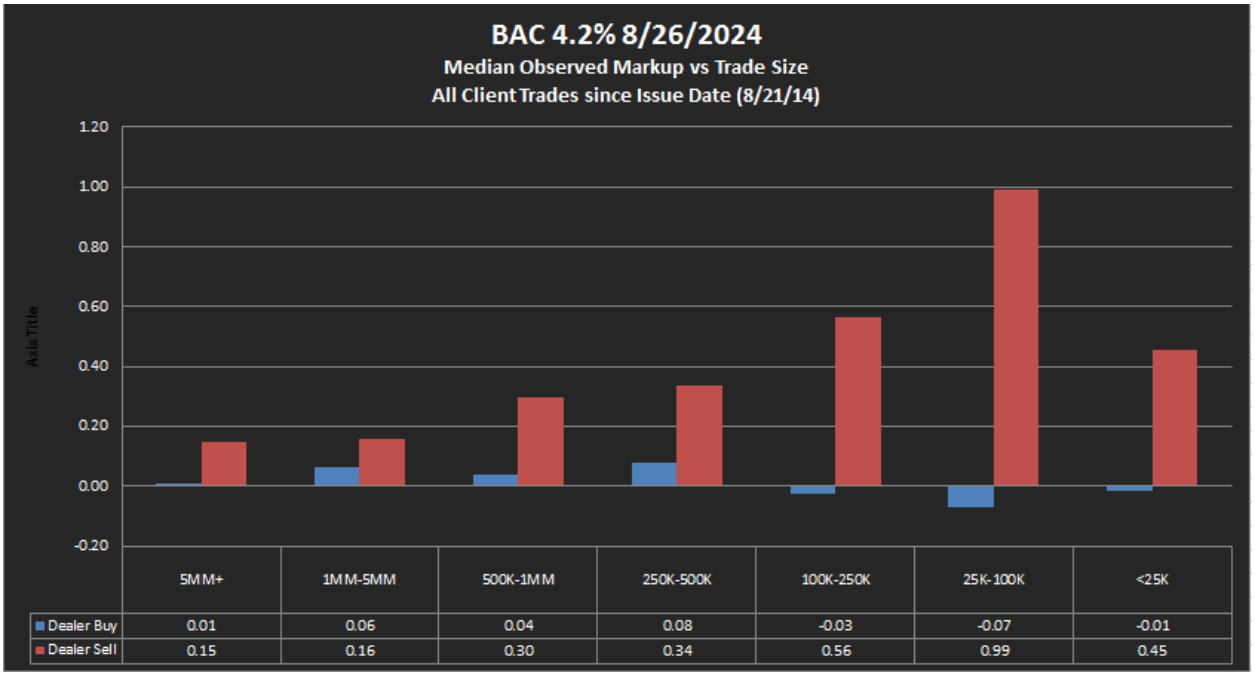

Figure 1 displays an example of observed mark-ups by trade size for Bank of America's 4.2% bond maturing on 8/26/2024. The size of the markup was estimated as the median difference between the transaction price reported to FINRA's TRACE® system and the corresponding bid side of Interactive Data's Continuous Fixed Income Evaluated Price (CEP). The consistently low deviations for dealer buys suggests that, in the absence of an actual transaction, the continuous evaluated bid price provides a representative benchmark for a dealer's acquisition cost and, by extension, the transaction cost incurred by investors when they buy bonds.

We believe retail investors would be more likely to understand the cost of fixed income trades if the reference price presented with each trade captured the collective experience of investors. For this particular bond, half of the buyers making purchases between $25,000 and $100,000 were charged no more than $0.99 above the price at which dealers would be able to buy the bond.

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Figure 2

Figure 2 displays an illustration of Apple's 2.4% bond maturing on 5/3/2023. The blue line display's Interactive Data Continuous Fixed Income Evaluations for this particular security, while the red circles indicate dealer-to-client sells (the circle's area corresponds to the size of trade), the green circles indicate dealer-from-client buys and the yellow circles show intra-dealer trades.

Comment on Notice 2014-20

from John Smith,

on Wednesday, December 10, 2014

Comment:

Here's another example of muni investors getting ripped off.

I today put in a 'bid wanted' on 15 bonds which last traded yesterday at a price around 92.35. The best bid I received on these bonds today was 86.58. Really? Why such a wide spread on an issue that traded yesterday? I would have expected a price of around 90, give or take 1/2 point. BTW, when I had put in a bid wanted last week the best price was around 76.

When will FINRA or the SEC start enforcing real price checks using MSRB-provided time & sales data in arriving at the price given to investors?

Comment on Notice 2014-20

from Jorge Rosso,

on Monday, November 24, 2014

Comment:

It is a of great advantage for new bond buyers although they can figure out their commissions?

January 12th, 2015

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

Financial Industry Regulation Authority (FINRA)
Los Angeles Office
300 South Grand Ave., 16th Floor
Los Angeles, CA 90071

Re: Regulatory Notice: 2014-20
Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations.

Dear Mr. Smith, et al.,

My name is Karin Tex, a retiree, and a life-time resident of California and a Citizen of the United States.

In my retirement, I have invested in municipal bonds; but I was unaware that unlike stocks, municipal bonds disclosure rules for transactions are very different. A municipal bond confirmation does not need to state the commission/mark up amount. **I know.....shocking in this day and age....especially with the evolution of sophisticated computer systems.** Disclosure of a municipal bond commission or markup to the general public should be mandatory.

According to the Municipal Securities Rulemaking Board Annual Report 2013, the Municipal Bonds Marketplace is a: $3.7 Trillion Dollar Market. There are millions of retirees, who invest in the municipal bonds, expect full disclosure and transparency in retail municipal bond transactions. Furthermore, it is my understanding that the municipal bond market generates Tens (10s) of Billions of dollars in commission per year for brokerage firms. **This should not be at the expense of retirees/seniors who have limited income.**

With such a vast municipal bond market, it is impossible for retirees/seniors to solely trust their financial advisors. A municipal bond transaction must be confirmed on a confirmation statement indicating the commission or markup amount that was charged to a retail customer. It is imperative that this is done!

It is puzzling that it has taken this long to acknowledge this deficiency in the reporting process to retail customers by the various regulatory agencies. It is obvious according to many articles written about this problem – which has been ongoing. I am attaching herewith several articles that outline this existing problem. [Please see attached.]

Seniors/Retirees and other retail investors alike look forward to full commission/markup disclosure by municipal bond dealers. It will make the municipal bond market more honest and responsible. This will solve a huge problem.

I hope and pray that the Regulatory Powers act quickly implementing full disclosure of commissions/markups upon municipal bond dealers/brokerage firms for the benefit of all retail customers.

Best regards,

Karin M. Tex

Karin Tex

KT/cs
Encl:

Service List

1. Securities and Exchange Commission (SEC)
   Los Angeles Regional Office
   Michele Wein Layne, Regional Director
   444 Flower Street, Suite 900
   Los Angeles, CA 90071
   Tel: (323) 965 3998

2. Sen. Dianne Feinstein
   San Diego Office
   880 Front Street, Suite 3296
   San Diego, CA 92101
   Tel: (619) 231 9712

3. Sen. Barbara Boxer
   San Diego Office
   600 B Street, Suite 2240
   San Diego, CA 92101
   Tel: (619) 239 3884

4. Rep. Susan Davis – U.S. 53rd District
   San Diego Office
   2700 Adams Ave., Suite 102
   San Diego, CA 92116
   Tel: (619) 280 5353

5. San Diego Union Tribune
   350 Camino de la Reina
   San Diego, CA 92108
   Tel: (800) 533 8830

The articles referenced as attached in the comment letter are not reprinted here, and are as follows:

"If you own bonds, you could be getting ripped off," Bloomberg

"Muni-bond purchase fees sting retirees" [name of publication not provided in article]

Comment on Notice 2014-20

from George McLiney, McLiney And Company

on Monday, December 22, 2014

Comment:

December 22, 2014

Re: MSRB's Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations

After participating in the December 18 webinar on the proposed municipal price disclosure I am discouraged and confused.

Before I get into my reasons for discouragement and confusion let me give you a little background. I have a fifty-five year history in the municipal bond business in Kansas City having found McLiney And Company in 1966. Over this period of time neither the company nor I have had any customer complaints and no serious differences with the NASD, SEC or Finra.

I am discouraged to see additional burdens placed on our compliance requirement covering same day principal trades. The multiplication of rules and regulations has already burdened our operation and any additional one will cause additional hardship. I am ever hopeful that the next set of rules will not be the straw that breaks the camel's back. My understanding was that EMMA was going to be the solution to market transparency. Has it failed? We have found it challenging to comply with the existing EMMA's disclosure requirements. The logistics in complying with the proposed changes will be difficult for us to implement.

I am confused as to how the proposed rule would be implemented and what transactions it would cover. Would it cover a same day purchase and sale on a bid from a bond broker; purchase of a block of bonds and sale over several days or a new issue sold in one day or over several days?

The continuous onslaught of new rules and regulations are a factor in driving municipal dealers especially small ones like ourselves, out of business. These dealers specialize in serving the small retail investor and bond issuer. Eliminating these dealers does not help the investors or issuers. The large dealers perhaps have the personnel to jump through these added hoops, but do not have the interest in serving the small investor's $5,000 to $50,000 purchaser or the small nonrated issuer of $100,000 to $1,000,000.

As a reference to the effect of constantly increasing rules, I went back to a directory of municipal dealers when McLiney And Company was founded and checking Missouri I found that in 1966 there was listings of fifty-eight dealers in the state and two bond attorney firms. Currently there are approximately eighteen dealers and twenty municipal bond law firms. In that period of increased municipal activity, the number of dealers has decreased 70% and the number of municipal bond law firms has increased 900%.

More rules equals fewer small dealers and more lawyers. This in no way helps the small municipal investor or the small municipal issuer.

I would hope you could stick with the existing rules relying on the integrity of the dealers and the transparency provided by EMMA. We did not build a business being unfair to our customers.

Very truly yours,

George J. McLiney, Jr.
McLiney And Company
2800 McGee Trafficway
Kansas City, MO 64108
(816) 221-4042
gjm@mcliney.com

Morgan Stanley
2000 Westchester Avenue
Purchase, NY 10577

Morgan Stanley

January 20, 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 14-52,
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2014-20,
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 14-52 and the Municipal Securities Rulemaking Board's ("MSRB") Regulatory Notice 2014-20 (together, 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 over $2.0 trillion in client assets as of December 31, 2014. MSSB offers personalized services to its wealth management clients through its more than 16,000 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 supports 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. 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. Matching Methodology and Disclosure

Morgan Stanley is concerned the matching methodology set forth in the Proposals will confuse investors and inaccurately represent a dealer's contemporaneous cost as well as its compensation and transaction costs. In particular, the likelihood of intra-day volatility and the degree of such volatility increases as the window for matching trades increases, such that the matched or "reference transaction" may no longer represent the prevailing market price for the security and the resulting differential may over or understate dealer compensation. Moreover, as a result of the complexity of the matching methodology, investors are not likely to understand why pricing information is disclosed on some trade confirmations and not others, nor what the reference transaction represents or how it was determined for their particular trade (for example, whether a "LIFO" or volume weighted average approach was utilized to match customer trades to a group of reference trades under the FINRA Proposal). In addition, under the Proposals, it is conceivable that similarly situated investors trading on the same side of the market roughly contemporaneously would receive disclosures of different matched trades by application of the methodology or one investor may receive a disclosure while the other does not.

In order to address these concerns with the matching methodology and disclosures, consistent with SIFMA's comment letter on the Proposals, Morgan Stanley would support enhancing TRACE and EMMA and promoting their use by retail customers through investor education. As noted by SIFMA in its comment letter, the MSRB recently acknowledged that the Proposal "would provide investors with information generally already publicly available" on EMMA.[1] Among other important data, TRACE and EMMA provide investors with information concerning the prevailing market price of their securities so they are better positioned to assess the quality of their trade executions and dealer's contemporaneous cost and compensation. Dealers could also assist in this effort by providing links on trade confirmations to TRACE and EMMA.

In light of the Proposals' objective to enhance transparency concerning dealer compensation and transaction costs, Morgan Stanley suggests FINRA and MSRB limit any confirmation disclosure requirement to riskless principal transactions, consistent both with the Securities and Exchange Commission ("SEC") recommendations cited in the Proposals, as well as with existing SEC disclosure requirements for equity securities. While such a disclosure requirement would impose significant implementation costs, it would more accurately represent dealer compensation and transaction costs and address many of the challenges presented by the Proposals as described above and in the SIFMA comment letter. Should FINRA and MSRB extend any disclosure obligation beyond riskless principal transactions, Morgan Stanley urges FINRA and MSRB to narrow substantially the time window during which trades are matched to fifteen minutes, consistent both with the existing timeframe for complying with trade reporting obligations, as well as MSRB's recent study of secondary market transactions in municipal securities which reported that the vast majority of intraday paired trades occur within fifteen

[1] MSRB, 2014 Annual Report at 6.

minutes.[2] While the implementation costs of such a disclosure obligation would be significant, the narrowed time window substantially mitigates the risk of volatility and investor confusion and would also enable FINRA and MSRB to simplify the matching methodology. Alternatively, in lieu of disclosing matching or reference transaction prices, disclosure could consist of the most recent TRACE or EMMA print in the applicable security.

2. Inter-affiliate Transactions

As SIFMA commented, any disclosure obligation should not apply where the customer trade is matched to a trade between the dealer and its affiliate. As described above, 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.

3. Trades with Sophisticated Clients

Morgan Stanley also shares SIFMA's view that in addition to only requiring disclosures for trades below a certain size, specific price reference disclosure should not be required for trades with sophisticated customers (such as qualified purchasers (as defined in Investment Company Act Section 2(a)(51)), institutional accounts (as defined in FINRA Rule 4512(c) and MSRB Rule G-8(a)(xi)) and sophisticated municipal market professionals (as defined in MSRB Rule D-15(a))), regardless of trade size as these customers commonly transact in trade sizes below the threshold in the Proposals. As SIFMA notes, these are established concepts which evidence a regulatory or congressional determination that the clients in question do not require the same type of protection afforded to retail investors. These types of investors have the sophistication to assess pricing and are also more likely to have relationships with multiple dealers and to transact with those that provide more favorable pricing. In addition, utilizing existing sophisticated investor standards that firms already employ within their businesses would simplify implementation in comparison to developing a new definition of retail investor for purposes of the Proposals.

4. Implementation Costs and Challenges

Finally, Morgan Stanley stresses the 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 comment letter and should be compared against the costs and benefits of the alternative approaches to increase transparency in the fixed income markets suggested by SIFMA and Morgan Stanley.

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

In conclusion, rather than implement an overly complex, confusing and costly disclosure requirement, Morgan Stanley urges FINRA and MSRB to explore the alternatives suggested by SIFMA and Morgan Stanley to address the policy objectives set forth in the Proposals.

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,

Vincent Lumia
Managing Director
Morgan Stanley Smith Barney LLC

NATHAN HALE
CAPITAL LLC

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FAX: 980.237.4755
www.NathanHaleCapital.com

Member FINRA & SIPC

January 20, 2015

Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: 2014-20 – Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Information on Retail Customer Confirmations

Nathan Hale Capital, LLC is a fixed income institutional broker-dealer. Although we do not have any retail customers, we provide liquidity to broker dealers who have retail customers. It is our opinion that this proposal will significantly impact what has been described as "retail-size transactions" and the "retail-size" secondary market.

Best execution has been a focus of the regulators for quite some time now. We are concerned the current proposal may have un-intended consequences which ultimately hinder best execution for retail customers.

First, to circumvent the markup disclosure, it will be natural for salespeople and the bond desks at the retail broker dealers (primarily those with significant balance sheets) to sell bonds from their internal inventory. The reason they will focus on this is because these transactions will not report on confirmations and it will help them avoid "cost conversations" with clients. Please keep in mind that by focusing on their own internal inventory, as opposed to offerings from other broker dealers that may be more attractive and suitable (Price, Yield, Rating, Credit, Diversification, Portfolio Management), they are clearly being driven from best execution. It could put the salesperson in a position to do the wrong thing for their customers.

Second, broker dealers with large captive retail customer bases will look to internalize retail trading flow, i.e. buys and sells from customers. (Some of which already occurs when a broker dealer with a retail customer base dealer puts out a riskless bid wanted, receives the high bid, and then "tops" the

high bid). They will reduce transactions with other broker dealers, who are currently the "liquidity providers", in order to circumvent the disclosure. The liquidity providers' balance sheets and overall trading risk will increase as their turnover will decrease, forcing wider markets and weaker bids on "retail size" bids wanted (worse two-way execution for retail sellers). Broker Dealers with large retail customer bases will increase their balance sheets to take advantage of the weaker bid sides on the wider markets and will boost their revenue at the expense of their own customer base. These broker dealers may also look to transact with an affiliate company, if it would help the firm provide more favorable reporting. Transactions with affiliates/sister companies should be reported from the original cost basis.

Third, as turnover decreases it will be much harder for broker dealers that are the liquidity providers to stay in business. There will be a reduction in the number of bidders that currently help provide best execution for "retail size trades." As there will be less competition among dealers, bids will become weaker and markets wider. Each dealer can only commit a certain amount of capital. Once they have reached their limits, they will no longer be able to compete and provide the services and liquidity that they have been for the retail customers. Ultimately, the "Market" becomes more fragile.

Considerations:

Emma.msrb.org - The price discovery function on Emma is a far better tool of viewing actual relevant trade data. Bonds in similar states, sectors, maturities, and rating categories can be easily compared. A focus on educating the retail client about how to access and use this data should be a priority.

True Cost Picture – The focus of the proposed rule only considers the price of the transaction and revenue generated. It would not provide the retail investor with actual profit (or loss) of the trade realized by the broker dealer. For example, what if a bond is sold to a client at cost? By the time expenses (Bloomberg, Clearing Fees, Office Space, to name a few) are considered, the result is actually a loss to the broker dealer.

Effect on Risk Management and Customer Prices– Traders will spend more time managing the disclosure rule than their positions. At a time when volatility is increasing due to less activity from broker dealers, the industry should consider focusing more on risk management.

Firm Blocking- Currently there is an issue within most fixed income products where broker dealers are not allowing their retail customers or their advisors to view competitive offerings/markets from external dealers. It is generally a decision made by management at firms with large retail client bases in order to internalize their retail trading flows (kind of like their own dark pool) and maximize their trading desk's profits for their firm. We would expect for this proposal to lead to more blocking and hinder best execution.

Suggestions:

FINRA may want to consider creating and disclosing a scale (Expensive – Moderate – Reasonable- Cheap) of markups, based upon the size and maturity of the trade and require broker dealers to choose the acceptable range on retail customer confirmations. Based upon the markup on the transaction by the Advisor, the applicable range would be marked on the confirmation and the retail customer would know how they were treated.

Transaction Cost Scale (On Retail Customer Confirmations)

Expensive	Moderate	X	Reasonable	Cheap

Another alternative would be to disclose all the trades/prints within the security for six months or 1 year on the confirmation to clients designated as "Retail Customers". This would provide the customer with a greater range of information to determine the market price, range, and the mark-up/commission.

Why limit the proposal and process to just same day, secondary market "retail trades"? If there are going to be new disclosures on confirmations, it is our opinion that all trades to designated "Retail Customers", regardless of time and size should be included in this proposal. Finally, why would it be limited to only secondary market trades? Why should new issue trades be excluded?

Other:

FINRA is concerned with helping the retail investor determine value of a specific security. A price differential disclosure cannot tell someone what the intrinsic value of a security is because there is no regard to that person's risk tolerance, investment objectives, cash flow needs or portfolio management strategy as a whole.

Scenario - What happens when a firm loses money on a trade (intraday) and the confirmation shows a loss to a client? Will the price or suitability be questioned by the customer? – The professionals just took a loss on that bond! If the question arises, how should an Advisor handle that call?

Since the confirmations are in question, and will possibly be overhauled, please consider showing the anticipated future cash flows (barring default) that the customer will receive on a "Buy" Confirmation. This would be valuable and useful information for retail customers.

Thank you for your time and consideration.

Sincerely,

Peter G. Brandel
Senior Vice President Municipal Bond Trading
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OFFICE OF THE
INVESTOR ADVOCATE

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

January 20, 2015

Submitted Electronically

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

RE: Regulatory Notice 2014-20
Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations

Dear Mr. Smith:

Pursuant to Section 4(g)(4) of the Securities Exchange Act of 1934, the new Office of the Investor Advocate at the U.S. Securities and Exchange Commission is responsible for analyzing the potential impact on investors of proposed rules of the Commission and self-regulatory organizations ("SROs"). More broadly, we are also required to identify areas in which investors would benefit from changes in the existing regulations of the Commission or the rules of SROs. In furtherance of these objectives, we will routinely review existing rules and rulemaking proposals of the Municipal Securities Rulemaking Board ("MSRB"). We will make recommendations to the MSRB from time to time, utilizing the public comment process when appropriate. In addition, as required by Section 4(g)(4)(B), we will report to Congress on the actions taken in response to our recommendations.

We are pleased to have this opportunity to submit comments regarding your proposed rule requiring dealers to provide pricing reference information on customer confirmations for transactions in municipal securities, as described in Regulatory Notice 2014-20 (the "Notice").[1] In short, we support the MSRB's effort to increase price transparency for retail customers, and we urge you to adopt the proposed amendments to Rule G-15.

Although individual investors already receive some of the information at issue and have access to the MSRB's Electronic Municipal Market Access ("EMMA") website, customer confirmations are not currently required to include information about the cost of the security to the firm.[2] Nor is it easy for individual investors to determine the value of a security using the publicly available information. Requiring dealers to provide pricing reference information on retail customer confirmations is a

[1] The comments provided in this letter are solely those of the Office of the Investor Advocate and do not necessarily reflect the views of the Commission, the Commissioners, or those of any other Office, Division, or Commission staff. The Commission has expressed no view regarding the statements of the Office of the Investor Advocate expressed herein.
[2] Securities and Exchange Commission, Report on the Municipal Securities Market, at 147, July 31, 2012, http://www.sec.gov/news/studies/2012/munireport073112.pdf.

necessary step toward making pricing information accessible to all investors, including those who do not seek it out.

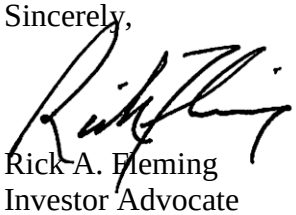
Steps to improve price transparency will benefit individual investors in significant ways. By requiring firms to disclose the price to the dealer in a reference transaction and the differential between the price to the customer and the price to the dealer, customers in retail-size trades will be better equipped to evaluate the transaction costs and the quality of service provided to them by dealers. This will promote competition and improve market efficiency. In addition, the proposed rule will deter abuses because firms will be less likely to charge excessive mark-ups when the price differential must be disclosed so clearly, and customers and the MSRB will likely detect improper practices more easily. Similarly, such a requirement may effectively facilitate the best execution of individual investor orders in municipal securities transactions.

In your consideration of the costs and benefits of the proposed rule, we urge you to consider the current costs already being borne by investors in municipal securities. To achieve the type of pricing information envisioned by the rule, investors today must learn to navigate through EMMA and then take the time to identify prices in corresponding transactions. While the cost or burden to each individual investor may be modest, the aggregate costs are high. It would be far more efficient to shift the burden to the dealers to disclose this type of information in an automated manner, rather than expect investors to go searching for the information.

The Notice seeks comment about the appropriate methodologies to use in determining the reference transaction price and differential to be disclosed when a firm executes multiple corresponding transactions. We believe the methodologies you adopt should be simple, based upon clear logic, and consistent with the methodologies adopted by FINRA.

In conclusion, we applaud the MSRB's efforts to improve price transparency in the municipal securities market. We also appreciate the collaborative and cooperative manner in which the MSRB has worked with FINRA to achieve consistent goals. Your significant efforts will impact post-trade price transparency for individual investors, and we encourage you to continue to make advances not only in post-trade price transparency, but also in pre-trade price transparency. Should you have any questions, please do not hesitate to contact me.

Sincerely,



Rick A. Fleming
Investor Advocate

Comment on Notice 2014-20

from Private Citizen,

on Sunday, November 23, 2014

Comment:

Basic background: I've been a muni bond investor for 10 years and have quite closely observed the pricing details posted on the EMMA site, which I find very helpful prior to executing my trades, to see if I'm being ripped off or getting a fair deal.

What I've noticed is that, on many occasions, the intra-day price discrepancy between customer and dealer transactions can be 5-10 points wide, rather than say within ~2 points which is more reasonable.

While I'm not against what this new rule is proposing, what would be more helpful to the retail customer is to know beforehand, just prior to trade execution, what the last price was, or in lieu of a last price should none exist, or if pricing details are too old to be of use, how the broker's price being offered to the customer was arrived at, so that the customer can better understand and discuss with his broker the reason for a markup (if buying)/markdown(if selling). In other words, the dealer should be required to discuss with the customer how their price was arrived at.

Otherwise, if this new rule is simply going to repeat already publicly availalbe EMMA data on a customer's trade confirmation documentation, and which won't be discussed with the customer pre-trade, then I don't think this rule goes far enough.

Greater transparency should be made available to the customer at the point of purchase/sale, not after the fact. Otheriwse, how can a customer determine a priori if what he's being charged is reasonable or not?

seelaus
the investment experts

January 8, 2015

Ronald W. Smith
Corporate Secretary, MSRB
Suite 600
Alexandria, Va. 22314

Dear Ronald:

I am writing to comment on MSRB proposed rule requiring dealers to provide pricing reference information on retail customer confirmations. As way of background R. Seelaus & Co., Inc. was established in 1984 as a municipal bond firm and today is a full service brokerage house specializing in all fixed income products. We do not have any proprietary products and do limited underwriting on a competitive basis in local northeast US names. We maintain inventory in municipals and taxable bonds and acquire most of our bonds in the secondary market. We sell bonds to individuals and institutions on a regular basis.

Over the last 30 years the municipal market has evolved and introduced significant improvements to the investing public. Book entry bonds, three day settlement and the MSRD reporting requirement for all trades has vastly improved the liquidity and safety of the market for all participants especially individuals. There can be no more transparency that the web site listing all transaction by time and size which thanks to the MSRB exists today. Underlying the explanation for the proposed rule seems to be disappointment that the public / individual investor doesn't use the web site more to check on dealer mark-up. I don't believe the solution to that situation is to take five steps backward into the 18th century. What the rule is proposing to do is to change printer layouts to add verbiage to a written confirm and send it through the US Mail in the hopes that the recipient will actually read the piece of paper. No offense to whoever dreamed this up but most people don't read their confirms anyway. With the advent of three day settlement the individual client either has the money in the account or gets the trade numbers from the broker. Most people throw the confirm in a drawer in case they ever need their tax cost.

In the digital age your emphasis should be on electronic confirms to all individual clients. Most people have email and use it frequently. If the trade is confirmed electronically the client would already be at the computer and with a mandatory link to EMMA on all confirms would be immediately in a position to access the web page.

What the current proposal boils down to is a regressive vision of the future which will be expensive, ineffectual, virtually unenforceable and totally out of sync with the direction of the world.

Sincerely,

Richard Seelaus
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Comment on Notice 2014-20

from Paige Pierce, RW Smith & Associates, LLC

on Wednesday, January 21, 2015

Comment:

We were part of the team that assisted in drafting SIFMA's response to this proposal and wish to give our full support of the positions stated in their comment letter.

sifma
Invested in America

January 20, 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 14-52,**
Pricing Disclosure in the Fixed Income Markets

MSRB Regulatory Notice 2014-20,
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:

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 14-52 and the Municipal Securities Rulemaking Board's ("MSRB's") Regulatory Notice 2014-20 (together the "Matched Trade Proposals" or the "Proposals"). SIFMA strongly supports efforts to enhance bond market price transparency in a carefully calibrated manner that strikes the right balance in pursuing desired goals while minimizing unintended consequences. However, because the enormous costs and burdens associated with the Proposals would significantly outweigh the purported benefits, SIFMA urges that the Proposals be withdrawn in favor of an approach that encourages increased usage of the extensive pricing data already available on the existing Trade Reporting and Compliance Engine ("TRACE") and Electronic Municipal Market Access ("EMMA") systems.

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

INTRODUCTION AND SUMMARY

The Matched Trade Proposals seek to enhance fixed income price transparency by putting more information into the hands of retail investors in fixed income securities. SIFMA fully embraces this objective. Unfortunately, the Proposals fail to leverage the very tools that have led to unprecedented improvement in fixed income price transparency: the price dissemination systems operated by FINRA and the MSRB. As the SEC predicted at the time of their development, the TRACE and EMMA systems currently "provide better market information to investors on a timely basis (e.g., before the transaction)" than approaches that "focus[] on only one portion of the market," i.e., riskless principal transactions. The Proposals' reliance on confirmation disclosure concepts is misplaced. FINRA and the MSRB should instead focus on increasing usage of the abundance of market data made available through TRACE and EMMA. The Matched Trade Proposals would provide inferior disclosure, to fewer investors, while imposing unjustified costs and burdens than alternatives that increase TRACE and EMMA usage. Moreover, the Proposals fail to adopt a uniform approach and terminology, inviting additional costs and burdens if they are administered differently.

SIFMA's views on the Matched Trade Proposals are summarized as follows:

- ***SIFMA believes that the Matched Trade Proposals should be withdrawn and replaced with disclosures that encourage increased usage of bond pricing data and investor tools already on the TRACE and EMMA platforms.*** SIFMA urges FINRA and the MSRB to withdraw the Matched Trade Proposals in favor of an approach that furthers the shared objective of increasing fixed income price transparency by increasing investor usage and reliance on TRACE and EMMA. Specifically, SIFMA supports adding additional disclosure for retail customers on confirmation backers for TRACE and EMMA transactions providing explanatory information about the availability of comparative CUSIP-specific transaction data – together with pointers or hyperlinks to the relevant FINRA and MSRB webpages. SIFMA supports making periodic disclosure about the availability of pricing data and public user accounts through TRACE and EMMA in connection with account opening and customer statements. SIFMA also supports greater opportunities for direct access to TRACE and EMMA by retail customers through their online brokerage account platforms, as well as retail investor education efforts more generally. In short, FINRA and the MSRB should promote TRACE and EMMA as the solution for increased transparency, using the power of the internet to reach the ever-increasing portion of retail investors who rely on it on a daily basis for communications and commerce of every sort.

  The confirmation disclosure obligation set forth in the Proposals has a storied past. Some form of it has been entertained and rejected by the SEC on at least four occasions since 1978. On each occasion, the significant costs, burdens, and expenses it would have imposed were determined to fail cost-benefit assessments,

leading the SEC to pursue less costly (and more effective) alternatives. (Part I.A.) The alternatives that were pursued – the current TRACE and EMMA platforms operated by FINRA and the MSRB – have dramatically improved price transparency for the bond markets and continue to evolve. They were funded, and continue to be funded, by tens of millions of dollars in transaction fees every year and are resourced on an ongoing basis by the bond dealer community. (Part I.B.) Since 1994, FINRA, the MSRB, and the SEC have embraced these platforms as the primary vehicles for enhancing bond market price transparency. (Part I.C.) At a time when internet usage by American investors is at an all-time high, with mobile internet access ubiquitous, the Proposals are regrettably backward-looking, more costly, and inferior to existing forms of post-trade transparency. Rather than denigrate and circumvent their utilities, FINRA and the MSRB should explore ways to increase their everyday use by investors. (Part I.D.)

- ***SIFMA objects to the Matched Trade Proposals because they risk confusing retail investors, present unworkable challenges in application, and threaten burdensome operational challenges that would dwarf any claimed benefits***. The Proposals would mandate new disclosure that would be inherently confusing to retail investors. They would introduce the concept of a "reference transaction" – a term that is without meaning to retail customers in form or substance and is not readily determinable. Customers would understandably mistake the disclosure for a bond's prevailing market price and the corresponding mark-up – terms that do have meaning to them. The disclosure would do nothing to advance investor understanding of the market activity in their bonds more generally and – by artificially matching unrelated trades occurring potentially hours apart – actually threatens to mislead investors about the quality of execution.

  The many problems confronting the Proposals lead SIFMA to conclude that the Proposals are unworkable as constructed:

  - Investors will be misled as to dealer compensation. The Proposals present a substantial risk of confusing the very group of retail investors that the new disclosure was intended to help. Neither the nature of the proposed reference price nor its occasional appearance would be capable of summary description. The price differential disclosure would be confused with dealer compensation. But when intervening developments cause a bond's price to move on an intraday basis, or when the "matched" trades are entirely unrelated (as described below), the figure reflects market movement or merely the happenstance of a separately-negotiated transaction. (Part II.A.)

  - Investors will be misled by negative price differentials. The Proposals do not address the potential for confusion when the price differential would be a negative figure, or even whether a negative figure ought to be disclosed. (Part II.B.)

- Trading by separate desks and affiliates is not envisioned by the Proposals. The Proposals do not seem to contemplate that dealers' institutional, retail, and proprietary trading desks may operate independently, whether by formal separation or simply as separate businesses, complicating whether and how transactions would or should be matched across these desks. Certain dealers operate these different bond trading operations as separate legal entities, using different execution and clearance platforms, calling into question the feasibility of design and implementation. (Part II.C.)

- The Proposals conflict with rules governing new issue disclosures. The Proposals threaten confusion in the market for new issues of debt securities by potentially introducing disclosure that would conflict with FINRA and MSRB mandated underwriting compensation and fee disclosures. (Part II.D.)

- The Proposals ignore size as a pricing consideration. Unlike other proposals addressing fixed income pricing, the Proposals ignore the potential differences in pricing between retail and institutional-sized transactions. (Part II.E.)

- The Proposals are overbroad and would apply to trades with institutional and other sophisticated investors. Although the Proposals profess an objective to limit the proposed disclosure to retail customers, the threshold used for this obligation is too high and overbroad because it will include many trades with institutional and other sophisticated investors. (Part II.F.)

- The Proposals present enormous operational challenges. The Proposals present potentially insurmountable operational challenges, in large part because they ignore the complexity created by a convoluted matching mechanism and are not limited in application in the same manner as prior SEC proposals. Even so limited, the challenges and costs associated with the Proposals would be enormous. (Part II.G.)

- ***SIFMA believes that – if FINRA and the MSRB were to require a new confirmation disclosure obligation with specific price references – a number of critical changes must be made to minimize the risk of investor confusion and to mitigate the unnecessary implementation challenges.*** SIFMA does not believe that the approach taken by the Proposals is advisable or workable, and further believes that retail investors would be better served by greater use and reliance on pricing data currently available free of charge on TRACE and EMMA. But if some form of the Proposals does proceed, it should be more carefully tailored to avoid investor confusion by limiting the confirmation disclosure to riskless principal transactions involving retail customers. Additional clarifying changes are also needed to mitigate the excessive burdens and costs associated with the current formulation. Necessary changes include:

- The FINRA and MSRB Proposals must be uniform in design and terminology. Despite an effort to be uniform, the Proposals use different terms, phrases, and structure. In the context of the Proposals, there is no policy justification for having divergent approaches or terminology. Unnecessary differences in formulation invite unintended costs and burdens if (and all too often as) they are administered differently. (Part III.A.)

- Any retail confirmation disclosure with specific price references should apply solely to trades in which no market risk attaches to the dealer effecting the transaction ("riskless principal transactions"). Any retail confirmation disclosure obligation with specific price references should apply only to riskless principal transactions to avoid investor confusion and to ensure greater consistency with current obligations for equity transactions. While still very much a distant "second best" alternative to steering investors to the breadth of pricing information available on TRACE and EMMA and one that would still impose many of the high costs and burdens of the Proposals – such an approach would be much more aligned with the stated objective of the Proposals to provide information about dealer compensation. (Part III.B.)

- Riskless principal transactions should be classified using the established definition. Any new confirmation disclosure with specific price references should use established and clear terms, capable of concise explanation and easily understood by investors and dealers alike. (Part III.B)

- Any confirmation disclosure obligation with specific price references should be better tailored to retail trades and investors by using defined terms to exclude institutional and other sophisticated investors and more appropriate quantity thresholds. The "qualifying size" for transactions ought to be set at $99,999 face amount or less to avoid the many institutional transactions that involve face amounts of $100,000. In addition, consistent with the stated policy objectives of the Proposals, any new disclosure obligation with specific price references ought not to apply to institutional or other sophisticated customers as defined by existing FINRA Rule 4512(c) and MSRB Rule G-8(a)(xi) (defining "institutional account"), as well as Investment Company Act Section 2(a)(51) (defining "qualified purchaser"). (Part III.C.)

- Trading activity by separate trading desks and affiliates should not be matched. Should a confirmation disclosure obligation with specific price references not be limited to riskless principal transactions, any matching methodology should apply only to those trades executed by a member's retail desk. (Part III.D.)

- Less burdensome price reference disclosures should be allowed. For dealers that utilize standard mark-up or sales credit schedules, any

confirmation disclosure obligation with specific price references should be satisfied through disclosure of the schedule or the specified compensation figure. (Part III.E.)

- Any new confirmation requirement should not require confirmations to be canceled and corrected due solely to a change in the reference transaction price. (Part III.F.)

- ***SIFMA objects to the inadequacy of the cost-benefit analyses undertaken by FINRA and the MSRB.*** Nothing in the Proposals suggests that FINRA or the MSRB has even begun to compile a record – as required under federal law and their own policies – that would either permit an informed analysis of the costs and benefits presented by the Proposals or allow an appropriate review by the SEC. Nor do the Proposals even purport to comply with federal laws governing new recordkeeping requirements or burdens on small businesses. (Part IV.A.) There has been no apparent consideration – quantified or otherwise – of other alternatives including making better use of TRACE or EMMA to achieve some or all of the regulatory objective. Given longstanding policy to use these platforms as the primary mechanism for enhancements to bond market transparency, the costs associated with their development and maintenance must be considered in connection with the Proposals. The Proposals fail to provide sufficient justification for a departure from previous conclusions to invest in these platforms rather than pursue costly additional disclosure obligations. (Part IV.B.) Finally, based on assessments SIFMA has gathered on its own, the implementation costs would be enormous and simply cannot be justified on the basis of the aspirational, speculative benefits described in the Proposals. (Part IV.C.)

DISCUSSION

I. FINRA AND THE MSRB SHOULD CONTINUE TO EMBRACE AND ENHANCE TRACE, EMMA, AND OTHER REAL TIME ELECTRONIC TRANSPARENCY INITIATIVES, RATHER THAN IMPOSE NEW (AND LESS EFFECTIVE) PRICE REFERENCE CONFIRMATION DISCLOSURE OBLIGATIONS.

A. The SEC, FINRA, and the MSRB Have Repeatedly Found that Confirmation Disclosure of the Sort Currently Proposed Is More Costly and Inferior to Alternative Forms of Post-Trade Transparency.

The SEC – citing concerns based on cost-benefit analyses – previously considered and rejected similar confirmation proposals on no less than four prior occasions. Ultimately, the SEC endorsed the development of electronic transparency platforms such as TRACE and EMMA over confirmation disclosure, finding that the price dissemination platforms would provide superior and more meaningful investor benefits.

The first SEC proposal to require disclosure of mark-ups on riskless principal transactions in municipal and corporate debt securities was deferred in large part because of concerns that the costs would outweigh the benefit, especially as to municipal bond investments.[2] In particular, the MSRB urged the Commission to consider whether such disclosure requirement was necessary in view of a proposed MSRB confirmation rule.[3] Deferring to the MSRB, the Commission ultimately withdrew its proposal with respect to transactions in municipal securities.

The second SEC proposal to require disclosure of mark-ups on riskless principal transactions in municipal and corporate debt securities was again deferred based on the policy views of the MSRB.[4] Citing the MSRB's conclusion that "the imposition of a requirement to disclose remuneration in principal transactions in municipal securities is unnecessary and inappropriate," the Commission decided to re-propose the requirement to gather additional public comment from bond market investors and participants.[5]

The third SEC proposal,[6] which was singularly focused on the disclosure of mark-ups on riskless principal transactions in bonds, was withdrawn after commenters – including the MSRB – stated their view that it "failed to take into account the substantial differences between the markets for debt and equity securities" and "imposed an unreasonable burden on small broker-dealers."[7] The withdrawal notice stated the SEC's conclusion that the proposal would not achieve its purpose "at an acceptable cost and that there are alternative ways of achieving the same goal with fewer adverse side effects."[8]

Most recently, in 1994, the SEC again considered and rejected confirmation disclosure of mark-ups on riskless principal transactions in corporate and municipal bonds.[9] Once again, the SEC concluded that price transparency initiatives underway

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[2] Securities Confirmations, Exchange Act Rel. No. 12806, 41 Fed. Reg. 41,432 (Sept. 22, 1976) (proposing release).

[3] Securities Confirmations, Exchange Act Rel. No. 13508, 42 Fed. Reg. 25,318, 25,319 (May 17, 1977) (adopting release).

[4] Securities Confirmations, Exchange Act Rel. No. 13661, 42 Fed. Reg. 33,348 (June 30, 1977) (proposing release).

[5] Securities Confirmations, Exchange Act Rel. No. 15219, 43 Fed. Reg. 47,499, 47,500 (Oct. 16, 1978) (final rule; rule; rule rescission) (quoting MSRB letter of Feb. 10, 1978).

[6] Securities Confirmations, Exchange Act Rel. No. 15220, 43 Fed. Reg. 47,538 (Oct. 16, 1978) (proposing release).

[7] Securities Confirmations, Exchange Act Rel. No. 18987, 47 Fed. Reg. 37,919, 37,920 (Aug. 27, 1982) (withdrawing release).

[8] *Id.*

[9] Confirmation of Transactions, Exchange Act Rel. No. 33743, 59 Fed. Reg. 12,767 (Mar. 17, 1994).

by FINRA and the MSRB – specifically referencing the predecessor to TRACE and a "developmental" version of EMMA – promised "more meaningful benefits to investors in the long-term" about a larger portion of the market than the proposed confirmation disclosure.[10]

The SEC's decision to withdraw the proposal was explicitly conditioned on the development by FINRA and the MSRB, with the support of the dealer community, of platforms that would provide greater price transparency for retail investors. The SEC viewed these price transparency platforms as a better, more effective alternative to confirmation disclosure. In reaching this determination, the Commission concluded that the proposed price information systems would provide superior investor benefits than the proposed mark-up disclosure:

> The Commission has deferred adoption of the riskless principal mark-up disclosure proposal in order to ascertain whether the proposed price information systems can provide more meaningful benefits to investors in the long-term and to assess the progress of the industry in developing the proposed systems. Price transparency, if fully developed, will provide better market information to investors on a timely basis (e.g., before the transaction). . . . The proposed mark-up disclosure, on the other hand, would have provided cost information to investors only in riskless principal transactions and would not have applied to other principal transactions, the majority of transactions in the debt market. Price transparency, if fully developed, meets investors' need for information without focusing on only one portion of the market . . . . The Commission recognizes that these benefits depend on the sound design and successful implementation of transparency proposals. . . . In the absence of progress on transparency, the Commission will revisit its riskless principal proposal.[11]

The Commission's policy choice was clear and informed: electronic post-trade price dissemination would bring "more meaningful benefits to investors" than piecemeal mark-up disclosure on riskless principal transactions. This choice – made at a time when the internet was in its infancy – recognized that the utility of confirmation disclosure must be assessed against the alternatives made possible by electronic transparency platforms.

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[10] Confirmation of Transactions, Exchange Act Rel. No. 34962, 59 Fed. Reg. 59,612, 59,616 (Nov. 17, 1994).

[11] *Id*.

Since the last consideration of some variant of the current confirmation proposal in 1994, there have been tremendous – indeed previously unimaginable – improvements in post-trade price transparency, coinciding with the explosive growth in internet access over the last two decades. Current and contemplated pricing transparency in TRACE and EMMA makes pricing information available to retail bond investors far more meaningful than anything under consideration in the confirmation disclosure proposals, all at the click of a mouse or swipe of a finger. Until now, at no point since 1994 – in spite of several dozen rulemakings addressing transaction reporting and dissemination and twenty years of published priorities – has the SEC expressed dissatisfaction with the transparency afforded by TRACE and EMMA. Similarly, FINRA and the MSRB have never before questioned the utility of TRACE and EMMA, despite statements in the Proposals questioning retail bond investors' usage and knowledge of these systems. As discussed in Part I.D, enhancing retail investors' use of TRACE and EMMA would result in greater post-trade price transparency at significantly lower cost than the Proposals.

B. The Policy Choice Made by the SEC, FINRA, and the MSRB To Fund and Construct Internet-Based Transparency Platforms To Reduce Informational Disparity Was Sound, Is Working Well, and Should Be Embraced.

Since 1994, FINRA and the MSRB have dramatically increased the information available to retail investors and the market generally about the prices of municipal and corporate bond transactions. The progress has been substantial. Over the course of two decades, retail bond investors have gained unprecedented access on a near-real time basis to prices of secondary transactions in corporate and municipal bonds across nearly every product class – far exceeding the SEC's expectation. The development and efficacy of these transparency platforms are directly relevant to whether – as proposed – a transaction confirmation approach to price transparency is warranted. As the MSRB itself acknowledged:

> Significant advances in the fixed income markets have helped to improve price transparency since the SEC's rulemaking efforts. Indeed, the SEC deferred consideration of its 1994 markup disclosure proposal due, in large part, to the planned development of systems that would make publicly available pricing information for municipal transactions.[12]

Indeed, the SEC's 2012 Report on the Municipal Securities Market ("SEC Municipal Report") also observed that "there have been significant improvements in recent years in the area of post-trade transparency," and that "[t]ransaction data can be accessed by the public free-of-charge through MSRB's EMMA website."[13] FINRA's TRACE

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12 MSRB Regulatory Notice at 5.

13 U.S. Securities and Exchange Commission, Report on the Municipal Securities Market

platform also "now provides investors with access to bond transaction and price information free of charge and on a near real-time basis for a significant portion of U.S. corporate bond market activity."[14]

Consistent with the explosion of electronic access made available with the internet, retail bond investors today have access to an increasing amount of information at no cost to them at speeds and in ways unimaginable in 1994. Rapid growth in internet access and penetration over the past two decades has paralleled the development and continued enhancement of TRACE and EMMA. In 1995, shortly after the SEC endorsed the development of price information systems, only 14 percent of American adults used the internet; by 2014, that number had increased to 87 percent.[15] The SEC recognized the transformative power of the internet more than 15 years ago, noting in a 1999 report that online-brokerage had caused "one of the biggest shifts in individual investors' relationships with their brokers since the invention of the telephone," and that "[f]or the first time ever, investors can – from the comfort of their own homes – access a wealth of financial information on the same terms as market professionals, including breaking news developments and market data."[16] Five years ago, an SEC survey found that 56 percent of investors rely on the internet in making investment decisions.[17] Inconceivable in 1994, today any retail investor with an internet connection has free access to information about corporate and municipal bond transaction prices that was previously unavailable even to professionals and regulators.

Today's TRACE and EMMA platforms are the result of more than twenty years of continued and incremental enhancements to corporate and municipal bond transaction reporting systems. The Fixed Income Pricing System (FIPS), the precursor

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(July 31, 2012) at 117 ("Data is searchable on EMMA and includes: trade date and time; security description and CUSIP number; maturity date; interest rate; price; yield; trade amount; trade type (i.e., customer bought, customer sold, or interdealer); and credit rating by S&P and Fitch, if available.") [hereinafter SEC Municipal Report].

[14] Commissioner Daniel M. Gallagher, Remarks at Municipal Securities Rulemaking Board's 1st Annual Municipal Securities Regulator Summit, Washington, DC (May 29, 2014). *See also* Commissioner Michael S. Piwowar, Remarks at the 2014 Municipal Finance Conference presented by The Bond Buyer and Brandeis International Business School, Boston, Massachusetts (Aug. 1, 2014) (noting that, "[i]n recent years . . . strides have been made to increase post-trade transparency for municipal securities through [EMMA]," which "now provides a wealth of historical pricing information in the municipal securities market in an easy to access format.").

[15] Pew Research Internet Project, Internet Use Over Time, http://www.pewinternet.org/data-trend/internet-use/internet-use-over-time/ (last visited Dec. 14, 2014).

[16] U.S. Securities and Exchange Commission, Online Brokerage: Keeping Apace of Cyberspace (Nov. 1999), *available at* http://www.sec.gov/pdf/cybrtrnd.pdf.

[17] Investment Company Act. Rel. No. 28584, 74 Fed. Reg. 4,546, 4,560 n. 195 (Jan. 26, 2009).

to TRACE, began operation in 1994 and required reporting transactions in certain high-yield bonds. FINRA launched TRACE in 2002 to disseminate pricing information across the broader corporate bond market. Public dissemination of transaction information was expanded in phases to allow FINRA to study the impact of transparency on liquidity. Today, transactions across an expanding range of eligible securities generally must be reported to TRACE within fifteen minutes; this information, in turn, is disseminated immediately for those securities subject to dissemination.[18]

With respect to the municipal securities market, the MSRB began disseminating transaction price information through the Transaction Reporting System (TRS) subscription service in 1995.[19] Following a series of scheduled improvements, TRS was replaced in 2005 by the Real-time Transaction Reporting System (RTRS), which disseminated transaction price information for most trades in municipal securities through an automated, real-time feed.[20] The launch of the EMMA website in 2008 "put timely market information directly at the fingertips of retail investors" for free.[21] The MSRB has continually sought to improve and enhance EMMA, most recently through the launch of a new "price discovery tool" that permits investors "to more easily find and compare trade prices of municipal securities with similar characteristics."[22]

The resources devoted to make the TRACE and EMMA platforms robust and widely available have been substantial. Accordingly, the benefits to retail bond investors gained from transparency enhancements have come at a significant cost. Launched in 2002, TRACE expenses exceeded $12 million for the first twelve months of operation.[23] By 2013, FINRA was expending nearly all of the $58 million it collected in relevant fees to support the TRACE platform.[24] From 2009 to 2014, the MSRB spent more than $76 million on market information transparency programs and operations, including its real-time transaction reporting service available on EMMA.[25]

In addition to supporting these transparency platforms through transaction fees, member firms have had to build out and implement systems necessary to populate data

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18 FINRA, TRACE Fact Book 2013, at 4.

19 MSRB, Long-Range Plan for Market Transparency Products (Jan. 27, 2012) at 16.

20 *Id* at 17.

21 MSRB, 2008 Fact Book, at 1.

22 MSRB Regulatory Notice at 5-6.

23 Exchange Act Rel. No. 49086, 69 Fed. Reg. 3416 (Jan. 23, 2004).

24 FINRA, 2013 Year in Review and Annual Financial Report.

25 MSRB, 2014 Annual Report; MSRB, 2013 Annual Report; MSRB, 2012 Annual Report; MSRB, 2011 Annual Report; MSRB, 2010 Annual Report; MSRB, 2009 Annual Report.

fields for TRACE and EMMA. At every stage of the development of price transparency initiatives on the TRACE and EMMA platforms – including expansion to various product classes and enhancements to dissemination practices – FINRA and the MSRB have justified the costs to member firms based on comparisons to, among other things, alternative disclosures of the type currently proposed. These costs have included considerable front- and back-end build-outs necessary to capture and report transaction information, ongoing system maintenance, enhancements to supervisory and compliance procedures and reviews, regulatory oversight of TRACE and EMMA obligations, and training. Notably, such costs are not limited to one-time implementation system build-outs; there are substantial and continuing costs associated with ATS reporting, tagging particular transaction types (e.g., affiliated transactions), and accounts (e.g., fee-based accounts). Some member firms have already provided links or data from TRACE and EMMA directly to retail customers on their electronic brokerage platforms. The industry, through SIFMA, has historically funded and supported a number of investor education initiatives and resources.

C. The TRACE and EMMA Platforms Provide More Information About Corporate and Municipal Bond Transactions and Pricing – At No Cost to Retail Investors – Than Ever Before, Far Exceeding What Was Historically Available to Dealers and Institutional Investors.

The amount of post-transaction information available on TRACE and EMMA is substantial and growing. Introduced in July 2002, TRACE "helps create a level playing field for all market participants by providing comprehensive, real-time access to public bond price information," and since March 2010, for U.S. agency debentures.[26] Following years of incremental expansions, the number of TRACE-eligible securities "increased from 37,000 in 2007 to 1.4 million in 2012."[27] In May 2011, TRACE began collecting transactions in asset-based and mortgage-based securities, with transactions in agency pass-through mortgage-backed securities traded to be announced (TBA transactions) currently subject to dissemination.[28] In July 2013, TRACE began dissemination of specified pool transactions in mortgage-backed securities.[29] Launched in 2009, the EMMA website provides free access to "official disclosure documents, trade prices and yields, market statistics and more about virtually all municipal securities."[30] Associated market transparency products include the EMMA Primary Market Disclosure Service, the EMMA Continuing Disclosure Service, the EMMA Trade Price Transparency Service, the Short-term Obligation Rate Transparency (SHORT) System, and the MSRB's municipal market research

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[26] FINRA, TRACE Fact Book 2013 at 2.

[27] Press Release, FINRA, FINRA Marks Fifth Anniversary, July 30, 2012.

[28] FINRA, TRACE Fact Book 2013 at 2.

[29] *Id.*

[30] MSRB Regulatory Notice at 5.

services.[31]

The SEC, FINRA, and the MSRB have historically recognized that retail bond investors are best served by having access to the breadth and depth of pricing information available on TRACE and EMMA. Notwithstanding statements in the Proposals criticizing retail bond investors' ability to use or their knowledge of TRACE and EMMA, FINRA and the MSRB have never before questioned the utility of these platforms. On the contrary, FINRA and the MSRB have consistently – and appropriately – characterized TRACE and EMMA as major advances that brought unprecedented transparency to the corporate and municipal bond markets. In 2005, the NASD said that full implementation of TRACE "may be the most significant innovation benefiting retail bond investors in decades."[32] In 2008, the MSRB said that EMMA "put timely market information directly at the fingertips of retail investors" and "vastly improved on the information that retail investors could readily obtain."[33] In 2012, FINRA noted that TRACE is "providing unprecedented transparency to market participants and data to FINRA for effective regulatory oversight," as well as "saving investors an estimated $1 billion per year" through reduced transaction costs.[34] In 2013, the MSRB recognized that EMMA "has brought transparency of the municipal market to new levels."[35] In 2014, the MSRB described EMMA as "perhaps its single greatest contribution to the municipal market," referring to the EMMA website as "an indispensable resource for the market, with interactive tools to help users understand municipal trade prices."[36]

Given the magnitude of information available to retail investors for free on TRACE and EMMA, any perceived problems with investors using these systems should be addressed directly rather than mandating trade-specific confirmation disclosure. If there are issues to address, efforts would be better directed at encouraging and directing investors to use this information and potentially making the platforms even more user-friendly rather than deemphasizing their use. Indeed, FINRA and the MSRB both suggest that some retail investors are unwilling to access, or are simply unaware, of the extensive information available on TRACE and EMMA. FINRA acknowledges that "[a]lthough knowledgeable industrious customers could observe [principal and customer trades] retrospectively using TRACE data, . . . retail customers do not typically consult TRACE data."[37] For example, the MSRB suggests

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31 MSRB, Long-Range Plan for Market Transparency Products (Jan. 27, 2012) at 2.

32 Press Release, NASD, NASD's Fully Implemented "TRACE" Brings Unprecedented Transparency to Corporate Bond Market, Feb. 7, 2005.

33 MSRB, 2008 Fact Book at 1.

34 Press Release, FINRA, FINRA Marks Fifth Anniversary, July 30, 2012.

35 MSRB, 2013 Annual Report at II.

36 MSRB, 2014 Annual Report at 9.

37 FINRA Regulatory Notice at 2.

that the Proposal could benefit primarily those retail customers "who do not actively seek out [pricing] information, *including those who may not know of EMMA* or may not have the time or wherewithal to conduct their own transaction research" (emphasis added).[38] This sentiment undermines the basic principle that the MSRB built EMMA with the "specific aim of serving the needs of retail investors who are not expert in financial and investing matters and of other infrequent investors in or holders of municipal securities."[39] Rather than depart from this principle, greater effort should be made to ensure that retail investors better understand – or, at the very least, are made aware of – the information available to them for free on TRACE and EMMA.

Currently, TRACE and EMMA provide a wealth of information about secondary market transactions that are relevant to the Proposals' policy objective: all transactions in a particular CUSIP by date and time; the price of every transaction; information about the quantity of transactions; whether a transaction was with a dealer or customer; information about the bond's yield; as well as information about the bond and issuer itself that may bear on prices and likely yields. Moreover, TRACE and EMMA enhancements already planned or underway would allow for greater ease of use by retail investors and would permit an even greater understanding of market prices than the Proposals. For example, the MSRB set forth its vision for "EMMA 2.0" in its Long Range Plan for Market Transparency Products, outlining a series of planned enhancements including improved search functionality, free personalized alerts, integrated displays of information, expanded document and data collection, access to new categories of information, a new real-time central transparency platform (CTP), access to new tools and utilities, and improved investor education.[40] Recently, the MSRB introduced MyEMMA, which "provides customized access to municipal securities information by allowing users to set up alerts to be notified when new information on a particular security or group of securities becomes available on EMMA."[41] This level of personalization allows retail investors a level of understanding far beyond the objectives of the Proposals.[42]

Alternative approaches to post-trade transparency – including the Proposals – come at the expense of other initiatives underway or contemplated, as well as future initiatives not currently contemplated. The MSRB acknowledges its obligation to "guide the marshalling of MSRB resources . . . in the most cost-effective manner to achieve the greatest positive impact on the protection of investors, municipal entities, obligated persons and the public interest."[43] Limited resources would be better spent

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38 MSRB Regulatory Notice at 7.

39 MSRB, Long-Range Plan for Market Transparency Products (Jan. 27, 2012) at 5.

40 *Id* at 5-7.

41 MSRB, 2013 Annual Report at 9.

42 *See* MSRB Regulatory Notice at 19 (asking "[w]ould the disclosure of additional information on EMMA meet some or all of the objectives of this proposal?").

43 MSRB, Long-Range Plan for Market Transparency Products (Jan. 27, 2012) at 2.

ensuring the existing TRACE and EMMA systems are more widely used and potentially more user-friendly, rather than mandating costly new confirmation disclosure requirements with unproven benefits.

D. Alternatives that Embrace Existing FINRA and MSRB Transparency Policy Initiatives and Increase the Usage of TRACE and EMMA By Retail Investors of All Ages – Including Disclosures, Hyperlinks, and Pointers – Would Result in Greater Post-Trade Price Transparency at Significantly Lower Cost.

SIFMA believes that the Proposals should be withdrawn in favor of a uniform approach that relies on existing price transparency platforms. Any new confirmation disclosure should be designed to encourage retail bond investors to access TRACE or EMMA and should coincide with renewed education efforts to help those investors better understand the information available on those systems. In contrast to the astronomical costs and uncertain benefits associated with the Proposals, enhancing retail investors' use of these existing systems – developed over the past two decades after considerable and ongoing investment – would constitute a more cost-effective use of limited resources and result in greater price transparency for investors. As the MSRB acknowledged in its most recent annual report, the Proposal "would provide investors with information generally already publicly available" on EMMA.[44] Information on these platforms allow greater insight into a bond's prevailing market price and market conditions generally than any reference price disclosure contemplated by the Proposals.

Accordingly, SIFMA's first and principal recommendation is that FINRA and the MSRB withdraw the Proposals as formulated in favor of a uniform alternative calling for the use of disclosures, hyperlinks, and pointers on trade confirmations – as well as other forms of investor education – as a means to increasing investor use of post-transaction price transparency already available for free on the TRACE and EMMA platforms. Account opening documentation, quarterly statement disclosures, and confirmation backers also could remind retail investors about the availability of pricing information on TRACE and EMMA, while emphasizing that prices for transactions involving different sizes or characteristics may vary.[45] This approach properly emphasizes TRACE and EMMA at a time when retail investors increasingly rely on the internet and success could be measured by retail usage statistics and penetration rates.

FINRA and the MSRB could think more broadly about how to make corporate and municipal bond trading data available to retail investors, for example, by making the data available to application developers who may be able to develop novel ways to

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[44] MSRB, 2014 Annual Report at 6.

[45] *See, e.g.*, Regulation NMS Rule 606 (detailing customer disclosure obligations related to order routing practices).

drive relevant data to investors in ways that FINRA and the MSRB may not have imagined. For a fraction of the cost of implementing the Proposals, FINRA and the MSRB could incentivize application developers for such an effort. In short, FINRA and the MSRB should consider how to use the systems it has already developed, in conjunction with rapidly developing, forward-looking technology to drive solutions, rather than focusing on confirmation delivered disclosure.

Consistent with prior regulatory guidance and in light of continued growth in internet access and usage, FINRA and the MSRB should adopt an "access equals delivery" model with respect to pricing information available on TRACE and EMMA. NASD previously recognized the need "to modernize prospectus delivery obligations in view of technological and market structure developments of recent years."[46] Similarly, the MSRB argued that an "access equals delivery" standard for official statement deliveries would "promote significantly more effective and efficient delivery of material information" than physical delivery.[47] This reasoning applies in the same way to pricing information available on TRACE and EMMA.

The SEC, FINRA, and MSRB should increase investor education efforts with a special emphasis on increasing usage of TRACE and EMMA. SIFMA is prepared to engage and assist with these efforts. Improving retail investor knowledge about TRACE and EMMA is a natural extension of FINRA and the MSRB's existing education initiatives. For example, among its several educational efforts, the MSRB recently introduced a series of investor education videos – including a video for first-time users of the EMMA website explaining "how investors can use EMMA to learn about the municipal market, evaluate municipal bond features, risks and prices, and monitor the health of their municipal bond investments over time" – the success of which was noted in MSRB's annual report less than a year ago.[48] Given the suggestion that some retail investors are unaware of or choose not to use TRACE and EMMA, FINRA and the MSRB should redouble their efforts to encourage use of these systems and to ensure that investors understand the information available to them. SIFMA has historically funded a variety of investor education efforts and is prepared to support new initiatives to improve investor knowledge and usage of TRACE and EMMA.

II. SPECIFIC ISSUES WITH THE CURRENT PROPOSALS DEMONSTRATE THAT THE PROPOSALS ARE UNWORKABLE.

As formulated, the Matched Trade Proposals risk confusing the very group of retail bond investors that the new disclosure was designed to help. Having a

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[46] NASD, Report of the Mutual Fund Task Force: Mutual Fund Distribution (Mar. 29, 2005).

[47] MSRB Regulatory Notice 2006-19, MSRB Seeks Comments on Application of "Access Equals Delivery" Standard to Official Statement Dissemination for New Issue Municipal Securities (July 27, 2006).

[48] MSRB, 2013 Annual Report at 9.

transaction confirmation disclose the difference between the price of a "reference transaction" and the customer's transaction price on some bond transactions, in circumstances in which the "matched" transactions may be riskless principal transactions (or not), occurring during periods in which prices remain static (or not), so that the figure approximates dealer compensation (or not), as long as the transaction is with a retail customer (or not) and does not involve bonds held in inventory (for longer than a day) is a recipe for investor confusion, not education. A number of specific problems show that the Matched Trade Proposals are unworkable as designed.

First, the Proposals invite retail investors to equate the difference in price between artificially matched trades as dealer compensation when circumstances suggest otherwise. (Parts II.A, B, and E.) Next, by focusing exclusively on a subset of matched or reference transactions that do not exist absent an artificial methodology, the Proposals threaten a cascade of unintended – and likely intractable – problems for dealers and retail customers alike. The issues presented by affiliated entities are left entirely unaddressed and seem not to have been considered at all. (Part II.C.) Moreover, the Proposals – with but a single question – fail to explain why inferior "reference transaction" price disclosure should compete with existing disclosure about underwriting fees and selling concessions in offering documents for new issues (Part II.D) or why longstanding differences in how institutional-sized transactions are priced should be ignored when creating a new category of "reference transaction" disclosure (Part II.E). Indeed, as currently formulated the Proposals would broadly apply to many transactions with institutional customers. (Part II.F.)

But even if FINRA and the MSRB limited the scope of the Proposals to address these difficulties, the operational challenges to the design and implementation of the Proposals would still be far more daunting than acknowledged. From the need to design matching logic to the potentially insurmountable impediments of reaching across desks and entities to match, calculate, and populate configurable fields while relying on third party correspondent firms and data providers, the resources that would be demanded by the Proposals would dwarf any claimed benefits envisioned by the Proposals. (Part II.G.)

A. As Proposed, the Matching Methodology Would Capture At-Risk Trades and Compel "Price Differential" Disclosure that Will Be Confused with Dealer Compensation.

There is a substantial risk that retail customers would be confused by price differential disclosure when trades matched pursuant to the specified methodology are not truly riskless principal trades or when the reference trade is not close in time to the customer trade. In these circumstances, the disclosure may portray an inaccurate picture of the market pricing for the security. For example, if the market price of the bond shifted between the reference transaction and the customer transaction, the difference between the two prices will reflect, at least to some degree, profit or loss related to market risk. Profit or loss related to market risk, however, is not the same as the dealer compensation the Proposals claim they were designed to address. The

meaningfulness of the reference price differential – which is already an inexact proxy for dealer compensation – necessarily degrades over time and could be misleading to customers because the data may imply that the dealer received either more or less compensation than it actually did.

Over time many factors can impact the price of a fixed income security.[49] These factors may cause the price of the customer trade to vary significantly from the price of a reference transaction over time. For example, to the extent the market yield is correlated to a benchmark security, such as the 10 year Treasury, the benchmark yield may shift, changing the price of the security. Market events and changes to risk perceptions that may be unrelated to the particular issuer can cause the spread between the benchmark yield and the yield on the bond the customer is trading to widen or narrow. Idiosyncratic events may affect the price of the particular issue. The lower the credit quality, the more likely is the price to be effected by idiosyncratic events. These multiple features of bond pricing increase the noise and decrease the signal implicit in the reference price information over time. Indeed, current FINRA and MSRB fair pricing guidance identify a host of factors that can have a dramatic impact on prices on an intraday basis.

The relevance of the price at which a dealer transacted in a particular bond compared to the price charged to a customer decreases over time. Although the FINRA Proposal observed that more than half of retail bond transactions involved a corresponding principal trade within 30 minutes of the customer transaction, the Proposals are not so limited and apply to trades that occur over the course of the entire trading day.[50] Indeed, 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.[51] Since the stated purpose of the Proposals is to provide information to customers to assess their transactions, the confirmation disclosure ought not to apply to those trades that do not provide useful information to customers and that have the potential for confusion. The Proposals fail to justify why a "same day" approach is appropriate given the capture of so many unrelated trades in the pairing methodology.

Left unchanged, the Proposals would bring about disclosure to retail customers about price differentials that include or fail to include these factors, which will obfuscate the dealer compensation that the disclosure aims to accomplish. Customer confusion has real costs to firms and associated persons. Firms will need to expend

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[49] *See, e.g.*, FINRA Rule 2121.02(b)(4).

[50] The FINRA Regulatory Notice observed that 3Q 2013 TRACE data showed that over 60% of retail size trades had a corresponding principal trade on the same trading day, and that in over 88% of these trades the principal and customer trades occurred within 30 minutes. FINRA Regulatory Notice at 2.

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

resources to explain to customers why the pricing information is on the confirmation and why the prices are not related to each other. In addition, the disclosure could trigger unfounded customer complaints, which could in turn require disclosures on a registered representative's Form U4. As the Form U4 disclosure obligations are allegation driven and publicly reported through BrokerCheck, client confusion about pricing that leads to unfounded customer complaints may be unjustly harmful to the registered persons who are unfairly the subject of complaints based on misunderstandings.

As designed, the Proposals present a number of foreseeable risks, with unforeseen risks that may manifest themselves upon implementation. Aside from the near certain risk that retail customers will confuse the price differential figure with dealer compensation, the sporadic appearance of the disclosure will also surely – and understandably – result in a flood of calls questioning why some (but not all) transaction confirmations identify a reference transaction and accompanying calculation. There is simply no good answer for firms to give. As formulated, the disclosure requirement would be incapable of summary description. It is decidedly – and by its terms – not a mark-up, a commission, the prevailing market price, or some other familiar term. Nor could it be described as occasioned by the dealer acting in a particular capacity (agent or principal or riskless principal) already known to them. Call centers and registered representatives would be in the unenviable position of trying to learn and communicate the FINRA and MSRB matching methodologies (including LIFO, FIFO, and average weighted price principles) and explain how this figure may bear on an assessment of their transaction and why it appears on some but not all transaction confirmations. By altering the traditional use of the confirmation as a type of invoice describing (i.e., "confirming") the terms of the specific transaction, the Proposals will cause unnecessary customer confusion.

Customer confusion about dealer compensation or the quality of execution that would be triggered by matching unrelated transactions also risks customer retreat from the secondary bond markets and related diminution in liquidity. There is no suggestion in the Proposals that this risk has been evaluated beyond an acknowledgement that bond market liquidity is a relevant consideration.[52] For this reason among others, SIFMA believes that any disclosure obligation with specific price references should be limited to actual riskless principal transactions as described in Part III.B.

B. The Proposals Do Not Consider the Risk of Customer Confusion When the Price Differential Would Result in a Negative Figure.

There is also a substantial risk that retail customers will be confused by price differential disclosure when trades matched pursuant to the specified methodology result in a negative price differential. (FINRA's illustrative examples do not address this very real occurrence, though a recent FINRA/MSRB webinar confirmed the staff's view that customers should be provided with a negative figure in such a circumstance.)

[52] FINRA Regulatory Notice at 9; MSRB Regulatory Notice at 17.

This risk of confusion would be most acute when retail investors understandably equate the price differential disclosure with a dealer's mark-up. FINRA and the MSRB should consider the risk that a retail investor, seeing a negative price differential, may actually reach an erroneous conclusion that a dealer sold bonds at or below the prevailing market price. By contrast, a review of TRACE or EMMA prints easily accessible online (or through a push notice) would make clear that the market had moved and allow a better assessment of the transaction price than the proposed disclosure.

For example, if a dealer purchased a bond at par in the morning and sold it to a customer at 99 in the afternoon, the matched price disclosure would require the disclosure of -1.0. Were a retail customer to equate this figure with the amount of the dealer's mark-up, he or she may believe that the dealer sold the bonds at one point below the prevailing market price – an erroneous conclusion suggested by the proposed matching methodology.

C. The Proposals Fail To Recognize the Complications Associated with Transactions by Affiliated Broker-Dealers or Separate Trading Desks within the Same Member Firm.

The Matched Trade Proposals do not address ordinary situations in which affiliated broker-dealers or separate trading desks may transact in a manner that has the potential to trigger the proposed matching and related disclosure requirement. SIFMA believes that, as a general matter, transactions by different legal entities or separate trading desks should not be treated as though they resulted from a single trading operation, so as not to disregard legal and operational boundaries that are observed in fact. But SIFMA is also mindful that certain of the policy choices reflected in the structure of the Proposals – for example, excluding sales from aged inventory from the scope of the requirement – may be frustrated by some of the mechanisms used to transact by larger financial services firms. These complications demonstrate the need to fundamentally revisit the "reference transaction" approach in favor of something more workable and effective.

1. Separate Trading Desks.

Absent revision or clarification, the Proposals create uncertainty as to whether transactions executed by separate trading desks and businesses that operate independently would be treated as reference transactions when they were entirely unrelated. Many firms have their institutional bond trading department separate from their retail bond trading department, as well as operate separate proprietary trading desks. These firms may observe formal separation principles, operate the desks as different "aggregation units," or, depending on the circumstances, simply have them function as different businesses with different P&Ls and staff, often with one trading desk a customer of the other. The Proposals do not 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 (where such are permitted to exist) as potential reference transactions.

These situations present both substantive and operational complexity. On the substance, an unrelated purchase of bonds by a proprietary trading desk occurring coincidentally on the same day that the retail trading desk sells the same bond to a retail customer from inventory or from another source would not reveal anything meaningful about dealer compensation. Yet the Proposals may require firms to treat the trade from the proprietary desk as a "reference transaction" for the customer trade, incorrectly suggesting a linkage or that they were two legs of a riskless principal transaction. The same problem exists with separate institutional and retail trading desks. In terms of operational complexity, some member firms operate their institutional bond department on a different trading or settlement platform than their retail bond department. Incorporating reference data from a separate platform used by the institutional bond department onto the retail confirmation would be extremely difficult.

2. Transactions by Affiliated Firms.

At some financial services firms, the retail bond desk and institutional bond desk may be in separate affiliated member firms, complicating application of the reference transaction methodology. Some firms may also have affiliates that are dually-registered investment adviser / broker-dealers operating primarily as asset managers. Transactions between affiliates should not be treated as one leg of a paired trade. For example, a purchase by an asset management affiliate for an advisory client should not be treated a "reference transaction" for an entirely unrelated sale of the same bond held in inventory by the retail trading affiliate. Yet the Proposals may compel that result. Nor should transactions executed on behalf of advisory clients by dually registered broker-dealer / investment advisers on an agency basis be used as reference transactions or require confirmation disclosure of reference transactions.

Similarly, many firms accumulate at-risk inventory positions in one affiliate and transact with retail customers in a separate affiliate. For example, it is a rather commonplace occurrence for an institutional trading affiliate to accumulate a large inventory position in a particular bond over several days, and then show the bonds out to its retail trading affiliate (and through it, to retail customers). As retail customers choose to buy small lots in that bond from the retail trading affiliate, customer orders are filled through riskless principal transactions with the institutional affiliate. Treating the inter-affiliate, dealer-to-dealer transaction as a qualifying reference transaction would produce meaningless disclosure. What was essentially a type of inventory trade would be treated otherwise. If firms were instead required to look through to the original acquisition by the affiliate, this would result in additional operational costs and burdens to match trades that occurred in separate entities to confirm whether the transaction was more in the nature of an inventory transaction. Affiliate to affiliate transfers are tantamount to an internal booking move and should not be viewed as a matching trade for a customer trade. Otherwise, customers of an

entity employing one entity will be treated differently than those with the affiliate structure for what are comparable trades.

D. The Proposals Are Unnecessarily Vague as to Their Application to New Issues.

The proposed confirmation disclosure should not apply to new issues of corporate or municipal debt securities. With the exception of the request for comment on whether the confirmation disclosure obligation should apply to new issue trades[53] and the MSRB's acknowledgement that its preliminary statistics excluded new issues,[54] the Proposals do not address their intended applicability to new issues. As a general matter, a dealer's underwriting compensation is disclosed in the offering documents and historically has been addressed in rules separate from those governing secondary market activity. There is no reason to start merging these obligations through the proposed confirmation disclosure.

FINRA's corporate financing rule (FINRA Rule 5110) sets forth detailed guidance on the calculation and fairness of underwriting compensation that is subject to prospectus disclosure, and MSRB Rule G-32 serves a similar purpose in governing new issues of municipal securities. These rules are separate and apart from the rules governing fair prices and commissions (FINRA Rule 2121 and MSRB G-30) that address dealer compensation on secondary market transactions. The Proposals should not apply for new issues where the underwriter's compensation is described in a prospectus, offering memorandum, official statement or similar document. In these circumstances, the disclosure in the offering materials is relevant; separate (and potentially conflicting) disclosure of reference pricing is not.

E. The Proposals Do Not Take Into Account Legitimate Differences in Pricing for Institutional-Sized Trades and the Implications of Using Those as "Reference Transactions."

The difference between the price of the reference transaction and the price of the customer trade would be confusing when the reference transaction is with an institution or another dealer (either directly or through an inter-dealer broker). The Proposals do not take into account the legitimate pricing differences that occur between institutional, dealer, and retail trades.[55] As proposed, the confirmation disclosure obligation would apply in instances where the reference transaction is with an institution (or with another dealer, or with another retail customer) and the customer trade is with a retail customer. But trades with institutions, dealers, or other retail

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53 *See* FINRA Regulatory Notice at 11; MSRB Regulatory Notice at 18.

54 *See* MSRB Regulatory Notice at 10.

55 *See* Letter from Sharon K. Zackula, NASD, to Katherine A. England, SEC (Oct. 4, 2005) ("[C]ommenters agree with NASD's recognition that a bond's contemporaneous cost may not reflect the [prevailing market price] in the case of certain large trades . . . .").

customers in a particular bond may be priced differently from each other, and institutional and dealer trades are priced differently than retail trades. For institutional trades, any mark-up may already be included in the price. Retail trades generally require far more effort than institutional trades, a point repeatedly acknowledged by the SEC, FINRA, and the MSRB in a variety of contexts.[56]

F. Although Designed To Benefit Retail Customers, as Proposed the Confirmation Disclosure Obligation Would Apply to Many Transactions with Institutional and Other Sophisticated Customers.

Although the 100 bond / $100,000 par amount threshold will generally capture retail trades and not institutional trades, institutional and other sophisticated investors often transact at the $100,000 par amount level.[57] For this reason among others, SIFMA strongly urges the exclusion of transactions with institutional and other sophisticated investors from any confirmation disclosure obligation with specific price references using existing FINRA and MSRB definitions.[58] While the Proposals aim to provide additional information to retail investors, they specifically recognize that they could capture some transactions for institutional accounts.[59] Calculating the price differential figure and making customer confirmation disclosure to these types of institutional and other sophisticated investors is well beyond the policy objectives of the Proposals. Recent SEC and GAO reports have emphasized that institutional investors have an abundance of pricing information already accessible and rely on

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[56] *See, e.g.*, District Bus. Comm. for District No. 5 v. MMAR Group, Inc., Complaint No. C05940001, 1996 NASD Discip. LEXIS 66, at *39 (Oct. 22, 1996) ("[T]he size of a transaction is an important factor to consider in determining the mark-up or the mark-down and . . . the percentage mark-up or mark-down should decline as the size of the transaction increases."); In re Century Capital Corp., Exchange Act Rel. No. 31203, 1992 SEC LEXIS 2335, at *8 n.10 (Sept. 21, 1992) (noting that a mark-up above 5% may be reasonable if size of total transaction is small and total compensation is reasonable), *aff'd* 22 F. 3d 1184 (D.C. Cir. 1994); In re Gateway Stock & Bond, Inc., Exchange Act Rel. No. 8003, 1966 SEC LEXIS 194, at *8 (Dec. 8, 1966) (setting aside an NASD finding of unfair pricing in which a mark-up of 7.3% was charged "where only 10 shares" were sold to the customer); MSRB Rule G-30, Supplementary Material .02(b) ("To the extent that institutional transactions are often larger than retail transactions, this factor may enter into the fair and reasonable pricing of retail versus institutional transactions.").

[57] The Proposals' use of the term "100 bonds" should be clarified to simply refer to the par or face amount. Referring to "bonds" in $1,000 increments is a type of trader jargon that may present unforeseen (and unnecessary) interpretative difficulty for certain instruments. Referring to a bond's par or face value is more precise and would avoid any such difficulty.

[58] *See infra* Part III.C.

[59] For example, the MSRB Regulatory Notice states that "[t]he proposal categorizes a transaction involving 100 bonds or fewer or bonds in a par amount of $100,000 or less as a retail-size transaction. However, this approach may not necessarily capture every retail trade and may, in some instances, capture some small trades executed on behalf of an institutional customer." MSRB Regulatory Notice at 9-10.

TRACE and EMMA data on existing data feeds,[60] and therefore do not have a need for this sort of pushed disclosure.

Moreover, obliging a member firm with a customer base consisting entirely of institutional and other sophisticated customers to comply with an expressly retail-directed disclosure imperative simply because a transaction involves bonds with a $100,000 par value serves no apparent regulatory purpose. Yet any trading by an institutional dealer of bonds in a par amount of $100,000 with an institution would trigger the need to adopt the full panoply of operational and system changes implicated by the Proposals. Such an obligation would be inconsistent with the claim made in the Proposals that they would not have a significant impact on the institutional market for municipal securities.[61]

As described in Part III.C, SIFMA has a specific proposal to exempt institutional transactions using existing standards and definitions. But this particular issue also highlights the need for a more targeted solution and suggests that FINRA and the MSRB should consider how to make better use of the TRACE and EMMA platforms, currently contemplated enhancements such as public user accounts, and related technological innovations such as push notices to voluntary subscribers. These alternatives would avoid unnecessary costs to member firms and the provision of meaningless disclosure to certain investors while allowing retail customers who desire additional pricing data to request near real-time alerts or notices, by CUSIP or otherwise.

G. As Proposed, the Confirmation Disclosure Obligation Would Present Substantial Operational Challenges Related to the Design and Implementation of Matching Instruction Logic.

The Proposals would present enormous operational challenges related to their implementation – challenges that do not appear to have been fully considered. The Proposals would require substantial technical systems and programming changes, as well as coordination among third party providers at the outset and on an ongoing basis. Unnecessarily complicated matching logic compounds these challenges. This structure and the related interdependencies would require significant investments of time and money and significantly outweigh any potential benefit to retail customers.

In addition, the Proposals do not consider the substantial operational challenges concerning the confirmation statement delivery process, particularly in light of

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[60] *See e.g.*, GAO Report to Congressional Committees, Municipal Securities, Overview of Market Structure, Pricing, and Regulation, GAO Report No. 12-265 Municipal Securities (Jan. 2012), at 20-27.

[61] MSRB Regulatory Notice at 11 ("Notably, because the proposal would apply to customer trades for 100 bonds or fewer or bonds in a par amount of $100,000 or less, the disclosure requirement should not have a significant impact on the institutional market for municipal securities.").

initiatives to shorten the settlement cycle. Exchange Act Rule 10b-10, MSRB Rule G-15, and FINRA Rule 2230 require that a broker-dealer that effects a transaction in the account of a customer must 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. 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 bonds, and unit investment trusts ("UITs") from T+3 (trade date plus three days) to T+2 (trade date plus two days).[62] Once achieved, DTCC has recommended a pause and further assessment of industry readiness and appetite for a future move to T+1.[63] The tension between the Proposals' greater disclosure requirements, which can only be added at the end of the trade day, on customer confirmation statements and a shorter settlement cycle adds further complexity and operational risk to this process.

1. The Proposals present substantial technical and programming challenges to their implementation.

Implementing the Proposals would present substantial technical and programming challenges. Placing the proposed information on trade confirmations would be a complicated task. Confirmations already draw on multiple sources of static and dynamic data. For example, trade confirmations obtain information about the security from the security master file, about the customer from the customer master file, and about the trade from the trade file. In addition, the generation of confirmations requires various computations, including accrued interest, yield and price, and total money. The final confirmation includes all the above mentioned information combined from the various sources into a single document.

The Proposals would require firms to add additional information about the reference transaction, perform computations on the price difference between the reference transaction and the customer trade, and print the reference transaction price and the difference between it and the customer trade price on the confirmation, along with the customer trade price – all of which would require costly and complex modifications to firms' systems. These proposed requirements would be especially burdensome in situations in which the reference transaction(s) and the customer trade are not easily associated with each other based on similarities in time or size.

2. The Proposals would require member firms to coordinate and rely on third parties for data necessary for compliance.

Information needed to generate compliant confirmations may reside with different entities, further complicating compliance efforts. Certain information may be

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62 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).

63 *Id* at 2.

with the introducing broker, other information may be with the clearing broker, and other information may be with vendors servicing either one. For example, clearing brokers would need to rely on introducing brokers to specify the reference transaction and corresponding information for those firms using their own order management systems. Introducing firms would need to ensure that at least two new fixed fields could be populated and transmitted to their clearing firms in an acceptable format. Clearing brokers (or self-clearing firms) would then need to ensure that these fixed fields are added to the trade record and stored in a fashion that allows use by downstream systems. Systems that generate trade confirmations must be programmed to acknowledge these two new fields (for both COD and non-COD accounts) and populate them to a particular location on the confirmations. As confirmations have become increasingly crowded over the years, space reserved for trailer information would need to be reallocated.

Although the Proposals do not address this point, presumably the new required disclosures would need to be capable of correction, which is also a complicating factor. Clearing firms would need to allow correspondents to view and correct the new fields – requiring storage of numerous versions in the clearing firm's trade history database. Changes made by introducing firms would need to be passed along to the master books and records database. Correspondent firms would need to re-program their own system to ingest and review the changed format of daily standard files received from the clearing firm.

Nor do the Proposals address the obligations that a member firm would have in the event of a cancellation or re-billing of a reference transaction. If a new transaction confirmation would be required, systems at both the introducing firm and the clearing firm would need to have fixed links between the two (or more) separate transactions with re-issue protocols developed. (The potential for customer confusion upon receipt of a re-issued confirmation that changes only the reference price seems particularly acute.)[64]

3. Because "reference transactions" are not limited to riskless principal transactions, the Proposals would force member firms to navigate an overly complicated – and at times conflicting – matching methodology.

The Proposals would force member firms to navigate an overly complicated – and at times conflicting – matching methodology because reference transactions are not limited to riskless principal transactions. By design, this convoluted methodology suggests that the price differential is not readily determinable and therefore is inconsistent with one of the justifications for the specific recommendation in the SEC

64 *See infra* Part III.F for further discussion of cancellations and corrections.

Municipal Report that the Proposals cite in support.[65] Complex issues may arise under the various methodologies for determining the reference price, as described in the Proposals. Under certain circumstances, the Proposals specify a "last in first out" methodology.[66] Under other circumstances, the Proposals specify an average pricing methodology.[67]

The application of these methodologies to situations in which there is significant buying and selling activity at varying prices and varying size would become quite complex. The Proposals fail to contemplate that it may not be possible to program such methodologies with a high degree of certainty as to accuracy. It is also not clear how these computations would be made, and what disclosure would be included on the customer confirmation, if the customer trade was executed in partial fills and provided to the customer at one confirmation at an average price.

In addition, the Proposals could be read as imposing an obligation to create an automated matching engine for use with confirmation disclosure. SIFMA believes that member firms that engage in a relatively small amount of bond trading should be able to comply with any confirmation disclosure obligation manually, rather than through the use of automated identification of reference transactions and computation of the difference in price between it and the customer trade. If FINRA or the MSRB intend the Proposals to require automated matching systems, such a requirement should be explicitly proposed and separately subjected to robust cost-benefit analysis.

III. IF A NEW CONFIRMATION DISCLOSURE OBLIGATION WITH SPECIFIC PRICE REFERENCES IS TO BE EXPLORED, ALTERNATIVE FORMULATIONS WOULD BETTER ACCOMPLISH THE DESIRED REGULATORY OBJECTIVE – BUT SIFMA BELIEVES THE COSTS ALSO OUTWEIGH THE PURPORTED BENEFITS IN THESE ALTERNATIVE FORMULATIONS.

A. Any New Confirmation Requirement Must be Uniform in Design and Operation as Part of an Overall Approach to Consistency in Rulemaking.

Although the Proposals promised a "coordinated approach to potential rulemaking," they use different formulations that invite unnecessary ambiguity and differing interpretation. The companion Proposals appear designed to operate in an identical fashion – with the MSRB even referencing FINRA's thirteen examples – yet they use different terms and organization. For example, the MSRB proposal uses the

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65 SEC Municipal Report at 148 (tying recommended confirmation disclosure to the "readily determinable" markup on riskless principal transactions); MSRB Regulatory Notice at 4 (citing the SEC Municipal Report as the basis for the Proposal); FINRA Regulatory Notice at 3 (same).

66 *See, e.g.*, MSRB Regulatory Notice at 11; FINRA Regulatory Notice at 6.

67 *See* FINRA Regulatory Notice at 5.

term "reference transaction" to refer to the same category of same day transactions that the FINRA proposal describes similarly but using different words and without definition.[68] The FINRA proposal defines the term "Qualifying Size" to refer to the same size criteria that the MSRB proposal details in slightly different wording.[69] The MSRB proposal applies to trades "effected" as a principal, while FINRA's proposal applies to trades "executed" as a principal.[70] The FINRA proposal requires disclosure of the "differential between . . . the price to the member and the price to the customer" while the MSRB proposal requires disclosure of the "difference in price between the reference transaction and the customer trade, expressed as a percentage of par" – which seems the same, but creates totally unnecessary ambiguity.[71]

In the context of potential customer confirmation disclosure requirements, there is no justification for differences in structure and terminology. While differences in the markets for corporate and municipal debt securities often compel differing approaches to regulation, no purpose would be served by differently worded rules that are designed to operate identically. Unnecessary differences in formulation or terminology can result (and regrettably have resulted) in divergent regulatory approaches and interpretive guidance over time – which, in turn, increase the risk of noncompliance and the need to develop overlapping policies. Unnecessarily divergent

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[68] The MSRB proposal states, "A *reference transaction* generally is one in which the dealer, as principal, purchases or sells the same security that is the subject of the confirmation on the same date as the customer trade." MSRB Regulatory Notice at 8 (emphasis added). By contrast, the FINRA proposal states, "Specifically, 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 to the customer would be required." FINRA Regulatory Notice at 3.

[69] FINRA states, "The rule would define '*qualifying size*' as a purchase or sale transaction of 100 bonds or less or bonds with a face value of $100,000 or less, based on reported quantity, which is designed to capture those trades that are retail in nature." FINRA Regulatory Notice at 3 (emphasis added). By contrast, the MSRB states, "The proposal categorizes a transaction involving 100 bonds or fewer or bonds in a par amount of $100,000 or less as a retail-size transaction." MSRB Regulatory Notice at 21.

[70] *Compare* FINRA Regulatory Notice at 17, *with* MSRB Regulatory Notice at 21.

[71] The FINRA proposal states, "(3) with respect to a sale to (purchase from) a customer of Qualifying Size involving a corporate or agency debt security, where 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 where the size of the principal transaction(s) executed on the same trading day would meet or exceed the size of the customer transaction: (A) the price to the member; (B) the price to the customer; and (C) *the differential between the two prices* in (A) and (B)." FINRA Regulatory Notice at 17 (emphasis added). The MSRB proposal states, "the confirmation shall include: . . . (2) the difference in price between the reference transaction (as defined in paragraph (a)(vi)(I) of this rule) and the customer trade, expressed as a percentage of par." MSRB Regulatory Notice at 21.

approaches to trade reporting of transactions executed on or through an ATS is a recent example.[72] The failure to pursue cost effective solutions and to coordinate approaches between regulators (including uniform rules where reasonable) prevents operational efficiencies and inflates cost structures for dealers. Such regulatory failures only serve to reduce a dealer's ability to provide products and services in the most cost effective manner. Unlike the need to vary approaches to secondary trading execution obligations and fair pricing in the market for municipal and corporate debt securities, operational instructions concerning customer confirmation disclosure should be uniform and precise.[73] Whenever possible, including here, the SEC and SROs should seek to minimize unnecessary differences in regulatory obligations that serve the same or similar objective. Indeed, FINRA's rulebook consolidation effort was a multi-year exercise in eliminating unnecessarily dissonant, conflicting, or duplicative regulatory obligations. There is no apparent justification for the differences between the Proposals and they should be made identical.

B. Any Confirmation Disclosure Obligation with Specific Price References Should Apply Only to Riskless Principal Transactions with Retail Investors To Avoid Investor Confusion and To Ensure Greater Consistency with Current Obligations for Equity Transactions.

The Proposals as currently structured would capture both at risk and riskless principal trades. SIFMA believes, however, that any confirmation disclosure obligation with specific price references should be limited to those trades with retail investors in which the dealer does not incur market risk, i.e., truly riskless principal trades. To be clear, SIFMA strongly favors an approach that uses TRACE and EMMA to increase price transparency. Disclosure of dealer compensation on even riskless principal trades would still require enormously costly build-outs and changes to operational back office systems, cross-platform challenges, and changes to existing front-end systems and practices, all of which led the SEC to withdraw similar proposals in the past. For these reasons, SIFMA believes that the benefits of any such proposal would be far outweighed by the extraordinary costs of implementation. Disclosure of mark-ups or mark-downs on riskless principal trades, however, would appear to potentially have several advantages over the Proposals. First, the disclosure of dealer compensation on riskless principal trades with retail investors is at least consistent with SEC recommendations in this area as well as the purpose of the Proposals – to provide retail customers with information about dealer compensation. Second, it would avoid retail customer confusion by providing information related to the trade being confirmed, not information about other, unrelated trades as the

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[72] *See, e.g.*, FINRA Regulatory Notice 14-53, which unnecessarily diverged from an entirely reasonable MSRB approach to the same issue involving alternative trading systems.

[73] *See, e.g.*, MSRB Notice 2014-02 (Feb. 19, 2014) (detailing an effort to "propose a best-execution rule that is generally harmonized with FINRA Rule 5310 but tailored to the characteristics of the municipal securities market").

Proposals would otherwise require. Third, riskless principal disclosure would avoid the confusion inherent in the identification of other types of reference transactions.

1. Riskless principal transactions should be classified using an established definition, which requires offsetting orders.

A riskless principal transaction should be regarded as the functional equivalent of an agency trade, in which no principal risk (other than settlement risk) attaches to the dealer effecting the transaction. It is particularly important that risk transactions not be regarded as "riskless" solely because of their timing, or definitional ambiguities about what constitutes an order in the debt securities markets. Dealers often acquire debt securities in the expectation that they will meet known or anticipated customer interest, and customer transactions involving those securities may be executed shortly after a dealer acquires a position, in the same face amount, in a manner that resembles a "matched" or "crossed" transaction. However, such expectations of customer interest are not "orders," and until the security is sold, the dealer is entirely at risk. Underscoring this longstanding distinction, a leading treatise authored by former SEC Chief Economist Larry Harris defines "orders" as "trade instructions" that "specify what traders want to trade, whether to buy or sell, how much, when and how to trade, and, most important, on what terms."[74] In short, orders are actionable instructions to transact and any need to "firm up" or obtain customer assent to particular terms is inconsistent with an order as such.

The SEC has previously emphasized the importance of an order in hand as a predicate to a riskless principal transaction:

> In the respects relevant here, a trade on a riskless principal basis should be treated similarly to an agency transaction, in which a firm may retain no more than a commission computed on the basis of its cost. As we have noted, a riskless principal transaction is the economic equivalent of an agency trade. Like an agent, a firm engaging in such trades has no market making function, buys only to fill orders already in hand, and immediately "books" the shares it buys to its customers. Essentially the firm serves as an intermediary for others who have assumed the market risk.[75]

The existing provision of the SEC's confirmation rule applicable to certain riskless principal trades in equity securities by non-market maker dealers also emphasizes the need for offsetting orders. Exchange Act Rule 10b-10(a)(2)(ii)(A) applies to circumstances in which a "broker or dealer [that] is not a market maker in an equity

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[74] LARRY HARRIS, TRADING AND EXCHANGES: MARKET MICROSTRUCTURE FOR PRACTITIONERS 68 (2003).

[75] In re Kevin B. Waide, Exchange Act Rel. No. 30561 (Apr. 7, 1992).

security and, if, after having received an order to buy from a customer, the broker or dealer purchased the equity security from another person to offset a contemporaneous sale to such customer, the broker or dealer sold the security to another person to offset a contemporaneous purchase from such customer."[76] FINRA trade reporting rules also recognize the importance of offsetting orders as a predicate to a "riskless principal transaction."[77]

2. Disclosure of dealer compensation on riskless principal trades, not on at-risk trades, is more consistent with the SEC's recommendation and the Proposals' stated regulatory purpose.

Disclosure of the difference between the customer trade price and the reference transaction price on riskless principal trades is closest to the type of markup disclosure that the SEC has previously proposed and to the recommendation in the SEC Municipal Report.[78] As SIFMA understands the Proposals, the policy objective behind the confirmation disclosure requirement is to help bond investors understand the amount of dealer compensation in circumstances in which the amount of mark-up is "readily determinable."[79] In this regard, the SEC has stated that "[b]ecause riskless principal transactions are very similar, as a practical matter, to agency transactions, and the amount of the mark-up or mark-down is readily 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."[80]

The recommendation included in the SEC Municipal Report was limited to disclosure of the mark-up or mark-down on riskless principal transactions in order to provide customers information about dealer compensation. As the SEC Municipal Report pointed out, in the context of such trades, the mark-up or mark-down is "readily determinable" – an acknowledgement that alternatives would be more complicated and

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[76] *See also* Exchange Act Rule 3a5-1(b) ("[T]he term riskless principal transaction means a transaction in which, after having received an order to buy from a customer, the bank purchased the security from another person to offset a contemporaneous sale to such customer or, after having received an order to sell from a customer, the bank sold the security to another person to offset a contemporaneous purchase from such customer.").

[77] As recently as 2010, the MSRB also proposed to define a "riskless principal transaction" as "a transaction in which, after receiving an order from a customer, the dealer purchased the security from another person to offset a contemporaneous sale to such customer or, having received an order to sell from a customer, the dealer sold the security to another person to offset a contemporaneous purchase from such customer." MSRB Regulatory Notice 2010-10 (Apr. 21, 2010).

[78] SEC Municipal Report at 148.

[79] FINRA Reg. Notice 14-52 at 3 n.5 (citing SEC Municipal Report).

[80] SEC Municipal Report at 148.

potentially confusing to investors. The Report also explained that limiting such disclosure to riskless principal transactions would be "comparable" to existing Rule 10b-10 disclosure for certain equity transactions.[81] In fact, given the current state of corporate and municipal bond transaction reporting on TRACE and EMMA, any new confirmation disclosure requirement with specific price references ought to focus on the set of readily auditable riskless principal trades:

> In the past, limitations on the data reported for municipal securities transactions may have made it difficult to identify riskless principal transactions, for purposes of compliance with – and enforcement of – a rule requiring disclosure of markups or markdowns on such transactions. These limitations are no longer present in today's market, as pricing data on municipal securities transactions is reported soon after execution. Thus, we already have the data necessary to identify riskless principal transactions.[82]

3. Riskless principal transactions can be more reasonably identified but a disclosure requirement will still require significant technology and compliance expense to implement.

The disclosure of mark-ups or mark-downs on riskless principal trades most closely identifies dealer compensation, the information that the SEC believes is germane to customers. A riskless principal disclosure requirement is likely to necessitate the development of order tracking systems together with compliance surveillance and monitoring programs to ensure riskless principal transactions are properly identified in such systems or otherwise flagged in existing systems. Attempts to match customer trades to reference transactions as described in the Proposals would necessarily require an ex post analysis that would result in the disclosure of, at best, an approximation of dealer compensation that would risk investor confusion.[83] Simple disclosure of the difference in price between transactions executed in the same security at a prior point on the same day risks inaccurately treating any difference in price among transactions on the same day as a "mark-up" – something entirely at odds with FINRA mark-up rules and guidance and MSRB fair pricing rules. For example, the MSRB's Report on Secondary Market Trading in the Municipal Securities Market noted that "paired-trade differentials and total customer-to-customer differentials . . . generally do not equate to the formal concepts of 'mark-up' and 'mark-down,' . . . and generally would not be suitable for making direct comparisons to individual

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81 SEC Municipal Report at 148-49.

82 Commissioner Michael S. Piwowar, Remarks at the 2014 Municipal Finance Conference presented by The Bond Buyer and Brandeis Int'l Business School, Boston, Massachusetts (Aug. 1, 2014).

83 *See supra* Part II.A.

transactions in the current market."[84] There are still differences between agency disclosure and riskless principal disclosure that could cause customer confusion, the resulting costs of which still would need to be carefully considered. For example, in a riskless principal trade between two customers, each customer would receive the disclosure of the entire difference between the buy and sell price. This disclosure differs significantly from the typical agency transaction disclosure, where each customer confirmation would generally disclose the amount of commission paid just by that customer.

4. The identification of riskless principal transactions would avoid confusion inherent in identifying other types of reference transactions.

Identification of riskless principal transactions is less confusing and less uncertain than the identification of reference transactions that may occur at any time during the day and that may not be related in any meaningful commercial way to the customer trade. Traders would know whether trades are riskless or not, and could classify them as such, or firms could otherwise identify them at the time of trade. Classifications could be surveilled through order memoranda or related contemporaneous transaction documentation to determine whether riskless principal trades have been properly identified for disclosure of the reference transaction price on the trade confirmation. Firms' supervisory and compliance programs could be designed to test and verify the status of close-in-time executions.

Absent a limitation to riskless principal transactions, there is a risk that credit events will occur between the two (or several) legs of the matched transactions subject to the confirmation disclosure obligation as currently proposed. Customers may conclude that the difference in price is entirely a mark-up (which is indeed the implication of the disclosure), when in fact some portion of it would reflect a change in the bond's value or prevailing market price. FINRA and the MSRB have long acknowledged that credit events and news can have a significant and immediate impact on bond values, and permit dealers to consider these developments when assessing prevailing market prices.

Although SIFMA believes that a retail riskless principal disclosure requirement would impose enormous costs and burdens that would still outweigh the benefits – especially in light of the suggested alternative to promote greater usage of existing transparency platforms – any further regulatory pursuit of a price specific disclosure requirement should entail a reproposal with a focus on disclosure of dealer compensation solely in the context of riskless principal trades.

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[84] MSRB, Report on Secondary Market Trading in the Municipal Securities Market (July 2014).

C. Any Confirmation Disclosure Obligation With Specific Price References Should Be More Carefully Tailored To Apply Only to Retail Customers.

Institutional and other sophisticated customers often transact in bonds with a par value of $100,000. Accordingly, the "qualifying size" (FINRA) or threshold for providing pricing reference information (MSRB) should be changed to 99 bonds or fewer or $99,999 or less to avoid the substantial number of non-retail transactions at the $100,000 level.[85] FINRA has previously used "less than $100,000" as a standard for identifying retail bond transactions, instead of the proposed "$100,000 or less" metric.[86] In particular, 72.8 percent of transactions in municipal securities involve $50,000 or less in face amount. An additional 12.5 percent of transactions in municipal securities involve $50,001 - $100,000 in face amount.[87] Accordingly, setting the threshold at $99,999 or less would trigger the disclosure requirement in approximately 80 percent of all transactions with a reference transaction.

In addition to establishing more appropriate quantity thresholds, any confirmation disclosure obligation with specific price references should also use defined terms to exclude institutional and other sophisticated investors. Institutions and other sophisticated customers also regularly transact in quantities below $100,000 par amount when exiting orphan positions or accumulating a larger, desired position incrementally. Moreover, institutions and other sophisticated investors have multiple dealer relationships that provide additional insight into bond prices and the fixed income market more generally. For these reasons among others, an additional improvement on the approach taken by the Proposals to limit application of the disclosure requirement to retail transactions would be to also exclude transactions from the requirement that are with a defined set of institutional customers and customers recognized by statute as having a high level of financial sophistication and/or investable assets.[88] The Proposals are appropriately focused on the need (if any) for additional confirmation disclosure for retail bond investors. For a variety of reasons, institutional and other sophisticated investors do not need the type of disclosure called for by the Proposals – a point acknowledged in the SEC Municipal Report:

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[85] As set forth above at note 57, SIFMA urges FINRA and the MSRB to avoid the use of trader jargon that equates one bond with $1,000 in par or face amount.

[86] *See* Exchange Act Release No. 73623, 79 Fed. Reg. 69,905, 69,907 (Nov. 24, 2014) ("FINRA TRACE data shows that from 2007 through 2013, retail-sized transactions (*defined to mean trades with a face value of less than $100,000*) in corporate bonds increased approximately 97 percent to about 16,000 daily trades.") (emphasis added).

[87] MSRB, Report on Secondary Market Trading in the Municipal Securities Market (July 2014), at 22 (Figure III.C).

[88] "The proposal categorizes a transaction involving 100 bonds or fewer or bonds in a par amount of $100,000 or less as a retail-size transaction. However, this approach may not necessarily capture every retail trade and may, in some instances, capture some small trades executed on behalf of an institutional customer." MSRB Regulatory Notice at 9-10.

> Although institutional investors vary widely in size and sophistication, the larger ones tend to have access to a variety of sources of municipal securities pricing information. This pricing information can include indicative quotes provided by their municipal bond dealer networks and post-trade transaction information provided by vendors and others. Institutional investors also may directly employ analysts, traders, and other professionals who are experienced in using the available informational tools and making independent pricing judgments.[89]

Existing FINRA and MSRB rules and interpretations, specifically MSRB Rule G-8(a)(xi) and FINRA Rule 4512(c) (defining "institutional account"), as well as Investment Company Act Section 2(a)(51) (defining "qualified purchaser"), provide readily available classifications that dealers have already integrated into their business operations. These are the rules that are used to distinguish between retail and non-retail customers in many contexts, and regulators should maintain a consistent approach to making such distinctions. Whether by reference to an "institutional account" or "qualified purchaser," each of these terms reflects a regulatory or congressional determination that investors so classified are sufficiently sophisticated and/or resourced that they are unlikely to rely heavily on dealers to make their investment decisions. Moreover, it is operationally complex and prone to error to have different ways of seeking to distinguish between retail and non-retail customers. Accordingly, these pre-existing classifications should be used to avoid an unnecessary disclosure obligation to institutional and other sophisticated investors.

FINRA and MSRB should further clarify, whichever criteria are ultimately used to classify institutional and other sophisticated customers, that they should be applied at the parent account level, not at the sub account level. For example, transactions with investment advisers in amounts exceeding any qualifying size (whether $100,000 par value as proposed, or the more appropriate $99,999 level) or allocated to retail customers of the investment adviser, should not be subject to the proposed confirmation disclosure obligations. It would be enormously complex and potentially impossible for dealers to allocate various portions of an institutional block trade into retail customers' respective components. (For example, a purchase of $500,000 face amount of a bond by an investment manager on behalf of advisory clients will be booked as allocated and confirmed at the sub account/end customer level, potentially as ten, $50,000 transactions.) The investment adviser or other institution making the transaction decision has access to pricing information, and so

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[89] SEC Municipal Report at 121-122. *See also*, GAO Report No. 12-265, Municipal Securities: Overview of Market Structure, Pricing and Regulation (Jan. 2012) at 20-27 ("individual investors generally have less information and expertise to assess prices than institutional investors.")

disclosures aimed at retail investors should not be required.

D. Any Confirmation Disclosure Obligation Should Allow Separately-Operated Trading Desks To "Match" Only their Own Trades.

When proprietary, retail, and institutional trading desks operate independently, their transactions should not be disclosed in a manner that suggests integration. To the extent a member may set up bona fide aggregation units of bond trading desks, modeled on the aggregation units in Section 200(f) of Regulation SHO, 17 C.F.R. § 242.200(f), it should not need to identify trades in one aggregation unit as reference transactions for customer trades in another aggregation unit. The object of the Proposals would not be advanced by disclosing the price differential between unconnected transactions. For example, if a retail trading desk sells a customer 80 bonds at 99 from inventory and on the same day the same firm's proprietary trading desk is able to acquire 1,000 bonds at 97.5 in a separate transaction, disclosure of the 1.5 point price differential would convey no meaningful information about dealer compensation (the object of the proposal) and would in fact mislead the customer. By allowing dealers to disclose "matched" trades by aggregation unit and dealer MPID, the confirmation disclosure would be consistent with existing TRACE and EMMA transaction reporting obligations.

In addition, any confirmation disclosure requirement should be neutral as to business model. For example, some full service broker-dealers have institutional and retail trading desks within the same member. Others have their retail and institutional desk in different members. By applying the requirement at the aggregation unit level, the Proposals would operate the same and require the same, comparable disclosure, regardless of the structure of the business, even in situations where one aggregation unit sourced liquidity through another aggregation unit.

E. Dealers Should Be Permitted To Disclose a Standard Sales Credit or Mark-up in Lieu of the Confirmation Disclosure of the Proposal.

While SIFMA opposes the mandatory adoption of commission or mark-up schedules generally, in circumstances in which a dealer has an existing sales credit or mark-up schedule that details the compensation that the firm and its salesperson receive for retail bond transactions, disclosure of that schedule to customers via a link on the confirmation or of the actual markup on the confirmation, should satisfy the policy objective behind the requirement. Accordingly, firms should be given the option to choose to disclose mark-ups in this manner in lieu of making the confirmation disclosure (or observing any matching methodology) contemplated by the Proposals. SIFMA reiterates that this approach should be considered as an alternative option available to dealers that transact in this fashion and not as a mandate to create or adopt retail mark-up or commission schedules (which SIFMA has and continues to oppose).

F. Any New Confirmation Requirement Should Not Require Confirmations To Be Canceled and Corrected Due Solely to a Change to the Reference Transaction Price.

In the event any disclosure requirement uses a reference transaction concept, the re-billing or cancellation of a reference transaction should not occasion the issuance of a replacement confirmation for the matched trade unless its terms have also changed. At times, the trade that included the reference price may be cancelled or corrected in a manner that either changes the reference price or that obviates the trade as a reference price trade (for example, if the trade is cancelled outright or was accidentally booked as a buy but needed to be rebooked as a sell). In these instances, SIFMA requests confirmation that Firms would not be required to re-confirm the customer trade.

IV. IN LIGHT OF THE CONSIDERABLE BURDENS ACKNOWLEDGED TO BE ASSOCIATED WITH PROPOSALS, FINRA AND THE MSRB HAVE NOT CONDUCTED AN ADEQUATE COST / BENEFIT ANALYSIS.

As currently formulated, the Proposals may violate the Exchange Act, as well as other federal laws governing SRO rulemaking. These laws require, among other things, that FINRA, the MSRB, and the SEC consider the 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. Other federal statutes require the consideration and quantification of the effect that the Proposals would have on small business entities, including broker-dealers and issuers of debt securities, and restrict the adoption of new recordkeeping obligations absent compliance with certain procedural requirements. At the urging of the SEC, both FINRA and the MSRB have adopted policies that govern this type of economic impact assessment, designed to facilitate the agency review required by federal law. Indeed, FINRA and the MSRB should not even propose a rule without some meaningful, substantive evidentiary basis – however preliminary – to conclude that the benefits would outweigh the estimated costs and burdens, and not simply evaluate assumed or speculated benefits against invited comments on costs. Yet nothing in the Proposals suggests that FINRA or the MSRB has even begun to compile a record that would either permit an informed analysis of these assessments by public commenters or allow an appropriate review by the SEC offices charged with conducting the agency's review pursuant to Exchange Act Section 19(b)(2). (Part IV.A.)

Nor has there been any apparent consideration of the less burdensome alternatives that are available using existing infrastructure to accomplish the stated regulatory objective. For years the published policy of FINRA and the MSRB has been to use the TRACE and EMMA platforms to increase bond pricing transparency. The costs of these platforms must be considered in the context of a change of approach to accomplishing the same or similar objectives. (Part IV.B.) These costs, coupled with the enormity of the costs and burdens that would be associated with the Proposals

as currently formulated, simply cannot be justified by the putative benefits claimed to accompany the proposed disclosure. (Part IV.C.)

A. By Policy, 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.

Exchange Act Sections 15A(b)(9) and 15B(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]." Exchange Act Section 3(f) also 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." To aid in this consideration, SROs must provide a detailed statement regarding the burden on competition that may be imposed by a proposed rule. In the context of a proposed rulemaking, the obligation to justify the new obligation is on the SROs, and they cannot satisfy the requirement to analyze potential costs by simply punting questions to the affected entities.

Each of FINRA and the MSRB has adopted and published formal policies governing economic impact analysis.[90] These policies are quite clear in terms of the obligation to gather, analyze, and publish quantified costs and to catalog the evidence relied upon to arrive at those figures. For example, the MSRB policy provides, in pertinent part:

> The SEC Guidance stresses the need to attempt to quantify anticipated costs and benefits even when the available data is imperfect. In order to quantify costs and benefits, data is necessary. At an early stage in the rulemaking process, the rulemaking staff should identify data sources that would potentially assist in quantification and should attempt to obtain the necessary data. In its public comment process, the MSRB should describe the measurement approach used, include references and descriptions of data used and specify the timeframe analyzed.[91]

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[90] FINRA, Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking (Sept. 2013); MSRB, Policy on the Use of Economic Analysis in MSRB Rulemaking (Sept. 2013).

[91] MSRB, Policy on the Use of Economic Analysis in MSRB Rulemaking (Sept. 2013), at 2. *See also* Mark Schoeff, Jr., *Ketchum: What this industry is missing when it comes to CARDS*, Investment News, Dec. 5, 2014 ("'We think the benefits are absolutely obvious, but we recognize it's always our obligation to look closely at costs,' said Richard Ketchum,

The requirements of the FINRA and MSRB policies are referenced in the Proposals, in corresponding sections that address costs and benefits. Yet nowhere in either regulatory notice is there any description of efforts that were taken or are contemplated to quantify costs, to evaluate the specific costs of "firms developing a new system to capture and deliver required disclosures" (FINRA), or to identify "relevant empirical evidence available" (MSRB).

While the Proposals contain a number of recitals about the need to weigh costs and benefits, there are no statistics – not a single one – that purport to quantify any costs of the proposed requirement, even while acknowledging that "the proposal would impose burdens and costs on firms." As a result, the Proposals balance unmeasured, aspirational benefits against unquantified costs, and preliminarily conclude that the benefits are justified:

> FINRA believes that, in trades in the same security where the firm and the customer trades occur on the same trading day, requiring firms to disclose the price to the firm, the price to the customer, and the corresponding differential will provide customers with comprehensive and beneficial information, while balancing the costs and burdens to firms of providing disclosure.[92]

Such a statement presupposes an analysis of data that has been vaguely requested, not yet received, and not the result of any formulated or published methodology. It is so far from the requirements imposed by statute and policy that it suggests an effort to justify a regulatory decision already made – the very opposite of the approach required by FINRA and MSRB policies. When contrasted with the cost-benefit analysis undertaken by the SEC in connection with the most recent amendments to the confirmation rule,[93] the efforts undertaken to date to analyze the Proposals are wholly inadequate and would not withstand administrative or judicial scrutiny.

In addition to the inadequacy of FINRA and the MSRB's cost-benefit analyses to date, neither of the Proposals details any action to comply with the Paperwork Reduction Act of 1995[94] or the Regulatory Flexibility Act.[95] Specifically, any approval by the SEC of the Proposals as currently formulated would create a new "collection of information" requirement by imposing a "recordkeeping requirement" on ten or more persons to identify and track reference transactions and corresponding

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Financial Industry Regulatory Authority Inc. chairman and chief executive.").

92 FINRA Regulatory Notice 15-52 at 10.

93 Mutual Fund Distribution Fees; Confirmations, 75 Fed. Reg. 47,064, 47,126 (Aug. 4, 2010).

94 44 U.S.C. §§ 3501-3510

95 5 U.S.C. § 605(b).

price differentials.[96] The Proposals do not contain any representation that the proposed collection of information has been or will be submitted to the Office of Management and Budget for review of this new recordkeeping requirement. Nor has FINRA or the MSRB explained whether – or on what basis – they would be able to certify to the SEC that the Proposals would not have a significant economic impact on small business entities, such as regional broker-dealers with limited bond trading operations.[97]

Not only are the Proposals lacking in a numbers-driven assessment of the costs and burdens that would be borne by member firms, they do not address or even attempt to measure the potential impact on bond market liquidity. Such an endeavor is entirely within the capability of FINRA and the MSRB, as the recent commission and publication of secondary market analyses by experts retained by the MSRB demonstrates. Such an examination would be consistent with the prudence undertaken by FINRA and the MSRB in the context of trade dissemination and reflect that the risks of even small reduction in retail bond market liquidity could easily injure investors far more seriously than any benefit to be gained by the Proposals.

B. In Light of the Two Decades and Millions of Dollars Spent Pursuing Fixed Income Price Transparency Initiatives through the TRACE and EMMA Platforms, FINRA and the MSRB Must Justify with Particularity a Decision To Ignore Less Costly Alternatives Using This Existing Infrastructure.

Neither FINRA nor the MSRB has explained why, at a time when the bond markets have never had greater transparency, the Proposals – more sweeping and broader than a proposal rejected on four prior occasions based on cost / benefit analyses – is now necessary. Although the Proposals question the willingness of retail investors to "actively seek out information and make inferences as to which transactions are most relevant,"[98] they provide no statistics about usage of TRACE and EMMA or the portion of retail investors who access their accounts electronically or otherwise access the internet for investments or banking. Indeed, until the issuance of the Proposals in November, public pronouncements were replete with figures demonstrating the effectiveness of these platforms.[99]

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96 44 U.S.C. § 3502(3)(A)(i).

97 5 U.S.C. §§ 605(b) (certification requirement), 603(a) (initial regulatory flexibility analysis requirement).

98 MSRB Regulatory Notice at 13.

99 *Compare* SEC Municipal Report at 35 n.194 ("The Staff understands that the MSRB's EMMA website has received over 20 million page views per year, and the MSRB is forecasting over 25 million page views in 2012."), *and* MSRB, 2008 Fact Book at 1 (noting that EMMA had "put timely market information directly at the fingertips of retail investors" and "vastly improved on the information that retail investors could readily obtain"), *with* MSRB Regulatory Notice at 13 ("[U]sing EMMA to conduct the relevant pricing analysis

The benefits of the Proposals are acknowledged to be incremental given the amount of pricing information already available to retail investors.[100] In fact, the TRACE and EMMA information is more useful to retail bond investors than the disclosure specified in the Proposals, because the TRACE and EMMA data is available pre-trade, whereas some retail investors will not receive the proposed disclosure until approximately three days after the trade; the TRACE and EMMA data includes comparative data from multiple market participants, whereas the proposed disclosure includes comparative data from only one market participant; and the TRACE and EMMA data includes a rich data set of trade prices across time, whereas the proposed disclosure is largely a single data point. The MSRB has characterized the Proposal as one that simply would "provide investors with information generally already publicly available" on EMMA.[101] Accordingly, the resources that will be spent to comply with the Proposals, both initially and over time, would be better used to enhance retail use of TRACE and EMMA.

FINRA and the MSRB must include among the costs of the Proposal the funds that have already been spent on infrastructure and maintenance of their price dissemination platforms that will not be used to accomplish the stated objective. Since 1994, both FINRA and the MSRB have pursued long–range plans to design, build, maintain, and enhance centralized platforms for the dissemination of pricing information to retail investors. Any number of rule proposals and fee assessments since 1994 have been justified on the basis that these platforms would be enhanced over time to make an ever-increasing amount of price data available to investors electronically and free of cost in lieu of alternatives such as mailings or confirmation disclosure.[102] FINRA and the MSRB also need to compare the incremental benefit of the Proposals given the existence of pricing data available through TRACE and EMMA, to the total cost of the Proposals, as well as to the alternatives that may be available to enhance retail investors' use of TRACE and EMMA.

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requires that customers actively seek out information and make inferences as to which transactions are most relevant. Conducting this type of pricing analysis places a burden on customers.").

[100] MSRB Regulatory Notice at 13 ("Currently, retail customers may use EMMA to gain insight into the market for the securities they trade by viewing recent trade prices in the same or similar securities in similar quantities.").

[101] MSRB, 2014 Annual Report at 6.

[102] For example, the MSRB justified the substantial costs associated with EMMA by its contemplated use as the primary price dissemination vehicle for retail investors. *See* MSRB SR-2009-02 (Mar. 29, 2009), at 59 (stating that the MSRB "believes that the benefits realized by the investing public from the broader and easier availability of disclosure and price transparency information in connection with municipal securities that would be provided through the EMMA primary market disclosure service and EMMA trade price transparency service would justify any potentially negative impact on existing enterprises from the operation of EMMA.").

FINRA and the MSRB must also explain why they did not entertain alternatives that would make greater – and perhaps more innovative – use of TRACE and EMMA. For example, the MSRB has published plans for "free public user accounts" that would allow investors to "manage EMMA alert settings."[103] Presumably these accounts and alert settings would operate in a similar fashion to push notices that are commonplace and accessible on a variety of electronic devices. Neither FINRA nor the MSRB has explained why investors could not receive alerts of the sort currently proposed using this type of user account based on existing trade reports. Millions of bank depositors and credit card customers sign up to receive customized alerts on a daily basis. And neither FINRA nor the MSRB has explained why TRACE and EMMA could not be designed to send to interested investors emails with trading data by CUSIP, or be designed to allow firms to deliver to customers simple, one-click hyperlinks to access CUSIP-specific trading information.

C. The Costs and Burdens Associated with Implementation and Compliance Would Far Outweigh the Potential Benefits.

Although neither FINRA nor the MSRB appear to have performed any analysis of the actual costs of system enhancement necessary for the proposed disclosure requirement, the most recent SEC-required amendments to Rule 10b-10 disclosures for certain mutual fund distribution fees included a detailed cost-benefit analysis. In order to implement that requirement – which was far less complicated than the Proposals and did not involve the design of matching algorithms – the SEC estimated that clearing firms alone would incur one-time burdens in excess of $180 million and that total one-time burdens would exceed $258 million.[104]

Substantial system enhancements would be required of introducing firms, clearing firms, and vendor licensors of front-end systems to implement the Proposals. The costs would be disproportionately high for small and regional broker-dealers with limited bond trading operations or with overwhelmingly institutional customer bases. These entities compete with larger multi-service firms that may be better able to absorb the costs of infrastructure development and maintenance. Based on discussions with SIFMA member firms, preliminary assessments classify the work required by the proposals as requiring a large information technology project involving high complexity. Preliminary assessments suggest costs limited to firm-specific technology for introducing firms would range from $500,000 for a smaller firm to as much as $2.5 million for large diverse organizations. Preliminary assessments suggest that clearing firms may need to expend in excess of 5,000 man hours. Clearing firms would need to alter point of entry systems to accept two new fixed fields; enrich the fields and add them to the trade record in accordance with all other trade facts to be published downstream; enable confirmation systems to acknowledge the new fields, using either

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[103] MSRB, Long-Range Plan for Market Transparency Products (Jan. 27, 2012) at 8.

[104] Mutual Fund Distribution Fees; Confirmations, 75 Fed. Reg. 47,064, 47,126 (Aug. 4, 2010).

pre-formatted locations or trailer fields; modify corrections processes to permit correspondent firms to view and correct the new fields; and update daily activity reports to include the new values and fields. Although SIFMA does not currently have assessments from front-end vendor licensors, their costs are very likely to be substantial as well in light of experience with prior modifications to address regulatory reporting requirements.

The claimed benefits are acknowledged to be incremental[105] and less desirable[106] to increased use of TRACE and EMMA by retail bond investors. Neither FINRA nor the MSRB have evaluated alternatives that may achieve greater use of TRACE and EMMA by those "who may not know of EMMA or may not have the time or wherewithal to conduct their own transaction research" but who are nevertheless presumed to benefit from the proposed disclosure.[107] As discussed above, the cost of even a modified proposal limited strictly to riskless principal transactions significantly outweighs the purported benefits – something found repeatedly by the SEC in prior rulemakings.

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[105] *See, e.g.*, MSRB, 2014 Annual Report at 6 (acknowledging that the Proposal "would provide investors with information generally already publicly available" on EMMA).

[106] Confirmation of Transactions, Exchange Act Rel. No. 34962, 59 Fed. Reg. 59,612, 59,616 ("Price transparency [through TRACE and EMMA], if fully developed, will provide better market information to investors on a timely basis . . . .").

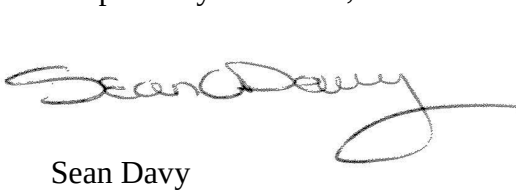
[107] MSRB Regulatory Notice at 7; *see also* FINRA Regulatory Notice at 2 ("Although knowledgeable industrious customers could observe these trading patterns retrospectively using TRACE data, our understanding is that retail customers do not typically consult TRACE data.").

CONCLUSION

SIFMA thanks FINRA and the MSRB for the opportunity to comment on the Matched Trade Proposals. SIFMA fully supports the objective to enhance bond market price transparency by putting more information into the hands of retail investors. To this end, SIFMA urges FINRA and the MSRB to withdraw the Proposals in favor of an approach that directs retail investors to the extensive pricing information available free of charge on TRACE and EMMA. As formulated, the Proposals risk confusing retail investors, present unworkable challenges in application, and threaten burdensome operational challenges while imposing unjustified costs and burdens than alternatives that would embrace TRACE and EMMA. SIFMA believes that – if FINRA and the MSRB were to require a new confirmation disclosure obligation with specific price references – alternative formulations would better accomplish the desired regulatory objective. Nonetheless, the enormous costs and burdens associated with even these alternative formulations significantly outweigh the purported benefits. Finally, SIFMA notes that nothing in the Proposals suggests that FINRA or the MSRB have conducted an adequate cost-benefit analysis as required under federal law and their own policies. The astronomical costs and burdens associated with implementation and compliance with the Proposals far outweigh the unproven benefits.

SIFMA welcomes the opportunity to discuss the Proposals, SIFMA's comments, and the various alternatives that would best serve our shared objectives. If you have any questions, please do not hesitate to contact the undersigned or Paul Eckert and Bruce Newman, SIFMA's outside counsel at Wilmer Cutler Pickering Hale and Dorr LLP, at (202) 663-6000.

Respectfully submitted,



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January 20, 2015

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

Re: Disclosure of Pricing Reference Information – Regulatory Notice 2014-20

Dear Mr. Smith:

Standard & Poor's Securities Evaluations Inc. (SPSE) is an independent evaluated pricing provider and a part of S&P Capital IQ, a division of McGraw Hill Financial, Inc. SPSE appreciates the opportunity to provide the Municipal Securities Rulemaking Board ("MSRB") with comments on Regulatory Notice 2014-20, regarding the disclosure of a reference price when dealers are acting as a riskless principal for retail size transactions in fixed income securities. The MSRB is proposing that for same-day, retail size principal transactions for the purchase or sale of 100 bonds or less or bonds with a face amount of $100,000 or less, dealers disclose on the customer confirmation the price paid by the dealer and the differential between the price paid by the dealer and the price paid for the same security by the customer. While the proposed disclosure contemplates using actual market prices, the proposal also requests comments on the use of alternatives to using market prices, including among other things, prices provided by independent external pricing services. SPSE would like to take the opportunity to provide its views on why it believes the MSRB should consider the use of evaluated prices provided by independent pricing providers as another source of prices to be used by member firms in computing the differential in the price to the customer and the price to the dealer.

SPSE supports transparency in the fixed income markets that promotes efficiencies and greater investor protections. SPSE has been a leader in providing evaluated prices for corporate bonds and municipal bonds and other fixed income securities and derivatives for more than 40 years, and presently evaluates more than 150,000 corporate securities and 1.5 million municipal securities on a daily basis. SPSE's evaluated pricing service supports operations throughout the financial services industry with client profiles that include dealers, mutual funds, hedge funds, custodians, insurance companies, and financial advisors.

SPSE strongly believes that a reference price proposal should contemplate the use of an independent evaluated price when a market reference price is unavailable or would be deemed to be unreliable for other reasons. A number of reasons may impact the availability of a viable reference price. For example, same-day reference prices may become stale due to timing, increased volatility, decreased liquidity, or the lack of a corresponding order. Adding to the challenge in determining the appropriateness of a reference price are the nuances involved with the pricing of retail-size blocks, otherwise known as "odd lots", and the potential for significant price dispersion as lot sizes change by even minimal amounts. SPSE believes further that using evaluated prices from an independent provider in certain situations could be beneficial to both

dealers and customers, especially when a market reference price is not available due to unforeseen market events or when the last available market price is too old to be reliable.

The cornerstone of SPSE's evaluated pricing service involves its ability to directly observe market inputs and where observable inputs are limited or unavailable, its ability to use proprietary tools that assist it in providing an evaluated price that is based on other indirect, but relevant, market factors and inputs. Grouping bonds with like characteristics enables SPSE to observe other market factors, thereby allowing it to provide evaluated prices across groupings of securities with similar trading characteristics, furthering price transparency reflective of the fixed income market.

SPSE'S Retail Pricing Service

In addition to providing its evaluated prices to institutional clients, SPSE recently implemented an additional pricing service that delivers adjusted pricing for retail (odd-lot) sized trades. Historically, independent pricing providers have provided prices at institutional levels but accounting standards, transaction requirements, and general regulatory and risk management concerns all indicate that it is time for more reflective odd-lot pricing. The dispersion of prices across different lot sizes can be significant so that a single reference (or evaluated price) may not be enough but instead, a range of values might better serve the evolving market needs, including the retail fixed income market. These values represent a lower-price boundary and an upper-price boundary, and are established through an analysis of observed spreads on both direct observables and comparable bonds that are sectored and grouped based on similar market behaviors and descriptive attributes.

Summary

SPSE appreciates the opportunity to submit comments on MSRB Regulatory Notice 2014-20. SPSE believes that there may be a benefit to a review of the feasibility and appropriateness of utilizing independent pricing services to support the MSRB's initiative. Independently sourced pricing could mitigate some of the operational challenges involved with establishing a reference price. SPSE believes that independent sources can play a supporting role in this and other price transparency initiatives. We look forward to working with the MSRB and the dealer community on this critical initiative.

Sincerely,

Gregory Carlin

THOMSON REUTERS

January 16, 2015

Via: pubcom@finra.org
msrb.org/CommentForm

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

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

Re: Response to the Requests for Comment from FINRA and the MSRB on Proposed Rules to Require Confirmation Disclosure of Pricing Information in Fixed Income Securities Transactions (Regulatory Notices 14-52 and 2014-20).

Dear Ms. Asquith and Mr. Smith:

Thomson Reuters appreciates the opportunity to comment on the rule proposal by the Financial Industry Regulatory Authority ("FINRA") outlined in Regulatory Notice 14-52, which would require member firms to disclose the price to the member, the price to the customer and the difference between the two prices on customer confirmations for a subset of retail fixed income transactions. Through BETA Systems, Thomson Reuters[1] offers a complete suite of products that enable retail and institutional brokers to manage the daily tasks of their front, middle and back office operations. With more than 30 years of industry knowledge and hands-on experience, Thomson Reuters partner with some nineteen clearing firms and over 300 introducing broker-dealers to address their unique business and regulatory requirements.

Thomson Reuters believes this approach presents a significant amount of processing change and may not accurately reflect transaction details to investors. FINRA has presented a method for providing same-day pricing disclosures, which could be achieved in back office processing with significant code and processing changes. However, as a Service Provider, Thomson Reuters is concerned that a batch process will match trades by defined business rules, which could result in the pricing disclosure being irrelevant to the actual transactions. We illustrate our concerns through examples provided in the following section. We recommend that FINRA consider a process in which the pricing disclosure is actually related to the security transaction "at the time "of the transaction – the current standard in FINRA Rule 2121 and MSRB Rule G-30, which requires broker-dealers to take into consideration circumstances related "at the

[1] 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. Headquartered in New York it employs approximately 57,800 people around the world and operates in over 100 countries. For more information about Thomson Reuters, please go to www.thomsonreuters.com. For more information about BETA Systems, please go to www.thomsonreuters.com/beta-systems.

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time" of transaction for fair prices and commissions. We believe EMMA and TRACE provides this information, since it is near real time. Firms could provide customers information related to their execution upon request, including detailing the price defined by a standard method or a fair market estimate. This would provide the needed customer disclosure and information and reduce the potential of making non relevant data as relevant. This is also similar to the Best Execution and Order Routing disclosures requirements.

Thomson Reuters details concerns below, and offers comments responsive to specific questions posed in Regulatory Notices 14-52 and 2014-20.

The Operational Complexities of the Proposals will Result in Reporting Information to Investors that is not Relevant to Their Transactions

Proposed revisions to FINRA Rule 2232 and MSRB Rule G-15 would require broker-dealers to disclose the price to the member, the price to the customer and price differential for transactions of qualifying size, when the member acts as principal on the same trading day in an amount that would meet or exceed the size of the customer transaction. Given the proposed scope of the amendments, Thomson Reuters is particularly concerned about three aspects from an operational and technical standpoint.

Determining what retail transactions qualify for the disclosure and what price to disclose as the broker-dealers price will be operationally complex and technically challenging. First, a broker-dealers's streetside executions and retail customer transactions are not related or aggregated systematically throughout the trading, meaning firms will have to build complex logic to compare all activity in dealer inventory and customer accounts in a particular security at the end of a trading day to determine whether the firm's dealer activity exceeded the aggregate customer activity in that security. Determining the appropriate member's price will be equally challenging because firms and service providers will have to develop functionality to evaluate the dealer and customer activity at the end of the trading day to determine which member price methodology is required (i.e. weighted average price, LIFO, closest in time proximity). This functionality will require a complicated tax lot-like system to link specific dealer activity and member price with customer activity for confirm reporting purposes, and account for the timing and amount of activity across multiple accounts and systems.

It was valuable that FINRA provided 13 examples in the regulatory notice, which the MSRB referenced in their Notice. However, these examples did not take into account the complexity associated with transaction processing. Generally a firm utilizes multiple order management systems and has several proprietary trading accounts, and their customers could be executing multiple transactions in the same fixed income securities, which will complicate the matching process and we believe this could result in irrelevant prices being legitimatized as the price the firm purchased or sold the security

Thomson Reuters offers the following examples to illustrate more complex trading scenarios that would require complicated matching logic in order to comply with the proposals:

Example 1:
10:00:00 AM Firm A, Trader 1 (INV Acct 1234), purchases 500 XYZ bonds from Dealer Y at $100 for $500,000
10:00:00 AM Firm A, Trader 2 (INV Acct 7890), purchases 50 XYZ bonds from Dealer Z at $102 for $51,000
10:00:15 AM Firm A, sells 30 XYZ bonds to Client A at $101.50 for $30,450

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Example 2:
10:00:00 AM Firm A, Trader 1 (INV Acct 9876), purchases 100 XYZ bonds from Dealer Y at $100 for $100,000
10:00:00 AM Firm A, Trader 2 (INV Acct 1234), purchases 50 XYZ bonds from Dealer Z at $102 for $51,000
10:00:15 AM Firm A, sells 75 XYZ bonds to Client A at a price of $101.50 for $76,125
10:00:15 AM Firm A, sells 30 XYZ bonds to Client B at a price of $101.50 for $30,450

Example 3:
09:30:00 AM Firm A, Trader 1 (INV Acct 2345), purchases 100 XYZ bonds from Dealer Y at $99 for $99,000
10:00:00 AM Firm A, Trader 2 (INV Acct 9876), purchases 50 XYZ bonds from Dealer Z at $102 for $51,000
10:00:00 AM Firm A, sells 80 XYZ bonds (INV Acct 2345) to Client A at a price of $101.50 for $81,200
10:10:00 AM Firm A, Trader 3 (INV Acct 4567), purchases 100 XYZ bonds Dealer Z at $101 for $101,000
10:15:00 AM Firm A, Trader 1(INV Acct 6543), purchases 100 XYZ bonds from Institution X at $100 for $100,000
10:20:15 AM Firm A, sells 30 XYZ bonds (INV Acct 6543)) to Client A at $101.50 for $30,450
10:00:15 AM Firm A, sells 50 XYZ bonds (INV Acct 4567) to Client B at a price of $101.50 for $50,750

The following illustrate instances in which the disclosure would be misleading or confusing to clients:

Example 4: Closest in Time Proximity Methodology
9:35:00 AM Firm A sells to Client A from existing inventory 50 XYZ bonds at $101 for $50,500
1:30:00 PM Negative news for XYZ
2:15:00 PM Firm A buys 100 bonds from Dealer Z at $93 for $93,000
2:30:00 PM Firm A sells to 50 XYZ bonds to Client B at $95 for $47,500

- Client A would receive a confirm reflecting dealer price of $93, a customer price of $101 and a price differential of 8.
- Client B would receive a confirm with a dealer price of $93, a customer price of $95, and a price differential of 2.

Example 5: Last In-FirstOut Methodology
10:00:00 AM Firm A buys 100 XYZ bonds at $99 for $99,000
10:15:00 AM Firm A sells to Client A 25 XYZ bonds at $101 for $25,250
10:18:00 AM Firm A sells to Client B 25 bonds at $101 for $25,250
1:00:00 PM Negative News for Company XYZ
1:15:00 PM Firm A buys 50 XYZ bonds at $92 for $46,000
2:00:00 PM Firm A sells to Client C 50 XYZ bonds at $94 for $47,000

- Client A and Client B will receive confirms disclosing dealer price of $92, customer price of 101, with price differential of 9 (prevailing market price and contemporaneous cost was $99 at time of customer transactions).

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- Client C will receive confirm disclosing dealer price of $92, customer price of $94, with price differential of 2.

Example 6: Weighted Average Price Methodology
10:00:00 AM Firm A buys 75 XYZ bonds at $98 for $73,500.
10:45:00 AM Firm A sells 75 XYZ bonds to Client A at $101 for $75,750
1:00:00 PM Negative news for XYZ
1:30:00 Firm A buys 75 XYZ bonds at $92 for $92,000
1:45:00 Firm A sells 75 XYZ bonds to Client B at $94 for $70,500

- Client A receives confirm disclosing a weighted average price of 95, customer price of 101, and price differential of 6.
- Client B receives confirm disclosing a weighted average price of 95, customer price of $94, and a markup of -1.

Example 7: Different confirms for same transaction
Day 1 – 10:00:00 AM Firm A purchases100 XYZ bonds at $99 for $99,000.
Day 1 – 11:30:00 AM Firm A sells Client A 50 XYZ bonds at $101 for $50,500
Day 2 – 2:00:00 PM Firm A sells Client A 50 XYZ bonds at $101 for $50,500

- Client A receives a confirm for Day 1 reflecting dealer price of $99 (LIFO), customer price of $101 and markup of 2.
- Client A receives a confirm for Day 2 reflecting customer price of $101 (even though transactions are identical, client receives different confirmations).

Example 8: Trade Corrections
Day 1 – 10:00:00 AM Firm A purchases 75 XYZ bonds from Dealer X at $97 for $72,750
Day 1 – 10:30:00 AM Firm A purchases 75 XYZ bonds from Dealer Z at $100 for $75,000
Day 1 – 11:00:00 Am Firm A sells 75 XYZ bonds to Client A at $100 for $75,000.
Day 1 – 2:00:00 PM Firm A sells 50 XYZ bonds to Client B at $101.50 for $50,750

- Client A receives a confirm reflecting dealer price of $100 (LIFO), customer price of $100 and price differential of 0.
- Client B receives a confirm reflecting dealer price of $100 (LIFO), customer price of $101.50, and differential of 1.5.

Day 2 – 9:00:00 AM Registered Rep makes trade correction for Client B, increasing quantity from 50 to 75 XYZ bonds.

- Trade correction would cause Day 1 Firm activity to equal customer activity, which would require firm to use the average price methodology. ***Would Firm A be required to issue a new confirm to Client B reflecting a dealer price of:***
  - $100 based on calculation used the prior day; or
  - $98.50 based on weighted average price?
- ***Would Client A have to be issued a corrected confirm if Firm is required to report $98.50 as dealer price?***

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Given these examples Thomson Reuters foresees additional processing logic that was not considered in the Regulatory Notices, and anticipates identifying additional challenges as analysis continues. Thomson Reuters believes the industry and regulators need to thoroughly evaluate all the potential scenarios to fully understand the complexity of reporting pricing disclosures and the accuracy of the disclosures under each scenario. As discussed above, automated processes are based on defined business rules which must account for unique events and complexities. Automated processes would facilitate processing client disclosures but at the expense of causing misleading price comparisons and legitimizing information that is irrelevant to the client's transaction. Importantly, Registered Representatives will not be able to disclose the actual markup to the client at the time of the transaction because the actual dealer price that will be the basis of the disclosure will not be calculated until the automated processes run after market close.

To reduce operational complexity and implementation costs, and allow firms to tailor their disclosure practices to their business models and technology infrastructure, FINRA and the MSRB should adopt a consistent and workable standard that:

- Allows firms to provide their retail customers fair and accurate price disclosure ;
- Determines dealer price using one consistently applied standard, rather than having to consider timing of activity and the extent to which dealer activity meets or exceeds customer activity;

Finally, service providers and print vendors, working with member firms will have to analyze existing confirm file layouts to ensure that information can be properly passed without causing unintended consequences downstream. As more fully detailed below, FINRA and the MSRB should consider alternatives to mitigate this risk and complexity by leveraging data that is already reported to TRACE or RTRS.

Regulatory Coordination

Thomson Reuters appreciates the manner in which FINRA and the MSRB have coordinated thus far on their respective confirm disclosure proposals, and stresses that the rules should diverge only to the extent necessary to account for differences between the municipal and corporate/agency markets. As a general matter, this type of coordination results in effective rulemaking, cost effective implementation for broker-dealers and regulators, and reduces implementation, technology and market risk. Thomson Reuters encourages FINRA and the MSRB to continue working with other regulators to address common regulatory concerns.

Thomson Reuters would also like to stress that FINRA and the MSRB should consider ways to consolidate rulemakings and implementation that impact common products, systems or processes. For instance, FINRA has released several proposals that impact various aspects of TRACE reporting and other proposals to increase market transparency. [2] Similarly, the MSRB has proposed transparency initiatives, along with its Long Range Plan for Market Transparency.[3] As FINRA and the MSRB consider the revisions proposed in Notices 14-52 and 2014-20, a critical objective should be to align

[2] Regulatory Notice 14-53 (Trade Obligations in TRACE-Eligible Securities); SR-FINRA-2014-050 (requiring a non-member affiliate indicator); and FINRA's announced proposal to require an indicator when a transaction does not reflect a commission or markup.

[3] Regulatory Notices 2014-14 (Enhancements to Post-Trade Transaction Data Disseminated Through a New Central Transparency Platform) and 2013-14 (Concept Release on Pre-Trade and Post-Trade Pricing Data Dissemination through a New Central Transparency Platform); Long-Range Plan for Market Transparency Products (http://www.msrb.org/msrb1/pdfs/Long-Range-Plan.pdf).

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implementation with other fixed income and market transparency initiatives. Consolidating related rulemakings in this way is more efficient for regulators and broker-dealers, and with this efficiency, broker-dealers can continue to invest in products, services and technologies that further benefit investors.

Assessment of Costs and Benefits – Economic Impact Analysis

Thomson Reuters believes that the costs and time to implement the proposed rule will be a significant undertaking, given it requires integration between multiple systems, new tax- lot like accounting application for matching trades and billing purposes and multiple changes downstream for processing, which will ultimately increase processing time for these transactions. As a point of comparison, the S.E.C. estimated in the 2010 proposal related to mutual fund disclosures that the one-time costs for broker-dealers to modify confirms was approximately $1.1 million (or aggregate cost of $180.7 million)..

Broker-dealers, FINRA and the MSRB have invested millions of dollars over the last several years in TRACE and RTRS reporting to capture additional detail for dealer and customer activity in fixed income securities. Thus, FINRA and the MSRB should work with the industry to enhance the existing TRACE Market Data and EMMA websites, which already aggregate and make publicly available significant amounts of trade related and pricing information. Moreover, as FINRA and the MSRB move forward with their market transparency initiatives, they will be in possession of more data which could be beneficial to investors if disclosed publicly. Leveraging the existing transaction repositories allows for consistency in disclosure, reduces burdens on investors by bringing the information together in two primary sources, and will arguably be of greater benefit to more investors by showing transaction costs and other reference information that investors will find useful. Broker-dealers could include links to the FINRA and MSRB facilities to further reduce the burden on investors. These alternatives must be considered before requiring broker-dealers to incur the significant costs of disclosures, which would only disclose a price based on a business rule, not a true indicator of the actual event (price).

Response to Specific "Request for Comment"

Thomson Reuters offers comments to the following questions raised in Regulatory Notices 14-52 and 2014-20:

MSRB and FINRA Question 2. What kinds of costs would this requirement impose on firms, including the anticipated costs to firms in developing and implementing systems to comply with the proposal?

Response: Thomson Reuters anticipates that firms and service providers would incur costs in four distinct areas. Firms and service providers will have to engage technical resources to develop functionality to comply with identification and reporting requirements. Additionally, modifications will have to be made confirm programming and layouts. Technical and subject matter experts will also have to coordinate internal technical changes with print vendors and support end to end testing with other order management systems, service providers, and print vendors. Finally, firms will have to develop internal systems to ensure that they are able to adequately supervise and oversee the new requirements. An approach that aligns the FINRA and MSRB proposals to every extent possible will likely reduce implementation and maintenance costs.

MSRB Question 3. For what time period should the dealer's trades be disclosed? Is the same trading day standard appropriate in light of the objectives, costs and benefits of the proposal

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Response: Requiring the disclosure on any activity which occurs in the same trading day makes the proposal overly complex and costly to implement. As the MSRB notes, "as the time period between trades increases, the degree to which the price of the reference transaction will be helpful to the customer may decrease." Instead, the rule should be based on the existing standard in MSRB Rule 30, which requires broker-dealers to take into consideration circumstances "at the time" of transaction for fair prices and commissions.

MSRB and FINRA Question 4. For which transactions should pricing disclosures be made?

Response: Requiring disclosure on any activity which occurs in the same trading day makes the proposal overly complex and costly to implement. FINRA should limit scope to retail activity with a definition based on existing account or customer demographics that dealers already capture as books and records requirements rather than trade size. For example, the rule could apply to accounts that do not qualify as an Institutional Account[4] under Rule 4512 or accounts of natural persons.[5]

MSRB and FINRA Question 5. Are there alternative forms of disclosure or methods to achieve the objectives of the proposal and are they better suited that the proposal?

Response: Before adopting the rule, FINRA and the MSRB should review the current investor protections under Rule 2121 and G-30 or enhance FINRA's Market Data and MSRB's EMMA websites to disclose more pricing information publicly and consolidating this with the other reference and market data that is already consolidated and disseminated by FINRA and the MSRB. By leveraging the existing Regulators' facilities, information can be disclosed in a common form accessible in two locations for corporate bonds, agencies and municipal securities.

FINRA Question 7. Should the concept of a "riskless principal" transaction be used in place of the proposed concept, and, if so, can "riskless principal" be defined in a manner that minimizes concerns that market participants would avoid the proposed disclosure requirements?

Response: While limiting scope to riskless principal activity may give the investor a more accurate representation of the costs to execute their particular transaction, Thomson Reuters is concerned that many operational challenges will persist, including the ability to accurately match riskless principal transactions real-time. Thomson Reuters does not believe that this will appreciably reduce the implementation cost or complexity for broker-dealers and service providers.

FINRA Question 9/MSRB Question 8. When a firm executes multiple municipal securities transactions as principal, what should be the appropriate methodology or methodologies to use in determining the reference transaction price and differential to be disclosed on the confirmation?

Response: Thomson Reuters believes strongly, as illustrated in the above examples that the proposed methodologies will result in misleading price comparisons and legitimize information that is irrelevant to the client's transaction. FINRA and the MSRB must consider an approach consistent with the "at the time of the transaction" standard of MSRB Rule G-30 and FINRA Rule 2121.

[4] Since the FINRA definition of Institutional Account and the MSRB definition of sophisticated municipal market professional are the same, the rules could be harmonized in this respect.

[5] Natural person indicator will be a new requirement for broker-dealers under the S.E.C.'s money market fund reform and is a proposed requirement for FINRA's Comprehensive Automated Risk Data System.

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FINRA Question 11. Are there other potential effects to markets and market participants of the proposal?

Response:, Thomson Reuters would not be in favor of a pilot program to test potential effects. Cost of implementation is the same without the same level of certainty in the long-term investment, and further strains resources dedicated to other significant regulatory initiatives.

Conclusion

Thomson Reuters believes that the proposed rule is overly complex, may not necessarily achieve FINRA's intended goal of providing greater cost transparency for investors and that the potential costs far outweigh the potential investor benefits. Before submitting the rule for approval, Thomson Reuters requests FINRA to consider a more effective alternative that may have greater benefit to investors. If FINRA determines that confirm disclosures are necessary, Thomson Reuters recommends that FINRA adopt a rule that allows for standardized and consistent application o the regulatory requirements and reduces the likelihood of providing investors with misleading information.

Thomson Reuters appreciates this opportunity to comment on the rule proposal and welcomes the opportunity to further participate in discussions with FINRA and other stakeholders about how to best achieve the proposal's policy goals.

Respectfully Yours,

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January 20, 2015

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RE: 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; MSRB Notice 2014-20 - 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:

Wells Fargo Advisors, LLC ("WFA" or the "Firm") appreciates the opportunity to comment on the Financial Industry Regulatory Authority's ("FINRA") Proposed Rule Requiring Confirmation Disclosure of Pricing Information in Fixed Income Securities Transactions, set forth in Regulatory Notice 14-52 ("Reg. Notice 14-52") and Municipal Securities Rulemaking Board ("MSRB") Notice 2014-20 ("MSRB Notice 2014-20") Request

for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations (collectively, the "Proposal").[1]

WFA is a dually registered broker-dealer and investment advisor that administers approximately $1.4 trillion in client assets. It employs approximately 15,189 full-service financial advisors in branch offices in all 50 states and 3,472 licensed financial specialists in 6,610 retail bank branches in 29 states.[2] WFA is a non-bank affiliate of Wells Fargo & Company ("Wells Fargo"), whose broker-dealer and asset management affiliates comprise one of the largest retail wealth management, brokerage and retirement providers in the United States. Wells Fargo's brokerage affiliates also include Wells Fargo Advisors Financial Network, LLC, ("WFAFN") and First Clearing, LLC, which provides clearing services to 76 correspondent clients, WFA and WFAFN. For the ease of discussion, this letter will use WFA to refer to all such brokerage operations.

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.

INTRODUCTION

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 data for retail investors. As a broker-dealer vested with the responsibility of seeking best execution on transactions for over 7.5 million customer accounts, WFA supports regulatory initiatives that will improve the quality of securities and capital markets for retail investors.

While the Proposal's stated aim is theoretically consistent with FINRA's and MSRB's price transparency objectives, from an operational and implementation perspective, it is irredeemably flawed.[3] The plan to provide retail investors with same day price differential information for certain same-day fixed income transactions via dated confirmation disclosures, while sounding deceptively simple to implement, would in fact require overcoming significant technical hurdles. Moreover, the plan would undermine use of more effective price dissemination tools and provide retail investors with confusing or, at worst,

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[1] 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/web/groups/industry/@ip/@reg/@notice/documents/notices/p601685.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.

[2] Wells Fargo & Company ("Wells Fargo") is a diversified financial services company providing banking, insurance, investments, mortgage and consumer and commercial finance throughout the United States of America and internationally. Wells Fargo has 275,000 team members across more than 80 businesses.

[3] Reg. Notice 14-52, at p. 3.

misleading information.[4] Furthermore, the Proposal represents a paradigm shift away from years of regulatory focus on transparency of contemporaneous market conditions at the time of transaction execution. WFA believes investors are best served by 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.

The Proposal's principal flaws include:

- The Proposal's reporting obligations are cost prohibitive and present operational and technical challenges that would be difficult, if not impossible, to effectively implement.
- The Proposal goes far beyond the recommendations included in the Securities and Exchange Commission's ("SEC" or "the Commission") Report on the Municipal Securities Market[5] and is inconsistent with current Exchange Act Rule 10b-10 requirements.
- The Proposal contradicts years of SEC, FINRA and MSRB policy favoring development of price dissemination platforms as a more effective alternative to confirmation disclosure.
- The Proposal provides a distorted view of dealer compensation and diverts attention away from whether a transaction is effected at a fair price relative to contemporaneous market conditions.

Notwithstanding WFA's objections to the Proposal as currently structured, should FINRA and MSRB move forward, WFA stands ready to assist in developing a workable and efficient means of providing greater price transparency for retail investors. WFA believes there are more narrowly tailored alternatives that present an opportunity for FINRA and MSRB to achieve their stated objectives while addressing many of the issues highlighted in this letter, specifically:

- Continued development and expansion of the Trade Reporting and Compliance Engine ("TRACE") and the Electronic Municipal Market Access ("EMMA"®) price dissemination platforms to provide additional near real-time market information to investors.

[4] The Proposal states that for same-day, retail-size transactions, firms must disclose on the customer confirmation: (1) the price to the customer; (2) the price to the member of a transaction in the same security; and, (3) the differential between those two prices. A "retail-sized transaction" is defined as 100 bonds or less or bonds with a face value of $100,000 or less.

[5] Securities and Exchange Commission Report on the Municipal Securities Market (July 31, 2012), p. 113, *available at*: http://www.sec.gov/news/studies/2012/munireport073112.pdf

- Increased client education to explain how to access and use TRACE and EMMA® along with increased firm usage of links and references to these services in various client communications.
- Confirmation disclosure of riskless principal transaction mark-ups consistent with current Exchange Act Rule 10b-10 disclosure obligations for equity securities.

WFA discusses the challenges presented by the Proposal in greater detail below as well as potential alternatives should FINRA and MSRB determine to move forward.

I. Regulatory Efforts Should Be Focused on Enhancing the Most Effective Methods of Providing Meaningful Price Transparency to Retail Investors.

The Proposal's stated purpose is to enhance disclosure requirements for transactions in fixed income securities that will permit retail investors to "better evaluate their transactions."[6] The policy choices made to ensure retail clients are informed and treated fairly have historically focused on evaluating fixed income transactions against contemporaneous market conditions and establishing price dissemination platforms to promote greater price transparency. WFA believes the Proposal changes the transaction evaluation dynamic and undermines the use of price dissemination platforms by the introduction of a confirmation disclosure that has repeatedly been deemed an inferior alternative.[7] Consequently, WFA believes the Proposal should be withdrawn or, if moved forward, substantially revised.

(a) Focus Should Remain on Value Versus Contemporaneous Market Conditions and Meaningful Disclosure.

As an initial matter, broker-dealers are currently obligated to generally seek the most favorable terms reasonably available in current market conditions for their retail customers' fixed income securities transactions.[8]

This has been a longstanding requirement under FINRA rules[9] and a more recent development under MSRB rules.[10] Historically, MSRB rules required a dealer to provide customers with a "fair and reasonable" price; however, in response to the SEC's 2012 Report on Municipal Securities which recommended certain actions to improve the municipal

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[6] Reg. Notice 14-52, at p.3.
[7] *See* Exchange Act Release No. 33743 (Mar. 9, 1994), 59 FR 12767 (proposing a rule that would have included disclosure of markups for municipal securities transactions); Exchange Act Release No. 15220 (Oct. 6, 1978), 43 FR 47538 (proposing mark-up disclosure for riskless principal trades in municipal securities); Exchange Act Release No. 13661 (June 23, 1977), 42 FR 33348 (proposing mark-up disclosure by non-market makers in riskless principal transactions involving equity and debt securities, but not municipal securities); and Exchange Act Release No. 12806 (Sept. 16, 1976), 41 FR 41432 (proposing mark-up disclosure by non-market makers in riskless principal transactions involving equity and debt securities).
[8] *See* FINRA Rules 5310 and 2121; MSRB Rules G-18 and G-30.
[9] *See* FINRA Rules 5310 and 2121.
[10] *See* MSRB Rules G-18 and G-30.

securities markets,[11] MSRB recently revised MSRB Rule G-18 to explicitly adopt a "best execution" standard for transactions in municipal securities. Moreover, common law duties of best execution have always applied to transactions in municipal fixed income securities.[12] Under common law, when accepting a customer order for execution, the broker-dealer has an implied duty to execute the order in a manner that maximizes the customer's position in the transaction.[13] In all these instances, the regulatory requirements are focused on measuring execution quality in light of contemporaneous market conditions.

WFA does not believe the proposed confirmation disclosure, which includes at-risk as well as riskless transactions, furthers an understanding of contemporaneous market conditions at the time of transaction execution. As currently set forth in the Proposal, however, there is the real possibility a customer may believe the confirmation disclosure represents contemporaneous market conditions or compensation received on riskless transactions. Under this scenario the confirmation disclosure could be thought to portray the prevailing market for the security at the time of execution, which could be inaccurate particularly when the reference trade is not close in time to the customer transaction. Indeed, an intervening market moving event may render the reference price envisioned in the Proposal completely meaningless and misleading.

More customer confusion may result when this information is displayed for only some fixed income transactions while not for others (only disclosed for qualifying transactions). There is also the scenario of a resulting negative spread, which will cause more confusion, particularly if an investor equates the price differential with dealer compensation. Finally, there is a distinct possibility a client could execute a qualifying and a non-qualifying transaction in the same security on the same day. In which case, a client would receive two confirmations, only one of which would disclose a reference price. In other words, the disclosures envisioned in the Proposal may confuse rather than enlighten retail investors. 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 than could any reference price.

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[11] *See* SEC Report on the Municipal Securities Market, p.149.

[12] *See Newton v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 135 F.3d 266, 273 (3d Cir.), *cert. denied*, 525 U.S. 811 (1998) ("[T]he basis for the duty of best execution is the mutual understanding that the client is engaging in the trade – and retaining the services of the broker as his agent – solely for the purpose of maximizing his own economic benefit, and that the broker receives her compensation because she assists the client in reaching that goal."). This case also recognized that the duty of best execution does not "dissolve" when an intermediary acts in its capacity as a principal. *Id.* at 270 n.1 (citation omitted). *See also* Regulation NMS, Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37538 (June 29, 2005) ("A broker-dealer's duty of best execution derives from common law agency principles and fiduciary obligations, and is incorporated in SRO rules and, through judicial and Commission decisions, the antifraud provisions of the federal securities laws."); Exchange Act Release No. 43963 (Feb. 14, 2001) (citing *Newton*, but concluding that respondent fulfilled his duty of best execution). *See also* Payment for Order Flow, Exchange Act Release No. 34902 (Oct. 27, 1994), 59 FR 55006, 55009 (Nov. 2, 1994) (discussing a broker-dealer's duty of best execution in relation to routing orders).

[13] *See Newton*, *supra* note 12, pp. 269-70.

Furthermore, from what can be gleaned from Reg. Notice 14-52 regarding same-day "matched" transactions, at least with respect to corporate bonds, there generally appears to be tight price dispersion for most transactions, with a minority of transactions experiencing wider price spreads. Given existing execution obligations, the likelihood of customer confusion and generally tight price dispersions, rather than imposing an incredibly complex and costly disclosure requirement on all broker-dealers, FINRA and MSRB should first obtain a better understanding of the reasons underlying these outlier price transactions. FINRA and MSRB can then make a more data informed judgment regarding what, if any, new rulemaking may be appropriate.

(b) Price Dissemination Platforms Have Been Deemed A More Effective Alternative to Confirmation Disclosure.

Since at least 1994, the SEC, FINRA and MSRB have favored development of price dissemination platforms as a more effective alternative to confirmation disclosure. WFA believes these platforms have succeeded in making available a wealth of price information at the click of a button and support the continued enhancement of TRACE and EMMA® as a more efficient and effective alternative than the Proposal. Enhancements to these platforms will put more real-time information in the hands of investors as opposed to the provision of data buried in a dated transaction confirmation.

The Commission in the past considered requiring confirmation disclosure of mark-ups for debt securities, yet in each instance determined not to adopt such a requirement. As early as 1976 the Commission requested comment on whether to require disclosure of mark-ups on riskless principal transactions in municipal and corporate debt securities, yet deferred in part due to cost concerns.[14]

In 1994, the last time this issue was considered, the SEC concluded the price dissemination initiative platforms under development offered "more meaningful benefits to investors in the long-term" than the proposed confirmation disclosure.[15] In the withdrawing release the SEC stated "[t]he Commission has deferred adoption of the riskless principal mark-up disclosure proposal in order to ascertain whether the proposed price information systems can provide more meaningful benefits to investors in the long-term and to assess the progress of the industry in developing the proposed systems. Price transparency, if fully developed, will provide better market information to investors on a timely basis (e.g., before the transaction)."[16] Consequently, WFA believes continued enhancements of TRACE and EMMA® would make more information available to more investors and in a more timely manner than the proposed confirmation disclosure.

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[14] Exchange Act Release No. 12806 (Sept. 16, 1976), 41 FR 41432 (proposing mark-up disclosure by non-market makers in riskless principal transactions involving equity and debt securities).
[15] SEC Final Rule, Confirmation of Transactions, Release No. 34-34962; File No. S7-6-94, p. 12
[16] Confirmation of Transactions, Exchange Act Rel. No. 34962, 59 Fed. Reg. 59,612, 59,616 (Nov. 17, 1994) (withdrawing release).

The period since 1994 has witnessed revolutionary technology innovation that has made electronic access to information via the internet widely accessible. Internet usage has become a normal part of everyday life for many investors with near universal mobile access now available. Indeed, the SEC found over five years ago that a majority of investors rely on the internet to help make investment decisions,[17] while more recent survey data found nearly 90% of adults use the internet.[18] FINRA and MSRB should be commended for using this time to successfully build and implement price dissemination platforms that have dramatically increased near real-time price transparency for retail investors to an extent that could hardly have been imagined in 1994.

This development has not come without cost as the investments needed to build and maintain these systems have been substantial. For example, in 2013 alone, FINRA deployed substantially all of the $58 million it collected in transaction fees to support TRACE.[19] Similarly, MSRB expended close to $14 million in 2013 on operations and market information systems, including EMMA®.[20] Moreover, FINRA and MSRB have plans to enhance these systems to provide greater transparency into market prices.

Furthermore, the broker-dealer community has also separately invested tens of millions of dollars to design, build and implement the infrastructure necessary to identify and report the relevant transaction information and build supervisory and oversight systems to support these activities. WFA will need to continue to spend substantial sums to maintain and upgrade its supporting infrastructure as FINRA and MSRB propose new reporting obligations in addition to the Proposal.

Given existing execution obligations coupled with policy choices and investments in price dissemination platforms that have been deemed superior to confirmation disclosures, WFA believes the most appropriate course is to continue to invest in upgrading TRACE and EMMA® to provide more near-real time information to retail investors free of charge. To implement a costly confirmation disclosure method that has previously been deemed inferior, even prior to the rise of the internet age and the implementation of TRACE and EMMA®, is not the best way to put more information in the hands of investors today.

II. The Proposal Is Cost Prohibitive and Difficult, If Not Impossible, to Effectively Implement.

As discussed above, the proposed confirmation disclosure, while appearing benign, in practice would require overcoming significant technical hurdles and a redesign of the confirmation process.

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[17] Investment Company Act, Rel. No. 28584, 74 Fed. Reg. 4,546, 4,560 n.195 (Jan. 26, 2009).
[18] Pew Research Internet Project, Internet Use Over Time, *available at*: http://www.pewinternet.org/data-trend/internet-use/internet-use-over-time/.
[19] FINRA 2013 Year in Review and Annual Financial Report
[20] MSRB 2013 Annual Report

The confirmation process is already a complicated activity that relies on inputs from multiple systems to generate a transaction confirmation that complies with the various 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. All 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.[21]

In addition, transaction confirmations have strayed far beyond the original purpose of providing investors with the terms of the transactions. So much so that simply identifying space to provide additional information is becoming problematic. To add more information as set forth in the Proposal without context has the potential for misinterpretation, is a recipe for confusion and is not the most efficient use of resources.

Pursuant to the Proposal, firms would be required to obtain additional information about a reference security and to conduct calculations on the price difference between the reference trade and the customer trade, and display the reference trade price and the difference between the trade price and the customer trade price on the confirmation, along with the customer trade price. To complicate matters, varying amounts of this information may not be available at the time of the transaction. Redesigning confirmation systems to accurately identify and incorporate relevant post execution information, while theoretically possible, would be technically challenging and require time consuming and expensive system upgrades. Moreover, the potential for a shortened trade settlement process would only further exacerbate technical and programming challenges.[22]

To further complicate matters, the Proposal attempts to incorporate into the confirmation generation process various matching methodologies for determining a reference price. Under certain circumstances a firm is obligated to use a "last in first out methodology" while under different circumstances a firm needs to use an average pricing methodology (or first in, first out (FIFO)). To illustrate the issue, Example 7 in Reg. Notice 14-52, states that where there are multiple firm trades which equal the amount of the customer trade, the firm would be required to disclose on the customer confirmation the weighted average price of the Firm trades to the Firm, the price to the customer and the differential between the two prices.

In Examples 9 and 10, the Firm engages in multiple transactions as principal that form the basis of its transactions with customers but exceed the number of bonds of the customer trade, FINRA expects that the Firm would apply a last in, first out (LIFO) methodology or the closest time proximity depending on whether the client transaction was before or after the

[21] There is also a potential impact to the ID confirmation process, wherein it is possible to have transactions effected for 100 bonds or $100,000 or less via delivery versus payment. The ID confirmation process is a real-time process and if trade information is not available until end-of-day, confirmations may need to be canceled and rebilled to include the price reference information. This could result in downstream impacts.

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

Firm's transaction. The Firm would also be required to disclose on the customer confirmation the price to the Firm of the last or closest transaction, the price to the customer, and the differential between the two prices. These examples only begin to cover various permutations when there are multiple customers and multiple transactions involved and do not consider intervening market events that may make the reference price meaningless. Firms generally do not build and offer positions in fixed income securities on a paired transaction basis. It is also unclear how cancellation and correction would be handled, particularly if the underlying cause is a change in the reference security. In any event, systems would need to be able to digest numerous contingencies that together can cause the design and implementation costs to skyrocket. WFA believes that smaller correspondent firms who do not have automated systems will have an even more difficult time in attempting to meet the Proposal's additional requirements on a manual basis.

WFA's early and quick estimate of the costs to design and implementation of system modifications to comply with the Proposal's requirements is approximately $1.5 million dollars.

WFA believes a fulsome cost benefit analysis needs to consider not only the direct technology upgrade costs associated with the Proposal, but also the context of an industry that is subject to multiple competing regulatory initiatives such as the recent expansion of the Order Audit Trail System, the Consolidated Audit Trail, Blue Sheets, Large Trader, Supplemental Statement of Income and potentially FINRA's proposed Comprehensive Automated Risk Data System. In addition, any cost benefit analysis needs to include the tens of millions of dollars already spent developing TRACE and EMMA® as well as planned improvements to these systems that makes near real-time market pricing information available to nearly all investors free of charge.

The cumulative effect of the Proposal combined with other ongoing regulatory efforts is to unnecessarily siphon a firm's finite resources, squeezing out investments that could otherwise be used to enhance broker-dealer operations, surveillance capabilities and the customer experience.[23]

III. The Proposal Undermines Prior/Current Efforts to Provide Greater Price Transparency for Retail Investors, such as TRACE and EMMA®.

WFA believes there are more narrowly tailored alternatives that present an opportunity for FINRA and MSRB to achieve their stated objectives while mitigating many of the issues highlighted in this letter.

[23] A cost analysis should not ignore the contextual backdrop of an industry with multiple regulatory reporting efforts underway (e.g., Consolidated Audit Trail). *See also* SEC Commissioner Daniel Gallagher, Interview at Security Traders Association Market Structure Conference (Oct. 1, 2014) (supporting a holistic review of market structure).

(a) Expand Current Price Dissemination Systems.

WFA believes TRACE and EMMA® are far more useful to retail bond investors than the disclosures outlined in the Proposal because TRACE and EMMA® data is available pre-trade and post-trade, where the information in the Proposal would not reach the retail investor until roughly three days after the trade. As discussed earlier, the SEC, FINRA and MSRB have favored price dissemination platforms over confirmation disclosure for cost *and* benefit purposes. At a time when internet use is ubiquitous, the most effective use of resources is to focus on enhancing those systems deemed to provide investors with the most timely and useful information.

TRACE was approved by the SEC and implemented in 2002 to specifically address issues of transparency in the bond market. TRACE contains: (1) rules that describe which bond transactions must be publicly reported and when; and, (2) a technology platform that gathers transaction data and makes it available to the public. According to FINRA, TRACE "helps create a level playing field for all market participants by providing comprehensive, real-time access to public bond price information."[24] As noted previously, on a number of occasions prior to TRACE enactment, the SEC considered and rejected confirmation disclosure mark-ups, stating that price transparency initiatives underway by FINRA, specifically referencing TRACE, promised "more meaningful benefits to investors in the long-term" than the proposed confirmation disclosure. [25]

EMMA® is the official repository for information on virtually all municipal securities. EMMA® provides public access to official disclosures, trade data, credit ranges, educational materials and other information about the municipal securities market free of charge. This system houses municipal disclosure documents that provide information for investors about municipal securities, including offering documents for most new offerings of municipal bonds, notes, 529 college savings plans and other municipal securities issued since 1990. With respect to market transparency, EMMA® provides retail customers with real-time prices and yields at which bonds and notes are bought and sold, for most trades occurring on or after January 31, 2005.

WFA is unaware of any current or ongoing issues with lack of information for retail investors in fixed income markets. Further, FINRA has not provided any statistical information that retail investors are unable to obtain relevant pricing information prior to trading fixed income products.

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[24] FINRA,TRACE Fact Book 2013 at 2**.** Items disclosed in TRACE include, but are not limited to: all transactions in a particular CUSIP by date and time, the price of every transaction, information about the quantity of transactions, whether a transaction was with a dealer or customer, information about the bond's yield, and information about the bond and issuer itself that may bear on prices and likely yields.

[25] SEC Final Rule, Confirmation of Transactions, Release No. 34-34962; File No. S7-6-94, p. 12.

WFA believes continued enhancement of TRACE and EMMA®, at a time of near universal access to and use of the internet, is the best means of providing meaningful transparency regarding contemporaneous market conditions to more investors and in a more timely manner than the Proposal's confirmation disclosure of artificial reference price data.

(b) Direct Confirmation Disclosure to Riskless Transactions.

Both FINRA and MSRB have cited the SEC's Report on the Municipal Securities Market and the June 20, 2014, speech given by SEC Chair Mary Jo White as a basis for the Proposal.[26] The Proposal however goes far beyond the recommendations contained in the Report on the Municipal Securities Market and discussed by Chair White. While not ideal, WFA believes a proposal that conforms to the recommendations regarding additional disclosure in "riskless principal" transactions as set forth in the Report and in Chair White's speech would at least be a workable alternative.

Confirmation disclosure of price differentials on riskless principal transactions would simplify the confirmation generation process and provide investors with information unimpeded by hedging or market factors that could lead to misinterpretation of the mark-up information. The confirmation disclosures should be applicable to "riskless principal" transactions as previously set forth by the Commission,[27] wherein the broker-dealer has an "order in hand" at the time of execution. The broker-dealer would have all the necessary information at the time of trade to initiate the confirmation generation process, somewhat simplifying the technical and programming challenges for implementing system upgrades.

The SEC,[28] FINRA[29] and MSRB[30] have all historically recognized the predicate qualification of having an order in hand to appropriately be deemed a riskless principal

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[26] Securities and Exchange Commission Report on the Municipal Securities Market (July 31, 2012), p. 113, *available at*: http://www.sec.gov/news/studies/2012/munireport073112.pdf. In a June 20, 2014 speech, SEC Chair Mary Jo White announced support for additional disclosures to help investors better understand the costs of their fixed income transactions. *See Intermediation in the Modern Securities Markets: Putting Technology and Competition to Work for Investors*, Economic Club of New York, New York, New York, *available at*: http://www.sec.gov/News/Speech/Detail/Speech/1370542122012.

[27] Securities Confirmations, Exchange Act Rel. No. 13661, 42 Fed. Reg. 33,348 (June 30, 1077) (proposing release).

[28] Exchange Act Rule 10b-10(a)(2)(ii)(A) applies to circumstances in which a "broker or dealer [that] is not a market maker in an equity security and, if, after having received an order to buy from a customer, the broker or dealer purchased the equity security from another person to offset a contemporaneous sale to such customer, the broker or dealer sold the security to another person to offset a contemporaneous purchase from such customer."

[29] FINRA Rule 6282(d)(3)(B) ("A 'riskless' principal transaction in which a member after having received an order to buy a security, purchases the security as principal at the same price to satisfy the order to buy or, after having received an order to sell, sells the security as principal at the same price to satisfy the order to sell.").

[30] MSRB Notice 2010-10 (Apr. 21, 2010). MSRB defined a "riskless principal transaction" as "a transaction in which, after receiving an order from a customer, the dealer purchased the security from another person to offset a contemporaneous sale to such customer or, having received an order to sell from a customer, the dealer sold the security to another person to offset a contemporaneous purchase from such customer."

transaction. Moreover, this definition of riskless principal transaction would provide consistency with Exchange Act Rule 10b-10 requirements as applied to equity transactions.

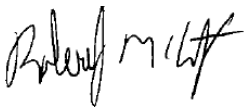
WFA does not believe confirmation disclosure on riskless principal transactions is the ideal solution. Such proposals have been withdrawn in the past because of cost and benefit considerations and still needs to be subjected to a cost-benefit analysis. Even moving forward with confirmation disclosures on riskless principal transactions will still require process changes and, although of lesser cost than the process contemplated under the Proposal, relatively expensive system changes.

Consequently, should FINRA and MSRB move forward with their respective proposals, WFA requests that any further publications are issued via a joint release that contains the same information and use of terms to ensure a standard and consistent approach. This would contain costs, minimize system changes and ensure uniformity in application.

CONCLUSION

WFA appreciates the opportunity to respond to the Proposals issued by FINRA and MSRB. Although WFA believes the Proposal as currently structured should be withdrawn, WFA remains willing to aid FINRA and MSRB in achieving greater price transparency for retail investors. WFA welcomes additional opportunities to respond as the Proposal evolves. If you would like to further discuss this issue, please contact the undersigned at 314-955-2156, or robert.j.mccarthy@wellsfargoadvisors.com.

Sincerely,



Robert J. McCarthy
Director of Regulatory Policy

MSRB
Municipal Securities Rulemaking Board

Regulatory Notice

2015-16

Publication Date
September 24, 2015

Stakeholders
Municipal Securities Dealers, Investors, General Public

Notice Type
Request for Comment

Comment Deadline
November 20, 2015
[Original deadline extended to December 11, 2015 on October 20, 2015]

Category
Uniform Practice; Market Transparency

Affected Rules
Rule G-15

Receive emails about MSRB regulatory notices.

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

[Comment deadline extended on October 20, 2015. *See* Notice 2015-19]

Overview

The Municipal Securities Rulemaking Board (MSRB) is seeking comment on draft rule amendments to require brokers, dealers, and municipal securities dealers ("dealers") to disclose the mark-up or mark-down (collectively "mark-up") on retail customer confirmations for specified principal transactions. The MSRB and the Financial Industry Regulatory Authority (FINRA) have been engaged in ongoing dialogue regarding potential rulemaking in this area. The FINRA Board of Governors has authorized the publication of a regulatory notice requesting comment on a revised FINRA proposal to require firms to disclose pricing information on customer confirmations for trades in corporate and agency securities with non-institutional customers, where the firm's principal trade and the customer trade both occur on the same trading day.[1] The MSRB, in addition to its mark-up disclosure proposal, which is based on a recommendation in the Securities and Exchange Commission's 2012 Report on the Municipal Securities Market ("SEC Report"), is broadly seeking comment on alternatives. These include the MSRB's previous proposal to require dealers to provide pricing reference information on retail customer confirmations

[1] *See* Letter from FINRA to Executive Officers, Update: FINRA Board of Governors Meeting (July 9, 2015), available at: http://www.finra.org/industry/update-finra-board-governors-meeting-13.

for same-day principal transactions in municipal securities,[2] with several possible modifications to that proposal as discussed below.

Comments should be submitted no later than November 20, 2015, and may be submitted in electronic or paper form. Comments may be submitted electronically by clicking here. Comments submitted in paper form should be sent to Ronald W. Smith, Corporate Secretary, Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314. All comments will be available for public inspection on the MSRB's website.[3]

Questions about this notice should be directed to Michael L. Post, General Counsel – Regulatory Affairs, or Saliha Olgun, Assistant General Counsel, at 703-797-6600.

Background

The MSRB is charged by Congress to foster a free and open municipal securities market and to protect investors and the public interest.[4] Under this mandate, the MSRB has adopted a set of rule provisions that address dealer pricing and compensation, as well as transaction confirmations. MSRB Rule G-30, on prices and commissions, provides that a dealer may only purchase municipal securities for its own account from a customer, or sell municipal securities for its own account to a customer, at an aggregate price (including any mark-up) that is fair and reasonable. For such 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.[5] For purposes of Rule G-30, the mark-up is calculated based on the inter-dealer market price prevailing at the time of the customer transaction.[6] When executing a transaction on an agency basis, the

[2] *See* Request for Comment on Draft Rule Amendments to Require Dealers to Provide Pricing Reference Information on Retail Customer Confirmations, MSRB Notice 2014-20 (Nov. 17, 2014) ("Notice 2014-20").

[3] Comments are posted on the MSRB website without change. Personal identifying information such as name, address, telephone number, or email address will not be edited from submissions. Commenters should only submit information that they wish to make available publicly.

[4] *E.g.*, Securities and Exchange Act of 1934 § 15B(b)(2)(C), 15 U.S.C. 78o-4(b)(2)(C).

[5] Rule G-30, Supplementary Material .01(c) & (d).

[6] Rule G-30, Supplementary Material .01(d).

commission or service charge must not be in excess of a fair and reasonable amount.[7] Whether effecting a transaction on a principal or agency basis, dealers must exercise diligence in establishing the market value of the security and the reasonableness of their compensation.[8] Under MSRB Rule G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to transactions with customers, dealers are required to disclose on the customer confirmation transaction-based remuneration received from the customer when the dealer acts as agent. There is, however, currently no comparable disclosure requirement under SEC or MSRB rules when the dealer acts as principal.

In 2012, the Securities and Exchange Commission (SEC) issued a report in which it broadly examined the municipal securities market, including regulatory structure, market structure and market practices.[9] The report expressed concern about transparency, particularly with respect to pricing and transaction costs for retail customers.[10] The report noted that virtually all customer transactions in the municipal securities market are executed by dealers acting in a principal capacity.[11] The report also expressed concern regarding the dichotomy between current dealer remuneration disclosure requirements for transactions executed in an agency versus principal capacity when, at least in the case of "riskless principal" transactions, the SEC viewed the mark-up to be "readily determinable."[12] The report recommended that the MSRB consider encouraging or requiring dealers to provide retail customers relevant pricing reference information with respect to a municipal securities transaction effected by the dealer for the customer.[13] The report also recommended that the MSRB consider requiring dealers to disclose to customers, on confirmations for riskless principal transactions, the amount of any mark-up.[14]

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[7] Rule G-30(b)(ii).

[8] Rule G-30, Supplementary Material .01(a).

[9] *See* U.S. Securities and Exchange Commission, Report on the Municipal Securities Market (July 31, 2012) ("SEC Report").

[10] *See id*. at 115-116, 123-126.

[11] *See id*. at 113 and 148.

[12] *See id.* at 148-149.

[13] *See id*. at 147-148.

[14] *See id*. at 148-149.

SEC Chair Mary Jo White later publicly called for mark-up disclosure on riskless principal transactions and stated that the SEC would coordinate with the MSRB and FINRA in pursuit of such a standard.[15] Each of the other SEC Commissioners also has publicly urged the MSRB to consider adopting a mark-up disclosure, or similar, requirement for some category of principal transactions, at least to include "riskless principal" transactions.[16] In recent

[15] *See* 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 ("[T]o help investors better understand the cost of their fixed income transactions, [the SEC] will work with FINRA and the MSRB in their efforts to develop rules by the end of this year regarding disclosure of markups in 'riskless principal' transactions for both corporate and municipal bonds. . . . 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.")

[16] *See* Luis A. Aguilar, Commissioner, SEC, Statement on Making the Municipal Securities Market More Transparent, Liquid, and Fair (Feb. 13, 2015) available at http://www.sec.gov/news/statement/making-municipal-securities-market-more-transparent-liquid-fair.html (commending the MSRB on its transparency initiatives and urging additional disclosure, stating that "both FINRA and the MSRB should consider implementing a true markup disclosure requirement"); Michael S. Piwowar, Commissioner, SEC, Remarks at the 2014 Municipal Finance Conference presented by The Bond Buyer and Brandeis International Business School (Aug. 1, 2014) available at http://www.sec.gov/News/Speech/Detail/Speech/1370542588006 ("The time has come to require dealers to disclose markups and markdowns on all riskless principal bond transactions on customer confirmations"); Michael S. Piwowar, Commissioner, SEC, Remarks at University of South Carolina and UNC-Charlotte 4th Annual Fixed Income Conference (Apr. 21, 2015) available at http://www.sec.gov/news/speech/remarks-usc-unc-fourth-annual-fixed-income-conference.html ("Shortly after assuming my role as a commissioner at the SEC, I gave a speech calling for common-sense reforms to the municipal and corporate bond markets, including the disclosure of markups and markdowns on riskless principal transactions. In August of last year I reiterated that call . . . ."); Daniel M. Gallagher, Commissioner, SEC, Remarks at Municipal Securities Rulemaking Board's 1st Annual Municipal Securities Regulator Summit (May 29, 2014) available at http://www.sec.gov/News/Speech/Detail/Speech/1370541936387 ("Disclosure of the markup or markdown in riskless principal transactions would enable customers to assess the fairness of the execution prices. I encourage the MSRB to review whether amendments to Rule G-15 to accomplish such disclosure would be appropriate."); Daniel M. Gallagher, Commissioner, SEC, A Watched Pot Never Boils: the Need for SEC Supervision of Fixed Income Liquidity, Market Structure, and Pension Accounting (Mar. 10, 2015) available at http://www.sec.gov/news/speech/031015-spch-cdmg.html ("[A] dealer acting as a principal is not required to disclose its markup on a confirmation, even for a riskless principal transaction. Given that 'riskless principal' is basically just a fancy name for 'agency,' there is no real reason to perpetuate this dichotomy"); Kara M. Stein, Commissioner, SEC, Keynote

months, SEC Commissioners have renewed, and even strengthened, those calls.[17]

In November 2014, the MSRB issued Notice 2014-20, in coordination with FINRA, requesting comment on a proposal to require dealers to provide pricing reference information on retail customer confirmations (the "pricing reference proposal"). Under that proposal, for same-day, retail-sized principal transactions, dealers would be required to disclose on the customer confirmation the price to the dealer in a "reference transaction" and the differential between the price to the dealer and the price to the customer. A reference transaction would generally be a transaction in which the dealer, as principal, purchases or sells the same security that is the subject of the confirmation on the same day as the customer trade and on the same side of the transaction as the customer. Additionally, to be a reference transaction, it must be in a trade amount that individually, or when combined with one or more other dealer transactions, equals or exceeds the size of the customer transaction.

The pricing reference proposal had dual goals: to provide retail investors with increased transparency into the market for their security and to provide them with increased transparency into their transaction costs. As the MSRB explained in the notice, the pricing reference proposal was designed to be a reasonable alternative to a mark-up disclosure requirement. The notice stated that while the differential between the reference price and the customer price "is not necessarily the same as a markup, it can provide the investor increased price transparency and significant insight into the market

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Address at Columbia Law School Conference on Current Issues in Securities Regulation: The 'Hot' Topics (Nov. 21, 2014) available at http://www.sec.gov/News/Speech/Detail/Speech/1370543515397 (discussing "areas where regulators should move forward" and stating that "[d]espite the transaction information being readily available on EMMA, investors do not receive disclosure on their confirmations showing the transaction costs that they pay when they buy or sell a municipal security in a principal transaction").

[17] Luis A. Aguilar, Daniel M. Gallagher, Kara M. Stein and Michael S. Piwowar, Commissioners, SEC, Statement on Edward D. Jones Enforcement Action (Aug. 13, 2015) available at http://www.sec.gov/news/statement/statement-on-edward-jones-enforcement-action.html ("The Commission's recent enforcement action against Edward D. Jones involving the offer and sale of municipal bonds to retail investors highlights the need for clear rules requiring the disclosure of mark-ups and mark-downs. We encourage the Financial Industry Regulatory Authority (FINRA) and the Municipal Securities Rulemaking Board (MSRB) to complete rules mandating transparency of mark-ups and mark-downs, even in riskless principal trades. If not, we believe the Commission should propose rules to address this important issue.")

for the security," and "an analysis of this differential may also achieve many of the regulatory objectives of a markup disclosure requirement."[18] In addition to this possible substitute for mark-up disclosure, the notice identified mark-up disclosure as an alternative to the pricing reference proposal and sought comment as to that alternative, though a mark-up disclosure requirement was not the primary focus of the notice.

In response to the notice, several commenters expressed the view that mark-up disclosure on riskless principal transactions could achieve similar or greater benefits than the pricing reference proposal but at significantly lower cost, particularly if the most important goal of the pricing reference proposal was transparency regarding transaction costs.[19] Some commenters expressed the view that the disclosure of mark-ups on riskless principal trades most closely identifies dealer compensation, whereas disclosure of the difference in price between dealer and customer trades executed in the same security at different points in time on the same day would inaccurately suggest that such differences in price are always equivalent to the mark-up.

Based on careful consideration of all of the comments received on the pricing reference proposal, the MSRB believes, at this juncture, that a mark-up disclosure requirement may have comparable or greater benefits for retail investors in the municipal securities market than a pricing reference information disclosure requirement, with fewer costs to the market as a whole. For example, under the mark-up disclosure proposal, the risk of customer confusion and the potential to misinterpret the disclosures may be substantially decreased because the term "mark-up" is commonly understood as an indication of dealer compensation.

Additionally, because dealers are already under a regulatory obligation to ensure that their mark-ups are fair and reasonable, and to determine the prevailing market price in connection with their establishment of a fair price in their customer transactions, dealers should already have processes and systems in place to determine their mark-ups. Dealers would be required to disclose their mark-ups to customers, rather than utilize potentially

[18] Notice 2014-20, at 7.

[19] These commenters included: the Securities Industry and Financial Market Association, Morgan Stanley Smith Barney, LLC and Wells Fargo Advisors, LLC. Three commenters, Bernardi Securities, Financial Services Roundtable and Hilliard Lyons, favored limiting any disclosure (whether mark-up or pricing reference information) to "riskless" principal transactions.

complicated methodologies to determine which of potentially many transactions should be used as a comparator for purposes of disclosing to the customer pricing reference information. Also, as discussed below, mark-up disclosure is less likely to disrupt the generation for customers of intraday confirmations. The MSRB believes that a mark-up disclosure requirement, as proposed here, would be complementary to a number of transparency and retail-investor focused initiatives the MSRB has undertaken in recent years.[20] The MSRB is seeking, from investors, dealers, other market participants and all other interested persons, comment focused on a mark-up disclosure requirement for specified principal transactions, including those that could be considered "riskless." The MSRB is also seeking comment on all other aspects of this mark-up disclosure proposal and seeks, in particular, comments about likely costs and benefits.

In addition, after carefully considering the comments received on Notice 2014-20, the MSRB is seeking comment as to potential modifications to its pricing reference proposal, which may be considered as an alternative to this mark-up disclosure proposal.

Summary of Draft Amendments to Rule G-15

Mark-up Disclosure

In summary, the draft amendments to Rule G-15 would require disclosure on retail customer confirmations of:

- 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 within two hours of the customer's transaction; and
- a hyperlink and uniform resource locator ("URL") address to the Security Details page for the customer's security on EMMA, along

[20] *See* MSRB Long-Range Plan for Market Transparency Products (Jan. 27, 2012); Concept Release on Pre-Trade and Post-Trade Pricing Data Dissemination through a New Central Transparency Platform, MSRB Notice 2013-14 (July 31, 2013); Request for Comment on More Contemporaneous Trade Price Information Through a New Central Transparency Platform, MSRB Notice 2013-02 (Jan. 17, 2013); SEC Approves MSRB Rule G-18 on Best Execution of Transactions in Municipal Securities and Related Amendments to Exempt Transactions with Sophisticated Municipal Market Professionals, Notice 2014-22 (Dec. 8, 2014); MSRB Creates Online Education Center to House Digital Resources About the Municipal Market, Press Release (July 28, 2014). *See also* SEC Report, at 117, 141 (noting MSRB transparency initiatives).

with a brief description of the type of information available on that page.

The amendments additionally would require inclusion on all customer confirmations of the time of trade execution, accurate to the nearest minute.

Specified Principal Transactions

Under the draft amendments, dealers generally would be required to disclose the mark-up on retail customer confirmations for principal transactions when they transact on the same side of the market[21] 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 transaction. The disclosure of the mark-up would be required only where the dealer's same-side of the market transaction occurs within the two hours preceding or following the customer transaction.[22] The MSRB is not proposing to use this timeframe to define a "riskless principal" transaction; rather, the MSRB believes this timeframe would be sufficient to cover transactions that could be considered "riskless principal" transactions under any current market understanding of the term.

Mark-up Calculation and the Prevailing Market Price

Under the mark-up disclosure proposal, and consistent with existing MSRB fair-pricing rules, the mark-up to be disclosed on the customer confirmation would be the difference between the price to the customer and the prevailing market price for the security. Presumptively, the prevailing market

[21] To illustrate, a dealer is on the same side of the market as a customer who purchases securities when the dealer also purchases securities. Thus, for example, when a dealer purchases securities and then sells those same securities to a customer, the dealer and customer have traded on the same side of the market.

[22] A preliminary review of MSRB trade data for purposes of seeking comment suggests that under the MSRB's mark-up disclosure proposal, mark-up disclosure would be provided for at least half of all retail-sized customer trades in the secondary market. Retail-sized customer trades in the secondary market were defined, for purposes of this data analysis, as transactions with customers for $100,000 par amount or less (excluding trades reported as list offering price transactions). The MSRB is not, at this juncture, proposing to require disclosures for same-side of the market transactions made during the same trading day because it currently believes that the additional costs and complexities associated with the broadening of this time trigger to a full-day time period might not be justified. As noted below, however, the MSRB seeks comment on this matter and, more broadly, seeks comment as to whether mark-up disclosures should be required on all principal transactions with retail customers, irrespective of whether the dealer has a same-side of the market transaction in the customer's security.

price for the customer's security for purposes of calculating the mark-up would be established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained, consistent with applicable MSRB rules (*e.g.*, Rule G-18). While dealers, to comply with their fair-pricing obligations, already have processes and systems in place that are designed to ensure that their mark-ups on all principal transactions are fair and reasonable, the MSRB is currently proposing to require disclosure of the mark-up only under the parameters described herein, as the prevailing market price and resultant mark-up on the customer's security should be more readily determinable under these circumstances.[23] As detailed in the questions at the conclusion of this notice, the MSRB specifically seeks comment on the appropriate strength of the presumption described above, including whether it should be rebuttable or conclusive when the dealer, after receiving an order for a security, executes a transaction to offset the customer's purchase or sale of the security.

Disclosure Format

The disclosed mark-up would be required to be expressed both as a total dollar amount and as a percentage of the principal amount of the customer transaction.[24] The MSRB believes that, when expressed in these ways, disclosure of the mark-up would assist retail customers in understanding and comparing their transaction costs across their other municipal bond transactions to better evaluate the fairness of their transaction costs.

Retail Customers in the Secondary Market

Disclosure of the mark-up would be required for transactions for an account other than an "institutional account," as defined in MSRB Rule G-8(a)(xi).[25]

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[23] The MSRB understands that some dealers currently provide the amount of their mark-ups to customers upon request or disclose their mark-ups on customer confirmations.

[24] For example, if a customer purchased a quantity of 50 bonds ($50,000 par amount) at a price of 102 when the prevailing market price for the bonds was 100, the disclosure would indicate that the mark-up on the transaction was $1,000 (2% of $50,000 par amount) and that it equates to a 2% mark-up on the principal amount of the customer's bonds.

[25] Rule G-8(a)(xi) defines the term "institutional account" as

> the account of (i) a bank, savings and loan association, insurance company, or registered investment company; (ii) an investment adviser registered 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.

Additionally, to focus the proposal on the secondary market, the draft amendments would exclude transactions in new issue securities effected at the list offering price by members of the underwriting group[26] from the requirements of the mark-up disclosure proposal. Specifically, mark-up disclosure would not be required for a transaction that is a "list offering price transaction" as defined in paragraph (d)(vii) of Rule G-14 RTRS Procedures.[27] As defined therein, "list offering price transaction" means a primary market sale transaction executed on the first day of trading of a new issue by a sole underwriter, syndicate manager, syndicate member or selling group member at the published list offering price for the security. 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.[28]

"Look Through" for Specified Trading Structures

The MSRB is aware that some dealers, on an exclusive basis, acquire municipal securities from, or sell municipal securities to, an affiliate that holds inventory in such securities and transacts with other market participants. Under this inventory-affiliate model, the dealer 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.[29] This "look through" is designed to ensure that the

[26] Underwriting group members include sole underwriters, syndicate managers, syndicate members, selling group members or dealers that have entered into long-term marketing arrangements with other dealers that serve in the syndicate or selling group relating to purchases and re-sales of new issue securities. *See infra* n. 27.

[27] Effective no later than May 23, 2016, the list offering price transaction definition will be amended to mean a primary market sale transaction executed on the first day of trading of a new issue by a sole underwriter, syndicate manager, syndicate member, selling group member, or distribution participant to a customer at the published list offering price for the security. As used in the amended "list offering price transaction" definition, the term "distribution participant" will mean a dealer that has agreed to assist an underwriter in selling a new issue at the list offering price. *See* Release No. 34-75039 (May 22, 2015), 80 FR 31084 (June 1, 2015) (File No. SR-MSRB-2015-02).

[28] Due to the limited nature of this exception, if a member of the underwriting group makes a sale at a price other than the list offering price, s*ee* In the Matter of Edward D. Jones & Co., L.P., 2015 WL 4760902 (Aug., 13, 2015), the exception would not apply.

[29] For example, Dealer 1 and Dealer 2 are affiliates. All municipal securities are held in inventory at Dealer 1 while all principal transactions with retail customers are executed through Dealer 2. Dealer 1 and Dealer 2 have an agreement under which Dealer 2 will fill all of its orders for municipal securities through securities held at Dealer 1. Thus, in order to

disclosed mark-up is a more accurate indication of the compensation paid by the customer when affiliated dealers effectively function as a single entity for purposes of executing the retail customer's transaction. Further, in the absence of a "look through," the dealer would be required to disclose the mark-up on virtually all retail customer transactions (because the trade between these entities occurs very close in time to the associated customer transaction).

Functionally Separate Trading Desks

Absent additional guidance regarding the mark-up disclosure requirement, a dealer with multiple principal trading desks would ordinarily look across all of its trading desks to determine whether a same-side of the market transaction was executed in the customer's security within two hours of the customer trade.[30] However, the MSRB understands that under certain dealer structures, trading desks may operate independently of one another such that one trading desk may have no knowledge of the transactions executed by another trading desk within the same dealer. Under such structures, mark-up disclosure would not be required for a customer transaction if the dealer can establish that: (i) the customer transaction was executed by a principal trading desk that is functionally separate from the principal trading desk that executed the dealer's same-side of the market transaction;[31] and (ii) the functionally separate principal trading desk through which such same-

execute a transaction in municipal securities for a retail customer, there will always be an intermediate trade between Dealer 1 and Dealer 2. Under the MSRB's mark-up disclosure proposal, Dealer 2 must "look-through" the intermediate trade between Dealer 1 and Dealer 2, such that a disclosure to a retail customer of Dealer 2 would require an analysis of whether Dealer 1 executed a same-side of the market trade in the customer's security within two hours of the customer trade.

[30] Only purchases or sales that are required to be reported to the MSRB's Real-Time Transaction Reporting System ("RTRS") (*i.e.*, purchase-sale transactions in which there is a transfer of ownership) would trigger an obligation to disclose the mark-up. Because an internal movement of securities between a dealer's principal trading desks is not a reportable transaction under MSRB Rule G-14, a dealer would not be required to disclose the mark-up to a customer based on an internal movement of securities between principal trading desks made within two hours of the customer trade. For example, if a dealer's "institutional" trading desk acquires 100 bonds in XYZ securities at 10:00 a.m., and the dealer's "retail" trading desk within the same firm sells those bonds to a retail customer at 10:10 a.m., the internal movement of XYZ securities from the institutional trading desk to the retail trading desk seconds before the 10:10 a.m. sale to the retail customer would not trigger the obligation to disclose the mark-up to the customer. Rather, the occurrence of the dealer's initial acquisition of XYZ securities by the institutional trading desk at 10:00 a.m. (within two hours of the customer sale) would obligate the dealer to disclose the mark-up.

[31] This might be demonstrated, for example, through the firm's policies and procedures.

side of the market transaction was executed had no knowledge of the retail customer transaction. Excepting such transactions is consistent with the objective of the proposal to have sufficient parameters to cover transactions that could be considered "riskless principal" transactions.

Security-Specific Link to EMMA and Time of Execution

Lastly, a dealer would be required to provide two additional data points on the customer confirmation, even if the dealer would not be required to disclose its mark-up. First, on all customer confirmations for non-institutional accounts, including those for agency transactions, dealers would be required to provide a hyperlink and URL address to the Security Details page for the customer's security on EMMA,[32] along with a brief description of the type of information available on that page.[33] Second, without exception, dealers would be required to disclose the time of execution for a customer's trade, accurate to the nearest minute. Currently, under Rule G-15(a)(i)(A)(2), a dealer must either disclose this time of execution or provide the customer with a statement that the time of execution will be furnished upon written request of the customer. The MSRB's current proposal would essentially delete the option to provide this information upon request.

The MSRB believes that the provision of a security-specific link to EMMA on retail customer confirmations, together with the time of trade execution, would provide retail customers a comprehensive view of the market for their security, including the market as of the time of their trade. It also reduces the risk that a customer may focus exclusively on dealer compensation to the detriment of other relevant considerations. Additionally, the promotion of

[32] The MSRB is in the process of developing a more succinct EMMA URL for direct access to a security's Security Details page on EMMA. While current URLs will continue to work to avoid potential disruption for persons with existing page-specific bookmarks or direct links to EMMA pages, the MSRB believes that the creation of an additional more succinct link, which may be used in connection with this proposed disclosure, would be more intuitive and would decrease the number of characters used to make the disclosure on a customer confirmation.

[33] While the proposal would require this disclosure only on customer confirmations for non-institutional accounts, dealers would be free to provide it voluntarily on all customer confirmations, including those for institutional accounts. The MSRB also notes that, for dealers that currently seek to satisfy their obligation to provide a copy of the official statement to customers under Rule G-32(a)(iii) by notifying customers of the availability of the official statement through EMMA, the provision of a single link to the appropriate Security Details page on EMMA would satisfy both the Rule G-32(a)(iii) obligation and the obligation proposed here to provide a link on the confirmation; provided, that the hyperlink and URL address is accompanied by the information required under Rule G-32(a)(iii) as well as the MSRB's mark-up disclosure proposal.

easier access to EMMA may lead a customer to learn more about the market for the security and assist the customer in understanding any mark-up disclosure received in the context of this market. Even in instances in which the mark-up would not be required to be disclosed to customers, the MSRB believes that the inclusion of a security-specific link to EMMA on retail customer confirmations and the time of execution on all customer confirmations would increase market transparency at relatively low cost to the industry.

Economic Analysis of the Mark-up Disclosure Proposal

1. **The need for the draft amendments to Rule G-15 and how they will meet that need.**

The need for the draft amendments arises from the MSRB's regulatory obligations under the Securities and Exchange Act of 1934 to protect investors and foster a free and open market in municipal securities.[34] One of the important ways in which the MSRB meets this mandate is by ensuring that investors have access to the information necessary to make informed choices and foster competition among dealers.

Specifically, the draft amendments address the need for retail customers to have access to information about transaction costs when their dealers act in a principal capacity[35]—similar to the information provided to municipal securities investors under Rule G-15 when their dealers act in an agency capacity[36] and to the information provided to individuals investing in other types of securities under SEC Rule 10b-10.[37] Requiring that dealers disclose their mark-up on retail customer confirmations for specified principal transactions may allow retail customers to participate more fully in the market and encourage competition that could result in lower transaction costs for their purchases and sales of municipal securities.

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[34] Securities and Exchange Act of 1934 § 15B(b)(2)(C), 15 U.S.C. 78*o*-4(b)(2)(C).

[35] A review of MSRB trade data for the third quarter of 2014 shows that approximately 85 percent of the retail-sized transactions (less than $100,000) that dealers engage in, are conducted on a principal basis.

[36] *See* MSRB Rule G-15(a)(i)(A)(6)(f).

[37] *See* Rule 10b-10(a)(2)(ii).

The MSRB recognizes that prices—and the dealer compensation/transaction cost component of those prices—may be fair and reasonable,[38] but still higher than they might be in an even more competitive market where customers have more information about prices. Municipal securities dealers may be more likely to seek to reduce mark-ups, ensure that mark-ups are fair and reasonable and compete with other dealers on the basis of transaction costs if investors have more insight into those costs. Multiple studies cited in the SEC Report[39] showing that retail municipal securities investors pay higher transaction costs than institutional investors or investors in other asset classes, and attributing these differences, in part, to a lack of information, support the potential benefit of additional disclosure.

Additionally, the MSRB believes that providing investors with more information about those costs would improve investor confidence that prices are fair and reasonable and could make the enforcement of Rule G-30 more efficient.

Although including this information on customer confirmations means that investors would receive the disclosure after a transaction is complete, the MSRB believes the draft amendments may, nonetheless, address the need articulated above through at least three mechanisms. First, dealers may seek to reduce transaction costs to maintain and strengthen customer relationships. Second, transaction costs for future trades may be reduced if the disclosure prompts investors to request additional information about transaction costs from their dealers. Third, if an investor believes that a disclosed mark-up is higher than he or she might have received from another

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[38] In addition to the level of transaction costs, there are other factors that may affect whether the price received by a customer is fair and reasonable, including the market value of the security. The requirement in the draft amendments that dealers include a hyperlink and URL address to the Security Details page for the customer's security on EMMA may offer customers easier access to relevant pricing information. The MSRB's pricing reference proposal (Notice 2014-20) focused more directly on the need for investors to have more insight into the market value being bought or sold and offered an alternative approach to providing customers with access to relevant information.

[39] *See* SEC Report, *supra* n. 9, at 123. *See, also*, Lawrence E. Harris and Michael S. Piwowar, *Secondary Trading Costs in the Municipal Bond Market*, Journal of Finance, 61(3), (June 2006) ("Harris and Piwowar, *Secondary Trading Costs"*), at 1379 and Amy K. Edwards, Lawrence E. Harris and Michael S. Piwowar, *Corporate Bond Market Transaction Costs and Transparency*, Journal of Finance, 62(3), (June 2007) ("Edwards, Harris and Piwowar, *Corporate Bond Market Transaction Costs"*), at 1437.

dealer, the investor may be incentivized to seek out other dealers offering lower transaction costs for future trades.

The MSRB also believes that requiring dealers to provide on the customer confirmation the time of a trade's execution and a hyperlink and URL address to the Security Details page for the customer's security on EMMA would provide a comprehensive view of the market at the time of the customer's transaction and reduce the risk that investors focus disproportionately on dealer compensation. The promotion of easier access to EMMA in connection with the mark-up disclosure on a customer's confirmation may lead a customer to learn more about the market for his or her security and assist him or her in understanding the disclosure received in the context of this market.

2. Relevant baselines against which the likely economic impact of elements of the draft amendments to Rule G-15 can be considered.

To evaluate the potential impact of the draft amendments, a baseline or baselines must be established as a point of reference in comparison to the expected state with the draft amendments in effect. The economic impact of the draft amendments is generally viewed to be the difference between the baseline and the expected states.

Two existing MSRB rules serve as relevant baselines. Rule G-15, as discussed above, requires dealers to disclose on the confirmation the price of a municipal securities transaction and, for agency transactions, the dealer must also disclose on the confirmation the amount of remuneration received from the customer in connection with the transaction.

Rule G-30 provides that dealers acting in a principal capacity may only purchase municipal securities from, or sell municipal securities to, a customer at an aggregate price (including any mark-up) that is fair and reasonable. The MSRB assumes that compliance with this rule means that dealers are currently aware of the mark-up associated with their principal transactions.

SEC Rule 10b-10 may also serve as a relevant baseline, particularly for municipal securities dealers who also transact in equity securities on a principal basis. Specifically, Rule 10b-10(a)(2)(ii)(A) requires that, if a broker or dealer, after having received a customer order to buy or sell an equity security, buys or sells that security from another person to offset a contemporaneous sale to or purchase from the customer, then the broker or dealer must disclose on the customer confirmation the difference between

the price to the customer and the dealer's contemporaneous purchase or sale price.

3. Identifying and evaluating reasonable alternative regulatory approaches.

The MSRB recognizes that there are alternatives to the approach proposed under the draft amendments that range from modifying specific parameters of the MSRB's mark-up disclosure proposal to employing significantly different mechanisms for providing relevant information to investors.[40]

The MSRB could make a number of modifications to specific parameters of the mark-up disclosure proposal including, but not limited to the following:

Modifying the time period separating the customer's trade from a dealer's same-side of the market transaction: The disclosure requirement could be narrowed to only riskless principal transactions, expanded to include principal transactions in which the dealer executed a trade in the customer's security on the same side of the market separated by more than two hours from the customer's trade, or expanded to include all principal transactions regardless of whether the dealer executed a trade in the customer's security on the same side of the market at any time.

Narrowing the requirement to only riskless principal transactions would likely simplify the programming required to determine if a transaction requires confirmation disclosure, improve the efficiency of enforcement, and more closely parallel SEC Rule 10b-10. This narrowing, however, would likely reduce the number of trades requiring mark-up disclosure. It may also create incentives for dealers to change their behavior by, for example, delaying transactions that might previously have been undertaken more contemporaneously so that they are no longer (or no longer appear to be) riskless, by filling more orders out of internal inventory, or by promoting greater use by customers of fee-based accounts.

Expanding the requirement to include principal transactions in which the dealer executed a same-side of the market transaction in the customer's security separated by more than two hours from the customer's trade would likely increase the number of trades requiring mark-up disclosure. Such an

[40] As noted above, in addition to the alternatives described in this section, the MSRB is specifically seeking comment on possible modifications to the MSRB's previous proposal to require dealers to provide pricing reference information on retail customer confirmations for same-day principal transactions in municipal securities.

expansion may require dealers to exercise more subjective judgment in determining the prevailing market price. It also may make programming systems to determine the trades that require a confirmation disclosure more difficult and could, depending on a firm's processes and the length of time used to determine whether a triggering transaction occurred, delay the generation of confirmations.

Expanding the requirement to include all principal transactions regardless of whether or when the dealer executed a same-side of the market transaction in the customer's security would significantly increase the number of customers receiving information on transaction costs. Such 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.

Modifying the size of the dealer's same-side of the market transaction that would trigger disclosure: The disclosure requirement could be narrowed so that it would only be triggered if the dealer executed a same-side of the market transaction in exactly the same trade size as the customer's trade or broadened so that it would be triggered if the dealer had a trade in the same security of any size.

Narrowing the proposal to only those instances in which a dealer executed a same-side of the market transaction in the exact same trade size would reduce the number of customers receiving disclosure. Broadening the proposal to include those instances in which a dealer had a same-side of the market transaction in the same security regardless of size would increase the number of customers receiving disclosure and would likely eliminate the need for dealers to develop a matching utility based on trade size and would allow confirmations to be printed immediately following the customer's transaction.

Modifying which investors receive mark-up disclosure: The MSRB could require that confirmation disclosure be provided to customers with institutional accounts, in addition to those with non-institutional accounts. Expanding the requirement would increase the number of customers receiving the disclosure but may make the necessary programming changes more challenging if these types of accounts are supported by different systems.

Modifying the form of the disclosure: The MSRB could allow dealers to provide mark-up disclosure on a document included with, but distinct from, the confirmation or online via a link included with the confirmation.

Alternatives to including the mark-up on the front of the confirmation would reduce the likelihood that customers would review the information but may reduce the burden on firms of modifying confirmations.

The MSRB could also consider approaches that differ more significantly from the draft amendments. For example, rather than requiring the disclosure of the mark-up on customer confirmations, the MSRB could require that dealers disclose the difference between the price paid by or received from the customer and a price estimated by a third-party price evaluator. These approaches may be more confusing to investors and create a more significant burden on dealers than what is proposed under the draft amendments.

Rather than disclosing a specific mark-up, the MSRB could require that dealers provide customers with a schedule indicating the range, in percentage terms, of the mark-up applied to certain transactions. This approach would significantly reduce the burden on dealers and would provide some basis from which customers could make comparisons between dealers. However, this approach would provide less precise insight into the transaction costs associated with specific transactions, might be misleading, and might cause investors to focus disproportionately on mark-ups to the detriment of an overall evaluation of the value of a specific transaction.

Finally, instead of requiring dealers to provide information about transaction costs, the MSRB could make modifications to EMMA that might provide greater insight into a dealer's transaction cost than currently possible from EMMA. For example, the MSRB could calculate, and report on EMMA, the difference between the prices of each reported trade and the trade in the same security that took place closest in time anywhere in the market. While such approaches would likely reduce or eliminate the burden on dealers, they would likely provide less insight into the transaction costs associated with specific transactions and specific dealers than under the mark-up disclosure proposal and could be misleading. Additionally, because such an approach would rely on customers to proactively seek out the information on EMMA, fewer customers may actually obtain the benefit of this approach.

4. Assessing the benefits and costs of the draft amendments to Rule G-15 and the main alternative regulatory approaches.

The MSRB policy on economic analysis in rulemaking addresses consideration of the likely costs and benefits of the rule with the draft amendments fully implemented against the context of the economic baseline discussed above.

The MSRB has identified various data to help quantify the economic impact of the proposal. Trade data from EMMA provides an indication as to the portion of retail-size trades in municipal securities to which a potential disclosure requirement would apply. In addition, the MSRB has identified several studies that estimate the magnitude of transaction costs in the municipal securities market.[41] The MSRB is seeking, as part of this request for comment, additional data or studies relevant to transaction costs, the costs of implementing the systems and processes necessary to comply with the draft amendments, and the potential unintended or indirect consequences of the draft amendments.

Benefits

The MSRB believes that the draft amendments would result in important benefits for a significant number of retail investors and promote a free and open municipal securities market.

Mark-up disclosure would provide investors with reliable insight into the transaction costs and dealer compensation associated with trading municipal securities and, thereby, foster more informed engagement between customers and dealers, as well as competition among dealers. Any resulting reduction in mark-ups would reduce costs paid by investors. The disclosure would also increase investor confidence that transaction costs are fair and reasonable.

Reducing transaction costs and increasing investor confidence may also encourage broader participation in the municipal securities market, improve liquidity, and lower borrowing costs for issuers. The draft amendments may also lower the cost of enforcement of existing regulations.

The MSRB also expects that the inclusion of a hyperlink and URL address to the Security Details page for the customer's security on EMMA would encourage greater use of EMMA and would provide customers with more information about the market for their security as of the time of their transaction.

Costs

Our analysis of the potential costs does not consider all of the costs associated with the proposal, but instead focuses on the incremental costs attributable to it that exceed the baseline state. The costs associated with

[41] *See supra* n. 39.

the baseline state are, in effect, subtracted from the costs associated with the draft rule to isolate the costs attributable to the incremental requirements of the proposal.

The proposal would likely require firms to modify their operational systems to identify customer transactions that require mark-up disclosure, specify the mark-up, and provide additional information on customer confirmations.

The MSRB expects that the modifications needed to identify the transactions that require disclosure are likely to be the most costly aspect as dealers would need to determine if a customer's transaction meets a number of criteria. While some determinations (*e.g.*, whether a transaction is for an institutional account) may be relatively simple, others such as whether the dealer has transacted in the same security within a certain time period may require the development of a matching utility.[42]

Because dealers are currently required under Rule G-30 to determine whether their mark-ups are fair and reasonable[43] and to determine the prevailing market price of a security as the basis for establishing a fair price in their transactions with customers,[44] the MSRB assumes that the determination of the mark-up will generally not impose significant costs for the universe of trades for which dealers would be required to provide disclosure under this proposal.[45] However, the MSRB recognizes that the transfer of this information to appropriate systems may involve costs.

The MSRB understands that changes to customer confirmations may be costly and has sought to limit this burden by limiting the amount of new

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[42] The MSRB notes that the costs associated with developing this type of matching utility may be avoided or significantly reduced if dealers were to voluntarily exceed the requirements of the draft amendments and provide mark-up disclosure for more, or even all, principal transactions.

[43] Rule G-30, supplementary material .01(a).

[44] *See* MSRB Reminds Firms of Their Sales Practice and Due Diligence Obligations When Selling Municipal Securities in the Secondary Market, MSRB Notice 2010-37 (Sept. 20, 2010).

[45] The MSRB previously published draft interpretive guidance on prevailing market prices and markups for transactions in municipal securities. *See* Request for Comments on Draft Interpretive Guidance on Prevailing Market Prices and Mark-up for Transactions in Municipal Securities, MSRB Notice 2010-10 (Apr. 21, 2010). However, this guidance was not adopted. As noted below, the MSRB seeks comment as to whether additional guidance is needed for establishing the prevailing market price in connection with the current mark-up disclosure proposal.

information that would need to be included. The MSRB also understands that changes to when and how confirmations are processed may have cost impacts and has sought to limit this burden by proposing to require firms to wait, at a maximum, two hours to determine whether disclosure will be required.

The MSRB assumes that the majority of the costs associated with these system changes would be one-time costs.

The MSRB is aware of the possibility that because the proposal only requires disclosure of a subset of transactions, dealers may reduce mark-ups on those trades that require disclosure but increase mark-ups on those trades that do not require disclosure.

The MSRB is aware that the inclusion of additional information on confirmations may prompt investors to engage more frequently with dealers, particularly given that investors will only receive disclosures on a subset of transactions. While these interactions have costs, the MSRB expects that the benefits of better-informed investors would be significant and would likely outweigh the costs.

The MSRB is also seeking comment on whether its mark-up disclosure proposal could have unintended impacts on market behavior including, but not limited to: firms holding fewer bonds in inventory, firms being incentivized to fill more orders out of inventory, and dealers promoting the greater use by customers of fee-based accounts.

Effect on Competition, Efficiency, and Capital Formation

The MSRB believes that the proposal would incentivize dealers to offer competitive prices in retail transactions to avoid losing transaction volume or putting client relationships at risk and, potentially, encourage clients to seek out other dealers that might offer more competitive mark-ups. Retail customers would have information that will allow them to make more informed choices, request additional information, and potentially evaluate the use of other dealers for future transactions.

It is possible that the costs associated with the requirements of the proposal relative to the baseline may lead some dealers to reduce services to retail investors. In some cases, the costs could lead smaller dealers to consolidate with larger dealers or to exit the market.

By encouraging dealers to seek ways to reduce transaction costs, the draft amendments may result in greater efficiency in the municipal securities market.

The MSRB also believes that lower transaction costs and increased investor confidence would encourage wider participation in the market and thus have a positive effect on capital formation.

In addition to the questions posed and matters discussed in this notice, the MSRB also requests comment, as a general matter, on any revised FINRA proposal as well as the below potential modifications to the MSRB's previously proposed pricing reference proposal.

Pricing Reference Information Disclosure Alternative

In Notice 2014-20, the MSRB sought comment as to the different elements of the pricing reference proposal, including: the retail-customer standard, exclusions from the disclosure requirement, disclosure format and reference transaction selection methodology in the event that more than one potential reference transaction was executed on the same day. The MSRB also sought comment as to explanatory notations that might be included on or with the confirmation.

Notice 2014-20 included an economic analysis of the pricing reference proposal. At this juncture, the MSRB believes that the below possible modifications to the pricing reference proposal may result in the proposal having the same or greater benefits than those that would result from the initial pricing reference proposal at a potentially lower cost. In response to comments received on the pricing reference proposal, the MSRB is now seeking comment on possible modifications to the proposal—including comments on the likely costs and benefits—in its ongoing consideration of the alternative.

Retail-Customer Standard

Under the pricing reference proposal, the MSRB has intended to require the pricing reference information disclosure only for retail customers, and the pricing reference proposal aimed to achieve this objective by requiring that the disclosures be provided only when the customer transaction involves 100 bonds or fewer or bonds in a par amount of $100,000 or less. In response to Notice 2014-20, some commenters suggested that the use of a status-based standard, rather than a transaction-size standard would better align with the universe of "retail" customers on whom the pricing reference proposal should be focused. Commenters also suggested that dealers have already integrated into their processing systems a status-based retail / institutional account identification and that the use of this existing standard in connection with a pricing reference disclosure requirement would decrease the costs, but not the benefits, of the proposal. The MSRB now seeks comment as to whether it should require the disclosures only for accounts that are not

"institutional accounts" as defined in MSRB Rule G-8(a)(xi). This would be the same retail customer standard as that proposed under the mark-up disclosure proposal.

Exclusions

While the need for the initial pricing reference proposal focused on secondary market transactions, the MSRB did not initially propose an explicit exception for specific types of transactions. The MSRB now seeks comment as to whether it should limit the pricing reference disclosure proposal to the secondary market by providing that disclosure would be required only for a customer transaction that is not a "list offering price transaction" as described above in the MSRB's mark-up disclosure proposal.

The MSRB also seeks comment as to whether it should exclude, as potential reference transactions, transactions between affiliated dealers upon the satisfaction of the same conditions set forth under the mark-up disclosure proposal. Specifically, if a dealer that transacts with customers acquires on an exclusive basis securities from, or sells on an exclusive basis securities to, an affiliated dealer that holds inventory in municipal securities and transacts with other market participants, the MSRB seeks comment as to whether the dealer that transacted with the customer should be required to "look through" its trades with its affiliated dealer and disclose as the reference transaction the external trade between its affiliated dealer and the third party with which its affiliated dealer transacted for the securities.

The MSRB also seeks comment as to whether a transaction should be excluded as a reference transaction if: (i) executed by a principal trading desk that is functionally separate from the principal trading desk that executed the customer transaction; and (ii) the functionally separate principal trading desk through which such transaction was executed had no knowledge of the retail customer transaction.[46] This would be consistent with the treatment of principal trading desks under the mark-up disclosure proposal.

[46] Note, however, that only purchases or sales that are required to be reported to RTRS (*i.e.*, purchase-sale transactions in which there is a transfer of ownership) could qualify as a reference transaction. Because an internal movement of securities between a dealer's principal trading desks is not a reportable transaction under Rule G-14, such an internal movement would not qualify as a reference transaction. For example, if an "institutional" trading desk acquires 100 bonds in XYZ securities, and the "retail" trading desk within the same firm sells those bonds to a retail customer, the reference transaction would not be the internal movement between principal trading desks, rather it would be the "institutional" trading desk's acquisition of those bonds (assuming the acquisition otherwise qualifies as a reference transaction).

Disclosure Format

The MSRB initially proposed to require dealers to disclose the differential between the customer transaction and the reference transaction expressed as a percentage of par. The MSRB now seeks comment as to whether, in addition to expressing this differential as a percentage, the differential should also be required to be disclosed as a total dollar amount.[47] These would be the same disclosure format requirements as proposed under the mark-up disclosure proposal.

Selection Methodology

The MSRB did not initially propose a specific methodology or methodologies to be used in determining which of potentially many reference transactions would be required to be disclosed on a customer confirmation. Rather, it sought comment as to the approach that should be used and sought comment on a number of methodologies set forth in FINRA's initial pricing reference proposal.[48] The MSRB again seeks comment on the appropriate standard(s) to be used in determining the reference transaction, and more specifically, seeks comment on the methodology proposed in FINRA's initial proposal and any revised FINRA proposal.

Cancels/Rebills

The MSRB seeks specific input on a possible clarification that dealers 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. In addition, associated with this possible clarification, dealers would expressly be permitted to include a disclaimer on the customer confirmation that the reference price and related differential were determined as of the time of confirmation generation.

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[47] The price of a transaction is an expression of percentage of the principal amount of the securities. The price differential would reflect the difference in percentages of principal between the customer's transaction and the reference transaction. Multiplying the price differential by the par amount transacted would provide the total dollar amount difference between the customer's price and the reference transaction price. For example, a price differential of 2 expressed as a percentage of par means 2% of the par amount (*e.g.*, 2% of $50,000 or .02 x $50,000). When expressed in dollars, this same differential would be $1,000 (2% x $50,000 par amount).

[48] *See* FINRA Regulatory Notice 14-52 (Nov. 2014).

Security-Specific Link to EMMA and Time of Execution

The MSRB seeks comment, in the context of the pricing reference proposal, whether dealers should be subject to the same requirements discussed above to provide a security-specific link to EMMA and include the time of execution for the customer's transaction.

Questions

Mark-up Disclosure Proposal

1. Would the proposed mark-up disclosure provide investors with greater transparency into the compensation of their dealers or the costs associated with the execution of their municipal securities trades? Would the proposed disclosures help ensure investors receive fair and reasonable prices? What are the other potential benefits of the mark-up disclosure proposal?

2. Do dealers have adequate regulatory guidance as to how they should determine their mark-ups or the prevailing market price for the class of principal transactions specified in the proposal, or for all principal transactions if any disclosure requirement were so expanded? If not, specifically what additional guidance would be helpful?

3. Is it appropriate to rebuttably presume that the prevailing market price for the customer's security, for purposes of calculating the mark-up or mark-down, would be established by referring to the dealer's contemporaneous cost or proceeds, and should such a presumption be adopted by rule? What is the appropriate strength of such a presumption? For situations in which the dealer, after receiving an order for a municipal security, executes a transaction to offset the customer's purchase or sale of the security, should the presumption be conclusive (*i.e.*, irrebuttable)?

4. How do dealers currently determine whether the mark-up being charged to customers transacting in municipal securities is fair and reasonable?

5. Is it more difficult, costly or burdensome for dealers to determine the prevailing market price and/or mark-up for those transactions for which they do not have a contemporaneously executed or nearly contemporaneously executed transaction in the same security?

6. What system changes would be required for dealers to comply with the requirements identified in the draft amendments? What are the costs associated with each of these changes?

7. Would the required disclosures encourage dealers to take actions to avoid making the proposed mark-up disclosures? For example, might dealers be incentivized to sell from inventory or hold securities until the relevant time period requiring disclosure has lapsed? If so, what effect might such actions have on the market? Would the risks or costs to dealers associated with holding securities in inventory significantly disincentivize such actions?

8. Since dealers already have processes and systems in place that are designed to ensure that their mark-ups on all principal transactions are fair and reasonable, should the MSRB take a different approach to determining which transactions require mark-up disclosure? For example, should the MSRB require disclosure on transactions for which a dealer had another transaction in the same security on the same day but more than two hours from the customer's transaction? Should the MSRB require disclosure on transactions for which a dealer executed another transaction(s) in the same security that did not equal or exceed the size of the customer's transaction? Should mark-up disclosure be required on all principal transactions?

9. Is there evidence of any error in the findings in the cited literature showing higher transaction costs in the municipal securities market compared to the corporate bond market and equities markets? Is there evidence of any error in the findings in the cited literature showing that retail investors pay more than institutional investors when trading municipal securities?

10. Is there evidence that the mark-ups associated with municipal securities transactions in which the dealer acts in a principal capacity are higher than they would be under conditions in which retail investors had access to more information about prices and/or dealer compensation or in which there was greater competition among dealers to serve retail investors?

11. Are there other relevant baselines the MSRB should consider when evaluating the economic impact of the mark-up disclosure proposal?

12. Are there data or studies relevant to the evaluation of the benefits and costs of the mark-up disclosure proposal that the MSRB should consider?

13. Are there data to support or call into question the MSRB's estimate, based on trade size, that at least half of retail trades in the secondary market would result in disclosure?

14. How are retail investors likely to use information about mark-ups?

15. What is the range of potential transaction cost reductions that could be expected after full implementation of the mark-up disclosure proposal?

Mark-up Disclosure Proposal and Potential Modifications to the Pricing Reference Proposal

16. Is the MSRB's proposed retail-customer standard, in connection with its mark-up disclosure proposal and the potential modifications to its pricing reference proposal, the standard that should be applied in light of the objectives of the proposals? If not, what should the standard be? Should the mark-up disclosures be limited to retail customers at all or should it be extended to all customers, retail and institutional?

17. Is the MSRB's proposed standard for excluding the primary market in connection with its mark-up disclosure proposal and the potential modifications to its pricing reference proposal the appropriate standard to apply? Are there alternative approaches that would better exclude primary market trades while still focusing the benefit of the proposed disclosures on retail investors in the secondary market?

18. What would be the cost to dealers, above and beyond the other costs associated with the mark-up disclosure proposal and the potential modifications to the pricing reference proposal, of the MSRB's proposed "look through?"

19. Should the proposed provision of a link (and URL address) to the EMMA Security Details page for a customer's security be required, as is proposed, on all retail customer confirmations, or just those for which mark-up disclosures or pricing reference disclosures would be required?

20. What changes should the MSRB consider making to EMMA to provide investors with additional insight into transaction costs?

Potential Modifications to the Pricing Reference Proposal

21. Should the MSRB require that a single reference transaction selection methodology be used under all scenarios? For example, in the case of a customer purchase, should the reference transaction be the dealer's last same-day purchase, if any, of the securities that the customer traded that preceded the customer trade; and in the case of a customer sale, should the reference transaction be the dealer's first sale of the same securities following the customer sale if the dealer makes any sale by the end of the same trading day?

22. For purposes of establishing a reference price, should the dealer be required to consider its principal trades with dealers and customers, or only its principal trades with dealers?

September 24, 2015

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Text of Draft Amendments*

Rule G-15: Confirmation, Clearance, Settlement and Other Uniform Practice Requirements with Respect to Transactions with Customers

(a) *Customer Confirmations.*

(i) At or before the completion of a transaction in municipal securities with or for the account of a customer, each broker, dealer or municipal securities dealer shall give or send to the customer a written confirmation that complies with the requirements of this paragraph (i):

(A) Transaction information. The confirmation shall include information regarding the terms of the transaction as set forth in this subparagraph (A):

(1) No change.

(2) Trade date and time of execution. The trade date and time of execution, accurate to the nearest minute, shall be shown. ~~In addition, either (a) the time of execution, or (b) a~~

* Underlining indicates new language; strikethrough denotes deletions.

~~statement that the time of execution will be furnished upon written request of the customer shall be shown.~~

(3) – (8) No change.

(B) – (C) No change.

(D) Disclosure statements:

(1) - (3) No change.

(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.

(E) Confirmation format. All requirements must be clearly and specifically indicated on the front of the confirmation, except that the following statements may be on the reverse side of the confirmation:

(1) – (2) No change.

~~(3) The statement concerning time of execution that can be provided in satisfaction of subparagraph (A)(2) of this paragraph.~~

(F) Mark-ups and Mark-downs.

(1) General. If the broker, dealer or municipal securities dealer ("dealer") is effecting a transaction in a principal capacity for an account that is not an institutional account (as defined in Rule G-8(a)(xi)), 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, if:

(a) In the case of a sale to a customer, the dealer (or affiliate of the dealer, in the case of an inventory-affiliate model) purchased the security in one or more transactions in an aggregate trade size meeting or exceeding the size of such sale within two hours of the customer transaction; or

(b) In the case of a purchase from a customer, the dealer (or affiliate of the dealer, in the case of an inventory-affiliate model) sold the security in one or more transactions in an aggregate trade size meeting or exceeding the size of such purchase within two hours of the customer transaction.

(2) Notwithstanding subparagraph (F)(1) above, 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.

(3) 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 transacts with other market participants.

(4) This paragraph (F) 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.

(5) This paragraph (F) shall not apply to transactions in municipal fund securities.

(ii) – (viii) No change.

(b) – (g) No change.

EXHIBIT 2e

ALPHABETICAL LIST OF COMMENT LETTERS ON MSRB NOTICE 2015-16 (SEPTEMBER 24, 2015)

1. Aaron Botbyl: E-mail dated October 9, 2015

2. Bernardi Securities, Inc.: Letter from Eric Bederman, SVP, Chief Operating & Compliance Officer, dated December 4, 2015

3. Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated December 11, 2015

4. CFA Institute: Letter from Kurt N. Schacht, Managing Director, Standards and Financial Market Integrity, and Linda L. Rittenhouse, Director, Capital Markets Policy, dated December 11, 2015

5. Charles Schwab & Co. Inc.: Letter from Jason Clague, Senior Vice President, Trading & Middle Office Services, dated December 11, 2015

6. Chris Melton: E-mail dated October 30, 2015

7. Christopher [last name withheld]: E-mail dated September 25, 2015

8. Consumer Federation of America: Letter from Micah Hauptman, Financial Services Counsel, dated December 11, 2015

9. Diamant Investment Corporation: Letter from Herbert Diamant, President, dated November 30, 2015

10. Fidelity Investments: Letter from Norman L. Ashkenas, Chief Compliance Officer, Fidelity Brokerage Services, LLC, and Richard J. O'Brien, Chief Compliance Officer, National Financial Services, LLC, dated December 11, 2015

11. Financial Information Forum: Letter from Darren Wasney, Program Manager, dated December 11, 2015

12. Financial Services Institute: Letter from David T. Bellaire, Executive Vice President & General Counsel, dated December 11, 2015

13. Gerald Heilpern: Letter

14. LPL Financial LLC: Letter from David P. Bergers, General Counsel, dated December 10, 2015

15. Morgan Stanley Smith Barney LLC: Letter from Elizabeth Dennis, Managing Director, dated December 11, 2015

16. Office of the Investor Advocate, U.S. Securities and Exchange Commission: Letter from Rick A. Fleming, Investor Advocate, dated December 11, 2015

17. Patrick Luby: Letter dated December 11, 2015

18. Public Investors Arbitration Bar Association**:** Letter from Hugh D. Berkson, President, dated December 8, 2015

19. RBC Capital Markets, LLC: Letter from David L. Cohen, Senior Counsel and Director, dated December 15, 2015

20. RW Smith & Associates, LLC: Letter from Paige W. Pierce, President & CEO, dated December 11, 2015

21. Securities Industry and Financial Markets Association: Letter from Sean Davy, Managing Director, Capital Markets Division, and Leslie M. Norwood, Managing Director & Associate General Counsel, Municipal Securities Division, dated December 11, 2015

22. Thomson Reuters: Letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, dated December 11, 2015

23. TMC Bonds, LLC: Letter from Thomas S. Vales, Chief Executive Officer, dated December 11, 2015

24. Wells Fargo Advisors, LLC: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated December 11, 2015

Comment on Notice 2015-16

from Aaron Botbyl, retired

on Friday, October 9, 2015

Comment:

I think this is a great idea.
Aaron Botbyl

BERNARDI SECURITIES INC.

MUNICIPAL BOND SPECIALISTS

Submitted Electronically

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

Re: Amendments to Confirm Disclosure—Regulatory Notice 2015-16

December 4, 2015

Dear Mr. Smith:

Founded in 1984, Bernardi Securities, Inc. (BSI) is a municipal securities dealer providing underwriting, secondary market trading, brokerage, and portfolio management services to our institutional and retail customer base. We appreciate the opportunity to provide the Municipal Securities Rulemaking Board (MSRB) with comments related to the above referenced proposed rule.

In comments previously submitted to the MSRB, BSI has stated that we strongly support appropriate transparency in our industry. We currently provide mark-up/mark-down information upon request to customers wishing information on trades executed in a principal capacity. We have also commented on the necessity of providing this information on a customer confirmation, as similar information is also made available to the public on the EMMA website.

We have reviewed MSRB Notice 2015-16 and FINRA Regulatory Notice 15-36. It is our opinion that if mark-up disclosure is ultimately required, the method of disclosure should be harmonized for all fixed income products. Different requirements would add extra levels of complexity for both the dealers and customers.

Below you will find our comments on the various aspects of the MSRB and FINRA proposals:

Applicability Timeframe

We support the MSRB proposal of a two hour window between a dealer's contemporaneous execution and the subsequent trade with the customer. A trade is only "riskless" if holding a customer order prior to executing a street side trade. The longer a dealer holds the position in inventory, the greater the risk to the dealer. While there is significant intraday risk, the first two hours represent a lower timeframe for the dealer's risk.

Markup Calculation

We support the calculation method proposed by FINRA. This method compares the customer's execution to the firm's contemporaneous price (i.e. the dealer's cost). This is a straightforward calculation that customers will understand. The MSRB's proposal for a comparison between the

customer's execution and "the prevailing market price at the time of the customer trade" will require the dealer to ascertain two prices at the time of a disclosable customer trade—first the fair market value for the customer's execution and second the dealer's prevailing market price. In cases of smaller and thinly traded issuances, the dealer's contemporaneous execution is prevailing market price—even within two hours. We believe the method proposed by FINRA will be more beneficial to the retail customer.

Disclosure Format

We believe the dealer should be allowed to develop its own format for disclosure. This format should include a basic calculation of the markup and shown as either a total dollar amount or per bond basis. Other elements, such as percent of par, should be up to the dealer with the format uniform for all disclosable trades.

Links to Repositories

We have no objection to the requirement that confirmations include links to the appropriate trade repository (TRACE and EMMA). However we request that both FINRA and the MSRB provide a URL structure that is standardized around the CUSIP number. Any non-standardized URL format will introduce the possibility of errors or "broken links."

BSI appreciates the opportunity to comment on this proposed rule and we look forward to providing additional feedback that will help the MSRB and the greater municipal bond marketplace.

Sincerely yours,

Eric Bederman
SVP, Chief Operating & Compliance Officer

BDA Bond Dealers of America

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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

CFA Institute

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22903-2981 USA

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+1 (434) 951 5262 fax
info@cfainstitute.org
www.cfainstitute.org

11 December 2015

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

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

Dear Mr. Smith:

CFA Institute[1] appreciates the opportunity to comment on the Municipal Securities Rulemaking Board's (MSRB, or the Board) proposal to require brokers, dealers, and municipal securities dealers (collectively "dealers") acting as principal to disclose markups and markdowns on transactions with their clients. 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 municipal bond market, and believes that measures to provide additional pre-trade information are warranted, in addition to the post-trade transparency that this proposal seeks.

Proposed two-hour reporting window. We support the use of a two-hour window for reporting trades, with the understanding that the MSRB believes this adequately captures the universe of riskless principal trades, which are the subject of the proposed disclosure.

[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.

Links to EMMA. While we support providing price information to customers when dealers trade as principal, we also recognize that customers in general need more information relating to municipal transactions. We therefore support the proposed links to EMMA that dealers would be required to provide all customers.

Discussion

As proposed, dealers acting in the capacity of principals would have to disclose a mark-up or mark-down (collectively, "mark-ups") on certain transactions in municipal securities when the transaction occurs on the same side as their retail customer, and within a two-hour window of that customer's transaction. The proposal would extend only to non-institutional accounts and would exclude a "list offering price transaction" (*e.g.*, a primary market sale of new issues offered by an underwriter at the list offering price).

Not only would proposed amendments to Rule G-15 require disclosure of such mark-ups on relevant customer confirmations, it also would require those confirmations to include a hyperlink and URL to details of the involved security on the MSRB's Electronic Municipal Market Access (EMMA). The time of trade execution to the nearest minute would also be noted to permit investors to review similar transactions that occurred around the same time as their trades.

Disclosure of Mark-ups

In particular, dealers would be required to disclose on customer confirmations all transactions in which they transact on the same side as their customer:

- When the dealer's transaction equals or exceeds the size of their customers' orders; and
- Occur during the two-hour window on either side of their customers' transactions.

For purposes of calculating the mark-up, the proposal notes that the amount to disclose would be "the difference between the price to the customer and the prevailing market price for the security." This amount would be reported in the confirmation as both a total dollar amount, and as a percentage of the principal amount of the customer's order.

We agree that the MSRB's proposal addresses a current omission in its rules. MSRB Rule G-15 requires disclosure on the customer confirmation of the amount of the mark-up received on a transaction when dealers act in an *agency* capacity. It also requires that commissions or service charges for trades executed on an agency basis must be of a fair and reasonable amount. However, there is no such MSRB rule requiring the same type of disclosure when dealers act as *principals*. We thus support adoption of the proposed disclosures to address this gap and to provide consistency with existing MSRB rules.

We also believe this approach serves an important investor protection by alerting investors to occasions when dealers are trading for their own accounts, which may be affecting the prices for their customers' transactions. By having to disclose the time of the dealers' purchases or sales, the amount of mark-up, and the percentage the mark-up represents (as a total of their customers' orders), dealers thus will provide investors information they need to assess the effect on their transactions and their relationships with their dealers.

We also agree with the approach the MSRB has taken in defining the situations in which providing such disclosure on customer confirmations is appropriate. First, the proposed "look through" provision would require dealers who trade securities with affiliates (who hold inventory and trade with other market participants) to "look through" to their affiliates' transactions with the parties with whom they originally bought or sold the securities. In this way, the "look through" would ensure that the disclosed mark-up is a more accurate indication of the compensation paid by customers when dealers and their affiliates effectively function as single entities for purposes of executing retail customers' transactions. We support this requirement and agree that it serves a reasonable objective of winnowing the group of transactions on which dealers would otherwise have to provide disclosure.

In recognizing that certain trading desks of a dealer can operate independently and without knowledge of specific executions handled by other desks, the proposed rule distinguishes between "functionally separate" trading desks in determining which transactions in a customer's account will be subject to the confirmation disclosure. Under amendments to Rule G-15, a dealer would *not* have to disclose the mark-up for a customer transaction if the dealer can establish that:

> (i) the customer transaction was executed by a principal trading desk that is functionally separate from the principal trading desk that executed the dealer's same-side of the market transaction; and (ii) 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 proposing this exemption, the MRSB reasons that this approach recognizes its intent to distinguish between riskless principal trades ("RPTs") and those requiring disclosures. We believe this approach reasonably accomplishes this goal.

Link to EMMA

Even if mark-up disclosure is not required, amended Rule G-15 would still require dealers to provide hyperlinks and URL addresses to the pages on EMMA that provide security details for their customers' accounts and descriptions of what those pages provide. Dealers also would have to disclose the execution times (to the nearest minute) of executions for their customers'

transactions, eliminating the current option for dealers to provide such on as-requested bases. We agree that these two requirements will provide customers with pertinent information and help broaden their understanding of the markets for their securities (and note that certain brokerages already make such information available through their on-line trading systems).

Whether to disclose all dealer transactions with retail customers

The Board also enquired whether all principal dealer transactions with retail customers should be disclosed, regardless of whether the transactions are on the same side of the market as any particular customer trades. While we see some potential for such information to be useful, we do not believe the marginal benefit gained from such disclosures to retail investors would be worth the potential confusion and additional cost providing that information will produce.

In particular, we are worried that the disclosure of all principal transactions with retail customers, rather than only RPTs, will cause "apples-to-oranges" comparisons by investors. Those involving RPTs reflect *de facto* agency trades where dealers are able to acquire the securities quickly either from affiliates or ready sources on the other side of the market. By comparison, non-riskless principal transaction require dealers to seek the securities in the marketplace and in a manner that may require the dealers to put their capital at risk, even for a short time. Likewise, disclosure of principal trades, even RPTs, occurring on different sides of the market may not provide direct comparisons for investors, as the attitudes of buyers is sure to be different from those of sellers. Comparisons of these types, therefore, could add to investor confusion and to higher costs for firms.

Timing Triggers

We do not believe that transactions occurring any time during a day on which a trade has occurred should be included in these types of disclosures by dealers. Rather, we believe the two-hour window is appropriate.

Our reasoning for this perspective is that market prices for securities can change substantially in a matter of seconds, depending on factors affecting the following:

- The supply and demand for a specific set of securities;
- Concerns about a specific type of securities;
- Issuer-specific news;
- Market-specific news;
- Macro-economic news; or
- Global events, among other things.

Market prices reflect the views about value of specific buyers and sellers at specific points in time in consideration of these and other factors. The dynamic nature of these views means that trades that occurred a short time ago may not reflect current sentiments.

Nevertheless, we believe disclosure of prices for dealers' RPTs on similar transactions occurring within a two-hour window can provide relevant comparative information to investors about market sentiment at or near the time of their trades. Therefore, we believe this is an appropriate time window.

Based on research in the corporate bond market by Larry Harris, CFA, of the University of Southern California[2], 73% of all riskless principal trades in corporate and agency securities occur within one minute of the customer's transaction. Furthermore, the Financial Industry Regulatory Authority notes in a companion consultation[3] that "approximately 93 percent of retail-sized customer trades in corporate debt securities with same-sized corresponding principal trades occurred within 10 minutes. Similarly, customer and principal trades occurred within 30 minutes of each other for approximately 96 percent and within two hours for more than 98 percent of the trades." While the municipal market differs in many ways from the corporate and agency debt markets, we believe the data provided by these two independent studies supports the MSRB's attempt to capture all transactions that could be considered riskless principal transactions.

Conclusion

We support the proposed amendments to Rule G-15 that will provide investors with important information pertaining to their account and actions by dealers trading for their own accounts. Should you have any questions about our positions, 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

[2] "Transaction Costs, Trade Throughs, and Riskless Principal Trading in Corporate Bond Markets," 22 October 2015: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2661801.
[3] See: http://www.finra.org/industry/notices/15-36.

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 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.

Schwab Supports Expanding the MSRB's Proposal to Include All Principal Trades

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

[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.

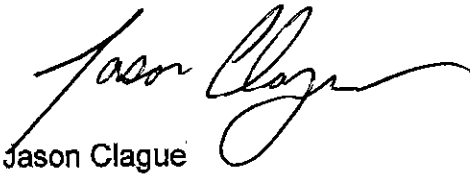
Security-Specific Link to EMMA and TRACE, and Time of Execution

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

Comment on Notice 2015-16

from Chris Melton,

on Friday, October 30, 2015

Comment:

Thank you for permitting me to comment on the proposed amendments to Rule G-15 related to confirmation disclosure. The current draft is a considerable improvement over the original proposal, particularly in the area of the time period for which trades are subject to the new requirement.
Reducing the turn-around time covered by the Rule to two hours will considerably increase the availability of reasonably priced bonds to retail clients and reduce the anti-competitive nature of the requirement. It is likely that some dealers will make bonds unavailable to retail during the time period when mark up disclosure is required. Reducing that time will provide retail clients with a better opportunity to buy the most reasonably priced securities: the cheapest bonds are generally the first out of the door. Reducing the time period subject to the requirement should also reduce the programming necessary for small firms to track the trades subject to the Rule, reducing the anti-competitive nature of the requirement.
Changing the disclosure requirement to mark up also clarified the nature of what is to be disclosed, although there are still any number of scenarios, which neither time nor inclination would result in discussion here, which will require further interpretation by MSRB staff. Additionally, while the requirement to add EMMA information is an improvement, certain logistical matters should be settled before requiring a direct link to CUSIP information. It may be better to provide the link to the EMMA home page for the time being.
Thank you for listening to many of the industry’s concerns on this matter.

Comment on Notice 2015-16

from christopher [last name withheld]

on Friday, September 25, 2015

Comment:

hi ...

as a long-time, individual, retail investor of individual municipal bonds, i find the lack of transparency in purchasing muny bonds quite appalling ...

retail investors are rarely offered the opportunity to buy new issues at the new issue price, and bonds are regularly marked up as the bonds pass from dealer to dealer well before the "when issued" date of the bond ...

at least the emma site provides trade information on bonds, but there remains a ton of information regarding the bond that remains hidden from the general investing public ... in general, there is no transparency in the muny bond market and a market without transparency is an inefficient market ...

any proposal that sheds light on mark-ups as bonds pass from dealer to dealer and from dealer to investor would be welcome to the individual investor ... also, emma should post these mark-ups on their website to improve competition and transparency in the industry ...

for example, if an individual, "when issued" muny bond is being offered at 99.5 to the
retail investor for an investment of $50,000 (ie, the investor pays $49,750), the dealer should quote their markup as well (ie, dealer paid 99 for a mark-up of $250 on this bond) ...

emma should post these markups on their website ...

additionally, emma should provide information on new issues
as to who the underwriter is for the bonds along with contact information ...

i would love to see emma post a calendar of new issues along with underwriter and contact info to improve transparency and better allow
the individual investor to participate in new issue offerings ...

personally, i use the emma site often and applaud emma on doing everything possible to improve transparency in this incredibly opaque marketplace

it all starts with understanding who is doing the underwriting and initial offering of the bond, understanding how the retail investor can take advantage of new issues and how they can contact the underwriter, and finally understanding price mark-ups as bonds pass from dealer to dealer ...

thanks for listening

sincerely

christopher

Consumer Federation of America

December 11, 2015

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, Virginia 22314

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.

[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
Financial Services Counsel

DIAMANT
INVESTMENT CORPORATION

Comprehensive Portfolio Management

November 30, 2015

Ronald W. Smith
Corporate Secretary
MSRB
1900 Duke Street, Ste 600
Alexandria, VA 22314

RE: MSRB Notice 2015-16

Dear Mr. Smith,

Diamant Investment Corporation (Diamant) is making the below constructive comments regarding the above proposed ruling detailed in the MSRB Notice 2015-16 (Proposal). First, I must compliment the MSRB for preparing a well thought out, workable, updated proposal.

My issue is not with much of the wording of the Proposal as it currently stands. Rather my comments focus on the basic issue of having the MSRB remain fixated on creating a principal markup disclosure that is not used in any other industry. What is alarming is the logic of the proposed rule still does not make any business sense.

The Municipal Bond Business

Diamant is a small, self-clearing, municipal 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 municipal bond business, having worked full time at Diamant, our family owned business, for over 37 years. As Diamant does not conduct a riskless business, it should not be directly impacted by this Proposal. It is precisely because of this lack of impact that I am able to step back and comment on what is the wrong direction for the municipal bond marketplace.

Markup disclosure will certainly disrupt parts of the industry, but no case can be made as to why disclosure is needed except that other regulators simply want the MSRB to show they did something. This is a terrible reason for the MSRB, which should be an independent regulatory body, to act. Actually this concept of the MSRB needing to force disclosure on certain trades seems to be an admission that the regulators are simply unable to enforce existing rules. Aside from the occasional inflammatory news article using cherry picked outlier trade data, I have yet to see any proof that overcharging is actually occurring on an industry wide basis. The MSRB has many years of data on every municipal bond trade that occurs, and FINRA conducts substantial audit work on the reasonableness of bond dealers compensation. This trade data has been entered by the industry within 15 minutes of the time of each trade, so it would seem

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reasonable to conclude that both regulators know if overcharging is commonplace. And if so, which bond dealers have a pattern of what may seem like overcharging, and what the circumstances are behind each trade. It would seem rather straightforward to focus regulatory efforts on questionable trades and further review instances where overcharging may occur. Given the detail that went into preparing this Proposal, rest assured such statistics would have prominently displayed as overwhelming proof of this allegation and the reason for such a Proposal. There simply is no industry wide problem that needs solving.

There is a misguided belief such disclosure information will help a customer by forcing more competition, while at the same increasing regulatory compliance costs to dealers that are reducing their supposedly excessive trading revenues. As a regulator, the MSRB should at least have the integrity to admit in this revised Proposal that retail bond trading volumes continue to decline over time, that most bond dealers are not making excessive trading revenues on retail trades, and the MSRB already has existing rules that cover markups that are sufficient to protect the customer. So here we go again, creating this Proposal to solve a problem that does not exist.

Still A Very Bizarre Line Of Reasoning

The tone of the Proposal is 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 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 municipal 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. 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, the MSRB 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.

In the municipal bond business, the retail customer needs the assistance of a professional to navigate the selection of available fixed income products. When a client buys bonds, their most important decision points may include: the income stream; years until their principal is returned; after tax return on the investment; what events can cause the principal to be returned early and what is the impact; what happens to this investment when rates move; what revenue streams secure the interest payment; what assets secure the principal payment; what is the after tax return after state taxation; what other alternatives are available; whether this investment should be made now or 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 makes this Proposal so bizarre is that the MSRB truly believes customers should focus their attention not on important information described above, but instead on the disclosure of a gross trade profit number that is really not terribly relevant to the overall decision to purchase a bond. Rest assured if profits are being reduced, time spent attending to the important customer decision points also will be reduced, and the customer will really be harmed.

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 the 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.

Of course the regulatory reader will respond by saying the disclosure may force the dealer to cut its gross profit and therefore the customer is better served. This is the problem with not having regulators with business experience in the bond industry they regulate. The gross profit is what is used to pay for all the components that keep a bond dealer in business. It is important to understand the difference between the gross profit and the 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.

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 municipal bonds to retail customers, as it is much easier to sell other investment products with a higher sales load.

EMMA

For those who want trade information, EMMA always remains available without charge. Apparently the MSRB believes that that EMMA is not widely used. This simply means such information is not deemed important by most customers. Yet if over time such available disclosure information has not been considered important by most customers, then there is no merit to move forward with this Proposal to mandate disclosure of what customers are already deeming to be unimportant information.

I strongly advocate that the mandate to require a link to EMMA be completely removed from the Proposal for all retail customer confirmations. This is a self-serving component of the Proposal where the MSRB is forcing dealers to place advertising about an MSRB product on every bond confirmation. It becomes a real conflict of interest when a regulatory authority forces dealers to provide free advertising copy on every trade, designed to tout an MSRB product. It seems the underlying reason for forcing EMMA text on every bond confirmation is the hope that usage of EMMA will rise, which will justify greater expenditures by the MSRB to keep the EMMA bureaucracy afloat. None of these reasons serve the retail customer's needs.

If the SEC forces the MSRB to provide such a link, then it would be meaningful only as part of the mark-up disclosures. Such disclosure about EMMA should be limited to the URL address, as one cannot place a hyperlink to a particular CUSIP on a printed paper confirmation. The current EMMA system is very easy to navigate, and anyone can enter a CUSIP without prompting from a link. As EMMA has been available for years to anyone who is interested, there is no benefit in further cluttering up all retail bond confirmations with this information.

Costs and benefits

Costs. Everyone should recognize that in addition to modifications to the processing of confirmations in the back offices, there are ongoing compliance costs brought by this Proposal. Such compliance costs occur even to dealers that do not conduct a riskless business.

Benefits? There are no real benefits to the dealers, and there really are no benefits to the customers. The main reason for proceeding with this Proposal is the philosophical argument that disclosure automatically means prices and markups will decline. I am absolutely certain that the dealers which the MSRB is attempting to target, already employ experienced traders who will find ways to show lower markups on confirmations while still making the same profits trading bonds. And firms with clever lawyers will properly render the disclosure language to become meaningless. At the end of the day, nothing will have changed with disclosure, except the customer will be more confused.

Conclusion

Despite well thought out enhancements, this current Proposal it still is trying to solve problems that do not exist. Most customers are being treated fairly by the markets. Disclosure will certainly create confusion. The proper conclusion must be that the MSRB thoroughly reviewed the matter in a meaningful way, but after careful consideration, decided to take no action in order to continue maintaining an orderly and regulatory compliant market in municipal bonds.

Yours truly,

Herbert Diamant
President

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.

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.

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

[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:

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Ms. Susan Axelrod, Executive Vice President, Regulatory Operations, FINRA
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December 11, 2015

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Office of the Corporate Secretary
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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

FINANCIAL SERVICES INSTITUTE

VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS AND INDEPENDENT FINANCIAL ADVISORS

VIA ELECTRONIC MAIL

December 11, 2015

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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

[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

[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

[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

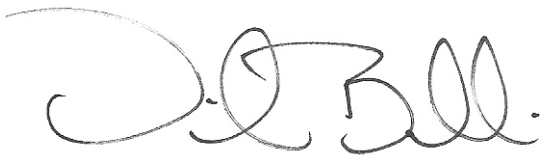
Should FINRA and the MSRB choose to pursue pricing disclosure requirements for retail fixed income transactions where the dealer acts as principal, we believe they should also undertake initiatives to seek to better educate investors about the structure of the secondary fixed income markets. Such education 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,



David T. Bellaire, Esq.
Executive Vice President & General Counsel

THOUGHTS ON THE POSSIBLE NEW DISCLOSURE RULE

I understand the good intentions that have led to the possibility of the New Disclosure Rule. Unfortunately, we all know where the road paved with good intentions leads to.

If this is adopted the customer might think that he/she is better off. Unfortunately the opposite is true. Right now firms can search the whole country for the best bond to satisfy the clients need and then mark it up perhaps one or two points for their efforts. Obviously, if this markup is shown the client is not going to be happy. Under the new procedure there will four classes of brokers:

1. Small firms that do not carry inventory. - These firms will be out of the bond business and all the diversity that they provide will be lost.

2. Small firms that carry inventory – these firms will ONLY show bonds in their inventory. This will result in a very narrow choice for their customers.

3. Large firms that carry inventory – these firms will benefit greatly from the change. The customer will have a larger choice than the small firm can provide, but no matter how large the firm is, it will never equal the choices now available by any firm being able to check for the best bond and the best price. The lack of competition will also allow these firms to put more spread into the bonds (this won't have to be disclosed because it will come from inventory). The customer will pay more or get less but not know it.

4. Discount firms using street inventory- One would think that this would be the ideal solution for the client. Low mark ups and a national inventory. There are two reasons why this will not work.

    A. These firms do not give any advice. All the decisions are left up to the customer. (Their new account forms expressly states that the take no responsibility for customer choices). As all professionals know bonds (especially municipals) are a very complex investment and should not be looked at as something that anyone can decide upon by just using a few metrics such as yield, coupon, maturity, and ratings. Just to give three examples, how many customers are aware of the difference between limited and unlimited go's; extra ordinary redemptions, or how a certificate of participations works. Even if the customer knows enough to ask a question, there is no one to speak to.

    B. The national inventory will not offer the diversity that is now available. Just a handful of large firms will control the market which, for lack of competition, will result in much larger spreads to the street. The customer will pay more or get less on a sale even if the commissions are vastly reduced.

Capitalism is based on competition. By eliminating whole classes of competitors the customers will suffer as to choice and price. Right now I am the fixed income manager of a small firm the does not

keep inventory. I have spent 38 of my 46 year career at several different small firms. I and my RR's have NEVER lost out to a large firm on an order based on competing with the large firm's inventory and price. We offer the inventory of every trading firm in the country and by careful shopping and using judicial mark ups we are always competitive. The only winners under the proposed plan will be the large firms.

The increased spread that will result will not only hurt the retail client. Once again the lack of competition will rear its ugly head and the municipal issuers will pay more to bring their offerings to the market. This means that every single taxpayer will be penalized by this proposal.

In summary this is a classic LOSE – LOSE situation. This customer will think that he/she is saving money when in effect the increased spreads will far exceed the markup savings. This is a cruel hoax that should not be fostered on the small investor. This is in addition to the increased costs that will be borne by the issuers.

One additional thought: There is a sense among regulators that a profit on individual trades is basically unfair. Instead of commissions/mark ups there is pressure to create managed accounts using an annual fee of 1% or more on the value of the account. Under past practices the client who buys 100m bonds might incur a markup of perhaps one to two thousand dollars. Under managed accounts, the customer would pay one thousand dollars **PER YEAR** for as long as the position is kept. I can't see how this benefits the customer.

Sincerely yours,

Gerald Heilpern

914-393-1782

Comment on Notice 2015-16

from Jonathan Bricker,

on Tuesday, October 20, 2015

Comment:

In my opinion we are crossing into an area of over correction. The transparency and rules have handcuffed the municipal securities dealers from the mark ups of the old days. The request to disclose the mark up will not be beneficial to anyone and frankly unjust to the dealers. Is there anyone out there requesting the mark up for all the other service industries? Does a restaurant have to disclose the food mark up on the menu? Does a jeweler have to show his 300% mark up on a diamond? What about the person cutting hair or even the funeral home down the road? Service, selection, and price are the three pillars of sales in that order. When you base everything around price you lose the willingness for the service provider to provide excellent service and what you get in return is mediocre. I'd rather pay a slight premium to know that someone is working on my behalf to get me the best return possible as opposed to the individual that is just trying to get by.
Allow me to make a request. Jennifer Galloway can you send me a copy of your most recent pay stub so I can make sure you're doing your job correctly?

LPL Financial

David P. Bergers
General Counsel

75 State Street
Boston MA 02109
617.423.3644 office

December 10, 2015

Via Electronic Submission

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

Mr. 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:

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]

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[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.

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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 P. Bergers

Morgan Stanley
2000 Westchester Avenue
Purchase, NY 10577

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

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
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

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

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]

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[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.

Current Proposals

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

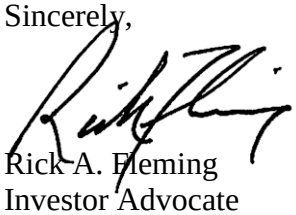
We appreciate the MSRB's and FINRA's acknowledgement of the information disparity inherent in fixed income market transactions, and we support your corresponding efforts to address retail customers' information disadvantage by increasing price transparency and the availability of pricing information. 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.

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Submitted electronically via www.msrb.org

Re: Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers. (Notice 2015-16, Rule G-15)

December 11, 2015

Summary: Investors and all municipal bond market participants will be best served by efforts that encourage transparency and liquidity. The complexity of the proposed amendments to the MSRB rules regarding disclosure of mark-ups will produce disclosures that will be very difficult for most investors to understand. While additional transparency is a good thing and will enhance liquidity, it appears that it would be far more direct to require disclosure of compensation paid to the recommending advisor for all trades conducted in a brokerage relationship, regardless of whether or not a trade was done on a riskless basis.

Having been involved in the municipal bond business for over 30 years, I know from first-hand experience that a healthy and liquid municipal bond market is good for investors and good for issuers.

For a market to operate, there MUST be a difference of opinion between sellers and buyers—otherwise, nothing would ever change hands, whether it is a market for collectible coins, movie scripts, used electronics on eBay, or securities in an over-the-counter market. Economic ignorance leads to the misguided efforts to somehow eliminate those differences of opinion about price and value by characterizing them as "conflicts of interest", a pejorative term which suggests that one party has a hidden agenda in the transaction. Yet it is certainly news to nobody that buyers want to pay less and sellers want to get more and are likely to have conflicting views about what a fair price is. It is only because of those conflicts that markets can thrive and be available to serve the interests of all interested parties. Because of the parties' differing valuations of a security, sellers can find buyers, and vice versa. Without the conflict of opinion as to intrinsic value, buyers may be unable to sell when what they have purchased no longer suits their needs. Knowing that there will be a ready market available when it comes time to sell allows buyers to be more selective when they buy, and also tends to increase the number of potential subsequent buyers. More buyers and more sellers means greater liquidity for everyone.

So it is not the fact of such "conflicts" that regulators and investors should be concerned about—it is rather the lack of transparency about pricing. What everyone should demand is transparency and honesty about the components of price. In the interest of transparency and honesty, I applaud the MSRB for seeking greater transparency in one of the most complex over-the-counter markets.

Even though the municipal bond market looks much different now than it did even a few years ago, as other markets and the availability of information have evolved and become more democratized, the complexity of the municipal bond market (with 60,000+ issuers and more than 1 million CUSIPs) has made keeping pace with changing technology an ever more expensive challenge for municipal dealers. (It requires a significant amount of capital to be a municipal bond dealer—and not just for carrying an inventory of bonds: human capital is scarce and expensive—experienced traders, underwriters, sales people, research analysts, market strategists, risk managers and compliance analysts;

licenses for access to technology and data; keeping pace with middle and back-office technology standards. The list goes on and on.) The forces (and costs) of evolution will continue, and perhaps even at a faster pace.

What will not change: the market for municipal bonds—like all functioning markets—requires the ability of participants to earn a fair return for the amount of capital risked and time invested. Making a market (providing liquidity) in municipal bonds will remain an expensive, capital-intensive and risky business.

Yet there seems to be a growing belief among commentators and some investors that access to the market should be free. Municipal bonds can be a great investment. But in fairness, the dealers who commit capital to provide liquidity and the advisors who commit time to working in the market deserve to be fairly compensated for those efforts—in a way that is commensurate with the efforts (and risks) involved. But what is fair? Some trades will be low risk and involve minimal effort, while others may involve significant amounts of time and risk. The legitimate question of what is fair is best answered in the marketplace. So pursuing transparency is the best course for maintaining the appropriate amount of capital in the market and liquidity for buyers, sellers and issuers.

However, the complexity of the proposed amendments to the MSRB rules regarding disclosure of mark-ups will produce disclosures that will be very difficult for most investors to understand. While additional transparency is a good thing and will enhance liquidity, it appears that it would be far more direct to require disclosure of compensation paid to the recommending advisor for all trades conducted in a brokerage relationship, regardless of whether or not a trade was done on a riskless basis.

The total amount of profit earned on any trade or trading position is a function of many things, not all of which are in the control of the buyer or the dealer. Some of the profit may be due to market changes, clearly not a factor that any particular dealer can control. Some will be because of the compensation to be paid to the recommending advisor, who deserves payment for the time involved in finding the security and evaluating its usefulness to the client. Suggesting to buyers that the amount of total profit on a trade is relevant to the judgment of the appropriateness of the particular bonds is not on point. What is relevant is the fairness of the compensation earned by the person making the recommendation. *Salespeople and advisors are entitled to a fair compensation—let that amount be fully and consistently disclosed.* The additional spreads earned by the firms' trading accounts are not involved in the "conflict" between the recommending advisor and the investing buyer.

For investors buying their municipal bonds within a fee-based relationship, trade confirmations should note that the fees paid for advice have been agreed to in advance, and are not relevant to the execution.

Sincerely,
Patrick Luby

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December 8, 2015

Submitted via email to pubcom@finra.org
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Submitted electronically
Ronald W. Smith
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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.

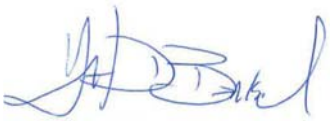
Abuse of undisclosed markups and markdowns is not a hypothetical problem. The last few years have seen FINRA pursue a number of disciplinary actions against member firms concerning excessive markups and markdowns of debt instruments. For example, in 2012, FINRA fined Citi International Financial Services 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

[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.

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December 15, 2015

BY ELECTRONIC MAIL

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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:

RBC Capital Markets, LLC ("RBC CM") 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").

RBC CM is a wholly owned subsidiary of the Royal Bank of Canada. The Royal Bank of Canada is a publicly traded company (RY on TSX and NYSE), RBC CM is a dually registered broker-dealer and investment advisor, As of October 31, 2015, RBC CM's Wealth Management US division had over $216 billion in client assets under administration.

The municipal banking, underwriting and distribution resources of RBC CM represent one of the largest and most diverse teams of capital markets professionals in the industry. We provide complete coverage for investors in municipal bonds:

- Top five underwriter by par amount for senior negotiated issues in 2015;
- More than 70 fixed-income institutional sales professionals covering Tier I, II and III investors, including approximately 30 dedicated municipal salespeople;
- Over 30 municipal traders and underwriters;
- More than 1,800 financial consultants operating from 175 different offices in 42 states;

- RBC CM's Wealth Management retail business is ranked as one of the world's top 10 largest wealth managers;
- RBC CM maintains an extensive inventory of fixed income securities and also sources securities from third parties, to provide liquidity to its customers on both sides of the market.

RBC CM supports efforts to enhance bond market price transparency in a way that provides retail investors with useful, clear, and consistent insight into their transactions. We have been actively involved in developing the advocacy of the Securities Industry Financial Markets Association ("SIFMA") on a wide range of issues, including fixed income market structure. RBC CM supports SIFMA's most recent comment letter[1] (the "SIFMA Letter") responding to the Proposals.

The SIFMA Letter requests: 1) a confirmation disclosure requirement uniform in design and operation; 2) 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"); 3) 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; 4) should some version of the Proposals 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 potential alternative approach is a daily volume weighted average (market) price ("VWAP").

RBC CM writes to add further support to adopting a framework that permits measuring the price to the customer against an objective measurement, such as a VWAP, or some other formula that is more in alignment with the FINRA Proposal (as well as the MSRB's initial proposal contained in MSRB Notice 2014-20). We believe that disclosure that is measured against an objective factor provides greater clarity, introduces certainty, reduces operational risk, and is more easily auditable – both internally and externally. We are also supportive of an approach that is system driven and can be automated. We believe a manual or subjective process introduces unnecessary operational and regulatory risk, as well as customer confusion.

Taken together with dealer's obligation for best execution, fair and reasonable pricing, and new confirmation disclosure of a reference price, and direct CUSIP links to EMMA and TRACE, a retail customer will have a greatly improved information to evaluate their trade.

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[1] *See* letter from Leslie Norwood and Sean Davy, SIFMA, to Marcia E. Asquith, FINRA, and Ronald W. Smith, MSRB, (December 11, 2015), available at http://www.sifma.org/issues/item.aspx?id=8589957983

RBC CM thanks FINRA and the MSRB for the opportunity to comment on the Revised Proposals and welcomes the opportunity to discuss them with you. Should you have any questions, please do not hesitate to contact me at 212-847-8805 or david.l.cohen@rbccm.com.

Sincerely,

David L. Cohen
Senior Counsel and Director

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 22314-3412

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

sifma
Invested in America

December 11, 2015

BY ELECTRONIC MAIL

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
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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

[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

[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.

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[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.

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[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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THOMSON REUTERS

Via Electronic Delivery

December 11, 2015

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FINRA
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Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
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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.

[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.

[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
Chief Regulatory Officer, Wealth Management
Thomson Reuters

[8] See MSRB Regulatory Notice 2015-07 published May 26, 2015 announcing a May 23, 2016 implementation date.

December 11, 2015

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

Request for Comment on Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transaction with Retail Customers

Dear Mr. Smith:

TMC Bonds, L.L.C. ("TMC") welcomes the opportunity to respond to the Municipal Securities Rulemaking Board's ("MSRB") Request for Comment on Confirmation Disclosure for Mark-ups for Specified Principal Transactions. 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 FINRA has filed a similar request for comment in Regulatory Notice 15-36, 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 (using TMC's 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 MSRB 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 the MSRB's RFQ states that 50% of principal trades would be disclosed under the 2 hour suggested window. 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 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 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 the MSRB. 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 MSRB 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 MSRB 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

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Member FINRA/SIPC

December 11, 2015

Via e-mail: ***pubcom@finra.org***
http://www.msrb.org/CommentForm.aspx

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

Mr. 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 & 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. FINRA and MSRB Should Revive Mark-up Disclosure for Riskless Principal Transactions As A Workable Alterative.

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. FINRA Must Exempt Institutional Customers From the Revised Proposal.

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

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

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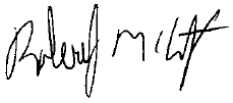
[6] Delivery Versus Payment (DVP) and Receive Versus Payment (RVP) accounts do not meet the "institutional account" definition, but rely on the institutional confirmation process.

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

MSRB
Municipal Securities Rulemaking Board

Regulatory Notice

2016-07

Publication Date
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Stakeholders
Municipal Securities Dealers, Investors

Notice Type
Request for Comment

Comment Deadline
March 31, 2016

Category
Uniform Practice

Affected Rules
Rule G-30

Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price

Overview

The Municipal Securities Rulemaking Board (MSRB) is seeking comment on draft amendments to MSRB Rule G-30, on prices and commissions, to provide guidance on establishing the prevailing market price and calculating mark-ups and mark-downs for principal transactions in municipal securities (the "Draft Guidance"). The MSRB believes additional guidance on these subjects may promote consistent compliance by brokers, dealers and municipal securities dealers (collectively, "dealers") with their existing fair-pricing obligations under MSRB rules, in a manner that would be generally harmonized with the approach taken in other fixed income markets. The MSRB also believes additional guidance could be necessary for the effective implementation of a potential future mark-up disclosure requirement.

Comments should be submitted no later than March 31, 2016, and may be submitted in electronic or paper form. Comments may be submitted electronically by clicking here. Comments submitted in paper form should be sent to Ronald W. Smith, Corporate Secretary, Municipal Securities Rulemaking Board, 1300 I Street NW, Suite 1000, Washington, DC 20005. Generally, all comments will be made available for public inspection on the MSRB's website.[1]

Questions about this notice should be directed to Michael L. Post, General Counsel – Regulatory Affairs, Margaret Blake, Associate General Counsel, or Saliha Olgun, Assistant General Counsel, at 202-838-1500.

[1] Comments generally are posted on the MSRB website without change. For example, personal identifying information such as name, address, telephone number, or email address will not be edited from submissions. Therefore, commenters should only submit information that they wish to make available publicly.

Background

The MSRB is charged by Congress to promote a fair and efficient municipal securities market and to protect investors and the public interest.[2] Under this mandate, the MSRB has developed and adopted a detailed set of regulatory requirements regarding dealer pricing and compensation. Rule G-30 generally provides that a dealer may only purchase municipal securities for its own account from a customer, or sell municipal securities for its own account to a customer, at an aggregate price (including any mark-up or mark-down (collectively, "mark-up")) that is fair and reasonable.[3] The "prevailing market price" of a municipal security is a central concept in Rule G-30. Under Rule G-30, the total transaction price to the customer must bear a reasonable relationship to the prevailing market price of the security,[4] and, in a principal transaction, the dealer's compensation (*i.e.*, the mark-up) must be computed from the inter-dealer market price prevailing at the time of the customer transaction.[5] Moreover, Rule G-30 obligates dealers to exercise reasonable diligence in establishing the market value of the security and the reasonableness of their compensation.[6] Thus, the MSRB has previously cautioned that it is possible for a dealer to charge reasonable compensation and still violate Rule G-30 because of insufficient attention to market value.[7]

MSRB Rule G-15, on confirmation, clearance, settlement and other uniform practice requirements with respect to transactions with customers, in relevant part, requires dealers to disclose on the customer confirmation remuneration to be received from a customer when the dealer acts as agent (*i.e.,* the commission). However, there is currently no comparable requirement with respect to disclosure of the mark-up when the dealer acts as principal.

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[2] *E.g.*, Securities Exchange Act of 1934 § 15B(b)(2)(C), 15 U.S.C. 78o-4(b)(2)(C).

[3] MSRB Rule G-30(a).

[4] Rule G-30(a); Rule G-30, Supplementary Material .01(c).

[5] Rule G-30, Supplementary Material .01(d).

[6] Rule G-30, Supplementary Material .01(a); Rule G-30, Supplementary Material .04(b) ("[D]ealers must establish market value as accurately as possible using reasonable diligence under the facts and circumstances."). The draft amendments include a clarification of this reasonable diligence standard in Supplementary Material .01(a).

[7] Review of Dealer Pricing Responsibilities - January 26, 2004 (archived and available at www.msrb.org).

In September 2015, the MSRB published MSRB Notice 2015-19 seeking comment on draft rule amendments to require dealers to disclose the mark-up on retail customer confirmations for specified principal transactions (the "mark-up disclosure proposal"). Under the proposal, dealers generally would be required to disclose the mark-up on retail customer confirmations 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 transaction.[8] The mark-up to be disclosed, consistent with Rule G-30, would be computed from the prevailing market price for the security at the time of the customer transaction. The MSRB specifically sought comment as to whether dealers could benefit from additional regulatory guidance on the establishment of prevailing market price and the calculation of mark-ups for the class of principal transactions specified in the proposal, or for all principal transactions with customers. In a coordinated effort, the Financial Industry Regulatory Authority (FINRA) also published a related, but not identical, confirmation disclosure proposal for other fixed income securities markets, which also requested comment on the MSRB's mark-up disclosure proposal.[9]

In response to the mark-up disclosure proposal, commenters strongly urged a coordinated and consistent approach to confirmation disclosure by the MSRB and FINRA for the fixed income securities markets. A number of commenters also indicated that additional guidance on prevailing market price would be beneficial to support effective compliance with a possible future mark-up disclosure requirement. Some commenters noted that while dealers may currently have in place processes and systems that are designed to ensure that their mark-up on a principal transaction is fair and reasonable and that the total transaction price to a customer bears a reasonable relationship to the prevailing market price of the security, the specificity with which dealers would need to ascertain the prevailing market price of a security under the mark-up disclosure proposal would require additional guidance.

These recent suggestions of additional guidance are consistent with a recommendation in the Securities and Exchange Commission's (SEC) Report

[8] Under the proposal, dealers also would be required to include on all retail customer confirmations a CUSIP-specific link to the MSRB's Electronic Municipal Market Access (EMMA®) website.

[9] *See* FINRA Regulatory Notice 15-36 (Oct. 2015).

on the Municipal Securities Market.[10] The SEC Report recommended that the MSRB consider providing more detailed guidance on how dealers should establish the prevailing market price for municipal securities and recommended consistency with guidance issued by FINRA for non-municipal fixed income securities.[11]

FINRA Guidance

For principal transactions in non-municipal fixed income securities, the prevailing market price and mark-up generally must be determined in accordance with FINRA Rule 2121, including Supplementary Material .01, Mark-Up Policy, and Supplementary Material .02, Additional Mark-Up Policy for Transactions in Debt Securities, Except Municipal Securities. Supplementary Material .02 was approved by the SEC and became effective in 2007 (the "FINRA Guidance").[12] Under the FINRA Guidance, the prevailing market price of a security generally is presumptively established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained. This presumption may be overcome in limited circumstances. If the presumption is overcome, or if it is not applicable because the dealer's cost is (or proceeds are) not contemporaneous, various factors are either required or permitted to be considered, in successive order, to determine the prevailing market price. Generally, a subsequent factor or series of factors may be considered only if previous factors in the hierarchy, or "waterfall," are inapplicable.

Summary of Draft Prevailing Market Price Guidance

The Draft Guidance, which would be codified in a new paragraph .06 of the Supplementary Material to Rule G-30, is designed to harmonize the manner in which the "prevailing market price" for municipal securities is determined with the manner established by FINRA for purposes of other types of fixed income securities, to the extent appropriate in light of the differences between the markets. As discussed in detail below, like many commenters on the mark-up disclosure proposal, the MSRB believes that consistency and harmonization of regulatory standards regarding the same subject matter and affecting, in many instances, the same regulated persons would increase efficiencies in regulation and reduce dealer implementation and compliance

[10] *See* U.S. Securities and Exchange Commission, Report on the Municipal Securities Market (July 31, 2012) ("SEC Report").

[11] *See id.* at 148. The MSRB previously sought public comment on draft interpretive guidance on these subjects in 2010. *See* MSRB Notice 2010-10 (April 21, 2010).

[12] The descriptions in this notice of the FINRA Guidance are based on the MSRB's understanding of that guidance.

costs. The MSRB believes that this is particularly the case with respect to a possible future mark-up disclosure requirement. The MSRB's consideration of harmonized guidance regarding prevailing market price is also consistent with the SEC's recommendation in the SEC Report.

At the same time, the MSRB is conscious of the unique characteristics of the municipal securities market, including the large number of issuers and outstanding securities, the infrequent trading of many securities in the secondary market, differing tax rules and treatment, and different credit structures, enhancements and redemption features that may not be applicable to or prevalent for other fixed income securities. Accordingly, the Board is concerned that a wholesale application of the FINRA Guidance to the municipal securities market, absent modifications or additional explanatory material to take into account the differences between the markets, in some cases, would result in inaccurate assessments of the prevailing market price and, consequently, inaccurate calculations of mark-ups.

With these issues in mind, the Draft Guidance on which the MSRB seeks comment was developed to be substantially similar to the FINRA Guidance, with modifications intended to tailor it to the characteristics of the municipal securities market. To help ensure appropriate tailoring, the MSRB seeks comment as to the appropriateness of this generally harmonized approach and, particularly, whether the modifications are appropriate and whether additional modifications should be made.

Rebuttable Presumption Based on Contemporaneous Cost or Proceeds. Under the FINRA Guidance, the prevailing market price of a non-municipal fixed income security is presumptively established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained, consistent with FINRA pricing rules, such as the best-execution rule (FINRA Rule 5310). A transaction is contemporaneous under the FINRA Guidance if it occurs close enough in time that it would reasonably be expected to reflect the current market price for the subject security. A dealer may be able to show that its contemporaneous cost (when it is making a sale to a customer) or proceeds (when it is making a purchase from a customer) are not indicative of the prevailing market price, and thus overcome the presumption, in instances where: (i) interest rates changed after the dealer's contemporaneous transaction to a degree that such change would reasonably cause a change in debt securities pricing; (ii) the credit quality of the debt security changed significantly after the dealer's contemporaneous transaction; or (iii) news was issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the debt security after the dealer's contemporaneous transaction. The Draft Guidance

follows these same policies for transactions in municipal securities, but, instead of referring to consistency with FINRA rules, refers to consistency with applicable MSRB rules, such as MSRB Rule G-18, on best-execution.

The MSRB invites comment as to whether there may be additional instances in the municipal market in which a dealer may be able to show that its contemporaneous cost or proceeds are not indicative of the prevailing market price. For example, should a dealer be able to overcome the presumption when there are intervening changes in yields against a widely used benchmark to such a degree that it would reasonably cause a change in municipal securities pricing? If so, are there any situations involving such changes in yield that would not already be adequately identified as associated with changes in interest rates or the issuance or distribution of news? Should trade size be included as a relevant consideration in either identifying a contemporaneous transaction or overcoming the above presumption, or do market participants believe that a contemporaneous transaction, regardless of trade size, is the most relevant and probative evidence of the prevailing market price for the security?

Hierarchy of Pricing Factors. Under the FINRA Guidance, if the dealer has established that the dealer's cost is (or proceeds are) not contemporaneous or if the dealer has overcome the presumption that its contemporaneous cost or amount of proceeds provides the best measure of the prevailing market price, the dealer must consider, in the order listed, a hierarchy of three additional types of pricing information: (i) prices of any contemporaneous inter-dealer transactions in the security; (ii) prices of contemporaneous dealer purchases (or sales) in the security from (or to) institutional accounts with which any dealer regularly effects transactions in the same security; or (iii) if an actively traded security, contemporaneous bid (or offer) quotations for the security made through an inter-dealer mechanism, through which transactions generally occur at the displayed quotations. Pricing information of a succeeding type may only be considered where the prior type does not generate relevant pricing information. In reviewing the available pricing information of each type, the relative weight of the information depends on the facts and circumstances of the comparison transaction or quotation. The Draft Guidance follows all of these same policies,[13] but includes explanatory material that makes explicit the

[13] These FINRA policies and those discussed regarding similar securities are generally consistent with, though more detailed than, those currently embodied in Rule G-30. For example, under Rule G-30, dealer compensation with respect to a principal transaction "is computed from the inter-dealer market price prevailing at the time of the customer transaction." Rule G-30, Supplementary Material .01(d). Also under Rule G-30, a dealer "may

expectation that these factors may frequently not be available for municipal securities. This explanatory material and the tailored treatment of isolated transactions and quotations under the Draft Guidance (discussed below) recognize that dealers may often need to consult factors further down the waterfall, such as "similar" securities and economic models, to identify sufficient relevant and probative pricing information to establish the prevailing market price of a municipal security.

The MSRB seeks comment as to all aspects of the hierarchy of pricing factors. Is the hierarchical approach an appropriate one for the municipal securities market? Are there any other factors that should be expressly included at this point in the process for establishing the prevailing market price? Is the requirement that the municipal security be actively traded in order for the dealer to consider quotations for the security an appropriate requirement, or should quotations be permitted to be considered for inactively traded securities?

Similar Securities. Under the FINRA Guidance, if the above factors are not available, other factors may be taken into consideration in establishing the prevailing market price. The FINRA Guidance sets forth a non-exclusive list of factors that are generally analogous to those set forth under the hierarchy of pricing factors described above, but applied here to prices and yields of specifically defined "similar" securities. These factors related to similar securities, however, are not required to be considered in a particular order or particular combination. The relevant weight of the pricing information obtained from these factors depends on the facts and circumstances surrounding the comparison transaction, such as whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction and the timeliness of the information.

Under the FINRA Guidance, a "similar" security should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor. At a minimum, the security or securities should be sufficiently similar that a market yield for the subject security can be fairly estimated from the yields of the "similar" security or securities. Where a security has several components, appropriate consideration may also be given to the prices or yields of the various components of the security. The FINRA Guidance also sets forth a number of factors that may be used in determining the degree to which a security is "similar," including: (i) credit quality considerations; (ii) the extent to which the spread at which the

need to review recent transaction prices for the issue or transaction prices for issues with similar credit quality and features as part of its duty to use diligence to determine the market value of municipal securities." Rule G-30, Supplementary Material .04(b)(i).

"similar" security trades is comparable to the spread at which the subject security trades; (iii) general structural characteristics and provisions of the issue; and (iv) technical factors.

Also under the FINRA Guidance, when a security's value and pricing is based substantially on, and is highly dependent on, the particular circumstances of the issuer, including creditworthiness and the ability and willingness of the issuer to meet the specific obligations of the security (often referred to as "story bonds"), in most cases other securities will not be sufficiently similar, and therefore, other securities may not be used to establish the prevailing market price.

The Draft Guidance follows all of these same policies, but includes an additional factor that may be used in determining the degree to which a security is "similar." The additional factor is the extent to which the federal and/or state tax treatment of a potentially "similar" municipal security is comparable to the tax treatment of the subject security. The MSRB seeks comment as to whether there should be different or additional factors that may be taken into consideration in identifying the degree to which a security is "similar" under the Draft Guidance. Do commenters believe that any additional guidance is warranted for "similar" municipal securities in light of the facts that there are many more municipal security issuers than, for example, corporate bond issuers, many more municipal CUSIP numbers than corporate CUSIP numbers, and secondary market trading in many municipal securities is not as active as it is for many other fixed income securities?

Isolated Transactions and Quotations. Under the FINRA Guidance, because the ultimate issue that the guidance is intended to address is the prevailing market price of the security, isolated transactions or isolated quotations generally will have little or no weight or relevance in establishing the prevailing market price. The Draft Guidance follows the same policy and adds explanatory material to the statement of this policy in light of the fact that isolated transactions and isolated quotations may be more prevalent in the municipal securities market than other fixed income markets. This material explains that, for example, in considering the factors in the hierarchy of pricing factors, a dealer may give due regard to whether the relevant pricing information is being derived from an isolated transaction or quotation.

The MSRB invites comment in particular as to whether this treatment of isolated transactions and quotations is appropriate given that, in the municipal securities market, the existence of only isolated transactions or quotations may be a more frequent occurrence than in other fixed income securities markets. Do commenters believe that additional guidance is necessary with respect to the treatment of isolated transactions or

quotations under specific circumstances likely to arise in the municipal securities market? If so, please describe such circumstances. Or do commenters agree that, if using guidance substantially the same as the FINRA Guidance, it would simply be the case that consideration of factors further down the waterfall will be more likely, as a matter of application of the guidance, in the municipal securities market? Do commenters believe that the proposed expanded explanatory material regarding the weight and relevance of isolated transactions and quotations provides dealers with an appropriate degree of flexibility to take into consideration factors at lower levels in the waterfall in the event that the only transactions or quotations for the subject security are isolated ones?

Economic Models. Under the FINRA Guidance, if information concerning the prevailing market price of a security cannot be obtained by applying any of the factors at the higher levels of the waterfall, dealers may consider as a factor in assessing the prevailing market price of a security the prices or yields derived from economic models. Such economic models may take into account measures such as credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value, and may consider all applicable pricing terms and conventions used. The Draft Guidance follows this same policy.

The MSRB invites comment as to whether dealers currently utilize economic models within their firms to establish the prevailing market price of municipal securities, and if so, to what degree. If used, are such models typically considered earlier in the analytical process or, consistent with the Draft Guidance, are they considered only after consulting relevant trade prices and quotations? Do commenters agree with the measures set forth in the Draft Guidance of which economic models may take account in determining prevailing market price, or should other or fewer measures apply in the municipal securities market?

Figure 1 below provides an overview of the Draft Guidance.

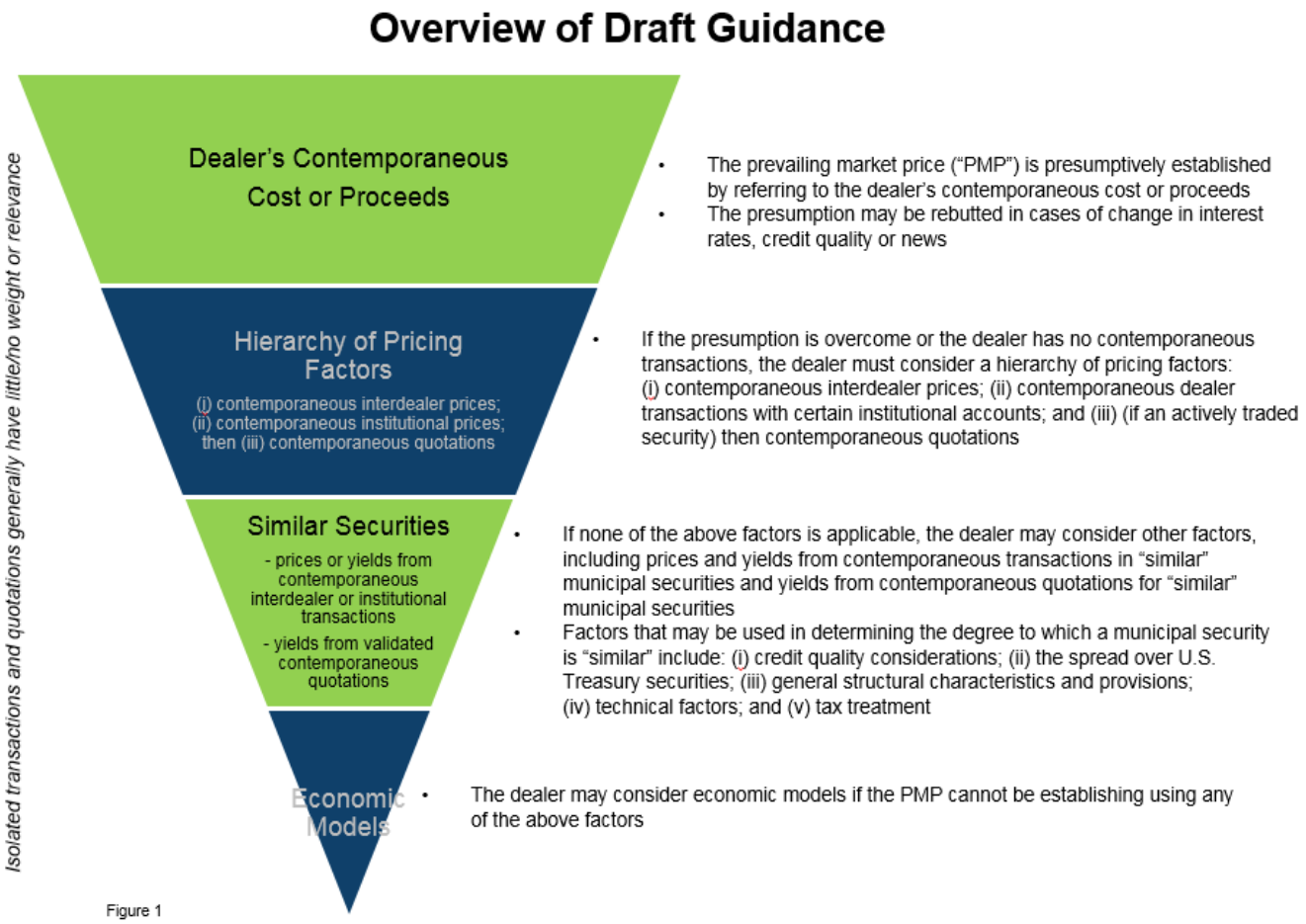

Figure 1

Economic Analysis

1. The need for the Draft Guidance.

As noted above, the need for the Draft Guidance arises primarily from the comments received in response to the MSRB's mark-up disclosure proposal. A number of commenters stated that at least some additional guidance would be necessary in order for dealers to comply with the proposal. In the absence of additional guidance, dealers may find it difficult to confidently calculate the prevailing market price of a municipal security with the specificity required by the MSRB's mark-up disclosure proposal. Commenters also strongly urged a coordinated and consistent approach to confirmation disclosure between the MSRB and FINRA, expressing support for providing disclosures in a manner that is consistent across fixed income markets. Specific guidance currently exists to assist dealers in determining the

prevailing market price of their non-municipal fixed income securities, while such specific guidance does not currently exist for municipal securities. To the extent that FINRA and the MSRB both proceed with a confirmation disclosure initiative that uses the prevailing market price of a security as a point of reference, this inconsistency in guidance could harm investors and could create a burden on dealers by potentially implying significantly different implementation approaches in response to any future MSRB or FINRA rules related to confirmation disclosure. The SEC Report recommended the MSRB consider providing additional prevailing market price guidance, independent of consideration of any mark-up disclosure initiative.[14]

In addition, because mark-ups on principal transactions have been the focus of significant attention,[15] additional guidance on the manner in which prevailing market prices for municipal securities should be determined may support dealer efforts to ensure they are in compliance with their existing obligations under Rule G-30 and make the enforcement of Rule G-30 more efficient.

The Draft Guidance would address these needs by providing a set of principles upon which dealers may rely under a wide range of market conditions. Because these principles are substantially similar to those already promulgated by FINRA, the Draft Guidance would support the goal of consistency across fixed income markets.

2. Relevant baselines against which the likely economic impact of elements of the Draft Guidance should be considered.

The relevant baseline against which the likely economic impact of the Draft Guidance should be considered is existing Rule G-30 that obligates dealers to "exercise diligence in establishing the market value [of a security] . . . and the reasonableness of the compensation" when effecting a trade on a principal

[14] SEC Report at 148.

[15] *See, e.g., id*. at 115-116, 123-126; 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, and Michael S. Piwowar, Commissioner, SEC, Remarks at the 2014 Municipal Finance Conference presented by The Bond Buyer and Brandeis International Business School (Aug. 1, 2014) available at http://www.sec.gov/News/Speech/Detail/Speech/1370542588006.

basis.[16] Rule G-30 also clearly establishes that the "prevailing market price" is the basis for evaluating whether prices are "fair and reasonable"[17] and for determining the amount of the dealer's mark-up or mark-down.[18] The baseline against which the likely economic impact of the Draft Guidance should be considered thus assumes that dealers currently have in place policies, procedures and systems necessary to exercise diligence in determining the prevailing market price of a security and assure that their mark-ups charged are reasonable when effecting a transaction.

In addition, for those dealers that transact in both municipal securities and corporate or agency debt securities, the FINRA Guidance may represent a baseline to the extent dealers are utilizing this guidance to determine the prevailing market price of municipal securities.

3. Identifying and evaluating reasonable alternative regulatory approaches.

The MSRB recognizes that there are alternatives to the approach taken in the Draft Guidance.

The MSRB could continue to rely on the existing guidance included in Rule G-30. While this approach would not place any additional burdens on dealers to modify existing policies, procedures or systems, it may make compliance with any potential MSRB mark-up disclosure requirement more burdensome or costly and would likely result in less consistent approaches to mark-up disclosure across fixed income markets which could increase confusion among market participants.

Alternatively, the MSRB could adopt guidance for determining the prevailing market price of municipal securities that diverges substantially from the FINRA Guidance. For example, the MSRB could adopt guidance that offers dealers significantly greater flexibility in determining which factors should be used. While the MSRB recognizes that such an approach could, under some circumstances, reduce compliance costs, the MSRB believes, at this stage in the rulemaking process, that the benefits of harmonization to the greatest extent possible likely provide benefits to dealers and investors that significantly outweigh the benefits of divergence.

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[16] Rule G-30, Supplementary Material .01(a).

[17] Rule G-30, Supplementary Material .01(c).

[18] Rule G-30, Supplementary Material .01(d).

Finally, the MSRB could adopt the FINRA Guidance without any modifications intended to accommodate ways in which the municipal securities market may differ from other fixed income markets. Particularly for dealers already complying with the FINRA Guidance, this alternative may represent a lower burden than the Draft Guidance. Nonetheless, the MSRB believes promulgating guidance that is identical to the FINRA Guidance and lacking any additional tailored explanatory material could, at times, result in inaccurate assessments of prevailing market prices and, consequently, inaccurate calculations of mark-ups.

4. Assessing the benefits and costs of the Draft Guidance.

The MSRB policy on economic analysis in rulemaking addresses consideration of the likely costs and benefits of the rule with the draft amendments fully implemented against the context of the economic baseline discussed above. The MSRB is seeking, as part of this request for comment, data or studies relevant to the determination of prevailing market price, the costs of implementing the systems and processes necessary to comply with the Draft Guidance, and the potential unintended or indirect economic consequences of the Draft Guidance. Preliminarily, the MSRB has evaluated the benefits and costs associated with the proposed amendments as follows:

Benefits

The MSRB believes that the Draft Guidance reflects an appropriate balance between consistency with existing FINRA Guidance for determining prevailing market price in other fixed income securities markets and modifications to address circumstances under which use of the FINRA Guidance in the municipal securities market might be inappropriate.

Consistency and harmonization between regulatory standards regarding the same subject matter and affecting, in many instances, the same regulated persons may reduce the burdens, costs, and time associated with dealer implementation and compliance and make enforcement more efficient. The MSRB also believes that harmonization could ultimately result in more consistent disclosures and expectations for retail investors across their fixed income security holdings. Harmonized prevailing market price and mark-up guidance between the MSRB and FINRA could also provide dealers with greater certainty in their current fair-pricing compliance processes and any potential future confirmation disclosure processes. In addition, harmonized guidance could provide investors with clearer expectations with regard to dealer obligations across markets. To the extent guidance is harmonized, dealers that effect transactions in other fixed income securities may also be

able to leverage existing processes developed to comply with FINRA Rule 2121 to comply with their Rule G-30 obligations.

Costs

Our analysis of the potential costs does not consider all of the costs associated with the proposal, but instead focuses on the incremental costs attributable to it that exceed the baseline state. The costs associated with the baseline state are, in effect, subtracted from the costs associated with the draft amendments to isolate the costs attributable to the incremental requirements of the Draft Guidance.

The MSRB believes that the Draft Guidance would likely require dealers to modify their existing policies, procedures, and systems currently used to ensure compliance with Rule G-30. These changes may, in turn, affect other aspects of a dealer's daily operations which could result in higher costs, particularly for those securities for which the determination of a prevailing market price cannot be automated.

The MSRB is not aware of any available data that would support a quantitative estimate of the overall impact of the Draft Guidance. The MSRB specifically seeks comments that would inform a quantitative estimate of the benefits and costs associated with the Draft Guidance.

Effect on Competition, Efficiency, and Capital Formation

The MSRB believes that the Draft Guidance may improve capital formation, competition, and efficiency to the extent it results in more competitive pricing and increased investor confidence in the municipal securities market. The MSRB acknowledges, however, that under some circumstances more detailed guidance may reduce efficiency. The MSRB recognizes that larger dealers, and particularly those with significant experience with the FINRA Guidance, may be able to implement the Draft Guidance at a lower cost than smaller firms and/or firms that only transact in municipal securities. On the other hand, firms that hold inventories for relatively short periods of time and, therefore, may be able to more frequently rely on contemporaneous cost or proceeds to determine prevailing market price, may find the ongoing cost of complying with the Draft Guidance to be relatively limited.

Request for Comment

In addition to the questions asked elsewhere in this request for comment, the MSRB seeks public comment on the following questions, as well as any other comments on the subjects of prevailing market price and mark-up calculation. The MSRB welcomes information regarding the potential to quantify the likely benefits and costs of the Draft Guidance. The MSRB also

requests comment on any competitive or anticompetitive effects, as well as efficiency and capital formation effects of the Draft Guidance on any market participants. The MSRB particularly welcomes statistical, empirical, and other data from commenters that may support their views and/or support or refute the views or assumptions or issues raised in this request for comment.

1. Do the principles laid out in the Draft Guidance represent the appropriate approach to establishing prevailing market price in the context of the municipal securities market?

2. Does the Draft Guidance provide dealers with additional helpful guidance for purposes of complying with their fair-pricing obligations under Rule G-30?

3. Would the Draft Guidance provide dealers with sufficient guidance to calculate their mark-ups for purposes of complying with a potential mark-up disclosure requirement where dealers had a corresponding trade(s) within two hours, on the same trading day, or regardless of whether dealers had a corresponding trade(s)?

4. Are there other viable alternatives to the Draft Guidance not identified in this request for comment?

5. Would the Draft Guidance impose any burden on competition that is not necessary or appropriate?

6. To what extent are dealers currently utilizing the FINRA Guidance or a similar approach to establish the prevailing market price of municipal securities?

7. Has the MSRB correctly described the baseline against which the costs and benefits of the Draft Guidance should be measured?

8. How should the MSRB evaluate the potential benefits of consistency with the FINRA Guidance?

9. Would the Draft Guidance impose any cost or burdens, direct, indirect, or inadvertent, on investors or regulated entities other than those identified in this request for comment?

10. Please provide data or other evidence including studies or research that support commenters' estimates of benefits and costs that would be associated with the Draft Guidance and any potential reasonable alternatives.

11. What system changes would be required to comply with the Draft Guidance and what are the estimated costs associated with those changes?

February 18, 2016

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Text of Draft Amendments*

Rule G-30: Prices and Commissions

(a) *Principal Transactions*.

No broker, dealer or municipal securities dealer shall purchase municipal securities for its own account from a customer, or sell municipal securities for its own account to a customer, except at an aggregate price (including any mark-up or mark-down) that is fair and reasonable.

(b) *Agency Transactions*.

(i) Each broker, dealer and municipal securities dealer, when executing a transaction in municipal securities for or on behalf of a customer as agent, shall make a reasonable effort to obtain a price for the customer that is fair and reasonable in relation to prevailing market conditions.

(ii) No broker, dealer or municipal securities dealer shall purchase or sell municipal securities as agent for a customer for a commission or service charge in excess of a fair and reasonable amount.

Supplementary Material

.01 General Principles.

(a) Each broker, dealer or municipal securities dealer (each, a "dealer," and collectively, "dealers"), whether effecting a trade on an agency or principal basis, must exercise <u>reasonable</u> diligence in establishing the market value of the security and the reasonableness of the compensation received on the transaction.

(b) – (c) No change.

* Underlining indicates new language; strikethrough denotes deletions.

(d) Dealer compensation on a principal transaction with a customer is considered to be a mark-up or mark-down that is computed from the ~~inter-dealer market price~~ prevailing market price at the time of the customer transaction. As part of the aggregate price to the customer, the mark-up or mark-down also must be a fair and reasonable amount, taking into account all relevant factors.

(e) No change.

.02 - .05 No change.

.06 Mark-Up Policy

(a) Prevailing Market Price

(i) A dealer that is acting in a principal capacity in a transaction with a customer and is charging a mark-up or mark-down must mark-up or mark-down the transaction from the prevailing market price. Presumptively for purposes of this Supplementary Material .06, the prevailing market price for a municipal security is established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained, consistent with applicable MSRB rules. (*See, e.g.,* Rule G-18).

(ii) When the dealer is *selling* the municipal security to a customer, countervailing evidence of the prevailing market price may be considered only where the dealer made no *contemporaneous purchases* in the security or can show that in the particular circumstances the dealer's *contemporaneous cost* is not indicative of the prevailing market price. When the dealer is *buying* the municipal security from a customer, countervailing evidence of the prevailing market price may be considered only where the dealer made no *contemporaneous sales* in the security or can show that in the particular circumstances the dealer's *contemporaneous proceeds* are not indicative of the prevailing market price.

(iii) A dealer's cost is (or proceeds are) considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the municipal security.

(iv) A dealer that effects a transaction in municipal securities with a customer and identifies the prevailing market price using a measure other than the dealer's own contemporaneous cost (or, in a mark-down, the dealer's own proceeds) must be prepared to provide evidence that is sufficient to overcome the presumption that the dealer's contemporaneous cost (or, the dealer's proceeds) provides the best measure of the prevailing market price. A dealer may be able to show that its contemporaneous cost is (or proceeds are) not indicative of prevailing market price, and thus overcome the presumption, in instances where: (A) interest rates changed after the dealer's contemporaneous transaction to a degree that such change would reasonably cause a change in municipal securities pricing; (B) the credit quality of the municipal security changed significantly after the dealer's contemporaneous transaction; or (C)

news was issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the municipal security after the dealer's contemporaneous transaction.

(v) In instances where the dealer has established that the dealer's cost is (or, in a mark-down, proceeds are) not contemporaneous, or where the dealer has presented evidence that is sufficient to overcome the presumption that the dealer's contemporaneous cost (or proceeds) provides the best measure of the prevailing market price, such as those instances described in (a)(iv)(A), (B) and (C), the dealer must consider, in the order listed and subject to (b)(viii), the following types of pricing information to determine prevailing market price:

(1) Prices of any contemporaneous inter-dealer transactions in the municipal security in question;

(2) In the absence of transactions described in (1), prices of contemporaneous dealer purchases (sales) in the municipal security in question from (to) institutional accounts with which any dealer regularly effects transactions in the same municipal security; or

(3) In the absence of transactions described in (1) and (2), for actively traded municipal securities, contemporaneous bid (offer) quotations for the security in question made through an inter-dealer mechanism, through which transactions generally occur at the displayed quotations.

In reviewing the pricing information available within each category, the relative weight, for purposes of identifying prevailing market price, of such information (*i.e.*, a particular transaction price or quotation) depends on the facts and circumstances of the comparison transaction or quotation (*e.g.*, whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction and timeliness of the information).

Because of the lack of active trading in most municipal securities, it is not always possible to establish the prevailing market price for a municipal security based solely on contemporaneous transaction prices or contemporaneous quotations for the security. Accordingly, dealers may often need to consider other factors, consistent with (b)(vi) and (b)(vii) below.

(vi) In the event that, in particular circumstances, the above factors are not available, other factors that may be taken into consideration (not in any required order or combination) for the purpose of establishing the price from which a customer mark-up (mark-down) may be calculated, include but are not limited to:

- Prices, or yields calculated from prices, of contemporaneous inter-dealer transactions in a “similar” municipal security, as defined below;

- Prices, or yields calculated from prices, of contemporaneous dealer purchase (sale) transactions in a “similar” municipal security with institutional accounts with which

any dealer regularly effects transactions in the "similar" municipal security with respect to customer mark-ups (mark-downs); and

- Yields calculated from validated contemporaneous inter-dealer bid (offer) quotations in "similar" municipal securities for customer mark-ups (mark-downs).

The relative weight, for purposes of identifying prevailing market price, of the pricing information obtained from the factors set forth above depends on the facts and circumstances surrounding the comparison transaction (*i.e.*, whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction, timeliness of the information, and, with respect to the final factor listed above, the relative spread of the quotations in the similar municipal security to the quotations in the subject security).

(vii) Finally, if information concerning the prevailing market price of the subject municipal security cannot be obtained by applying any of the above factors, dealers (and the regulatory agencies and organizations responsible for enforcing MSRB rules) may consider as a factor in assessing the prevailing market price of a municipal security the prices or yields derived from economic models (*e.g.*, discounted cash flow models) that take into account measures such as credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value; and consider all applicable pricing terms and conventions (*e.g.*, coupon frequency and accrual methods).

(viii) Because the ultimate evidentiary issue is the prevailing market price, isolated transactions or isolated quotations generally will have little or no weight or relevance in establishing prevailing market price. For example, in considering the pricing information described in (a)(v), a dealer may give due regard to whether such pricing information is being derived from an isolated transaction or quotation. In addition, in considering yields of "similar" municipal securities, except in extraordinary circumstances, dealers may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" municipal securities taken as a whole.

(b) "Similar" Municipal Securities

(i) A "similar" municipal security should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor. At a minimum, the municipal security or securities should be sufficiently similar that a market yield for the subject security can be fairly estimated from the yields of the "similar" security or securities. Where a municipal security has several components, appropriate consideration may also be given to the prices or yields of the various components of the security.

(ii) The degree to which a municipal security is "similar," as that term is used in this Supplementary Material .06, to the subject security may be determined by factors that include but are not limited to the following:

(1) Credit quality considerations, such as whether the municipal security is issued by the same or similar entity, bears the same or similar credit rating, or is supported by a similarly strong guarantee or collateral as the subject security (to the extent securities of other issuers are designated as "similar" securities, significant recent information concerning either the "similar" security's issuer or subject security's issuer that is not yet incorporated in credit ratings should be considered (*e.g.*, changes to ratings outlooks));

(2) The extent to which the spread (*i.e.*, the spread over U.S. Treasury securities of a similar duration) at which the "similar" municipal security trades is comparable to the spread at which the subject security trades;

(3) General structural characteristics and provisions of the issue, such as coupon, maturity, duration, complexity or uniqueness of the structure, callability, the likelihood that the municipal security will be called, tendered or exchanged, and other embedded options, as compared with the characteristics of the subject security;

(4) Technical factors such as the size of the issue, the float and recent turnover of the issue, and legal restrictions on transferability as compared with the subject security; and

(5) The extent to which the federal and/or state tax treatment of the "similar" municipal security is comparable to such tax treatment of the subject security.

(iii) When a municipal security's value and pricing is based substantially on, and is highly dependent on, the particular circumstances of the issuer, including creditworthiness and the ability and willingness of the issuer to meet the specific obligations of the security, in most cases other securities will not be sufficiently similar, and therefore, pricing information with respect to other securities may not be used to establish the prevailing market price.

EXHIBIT 2h

ALPHABETICAL LIST OF COMMENT LETTERS ON MSRB NOTICE 2016-07 (FEBRUARY 18, 2016)

1. Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated March 31, 2016

2. Breena LLC: E-mail from G. Lettieri dated February 23, 2016; and e-mail from G. Lettieri dated March 10, 2016

3. Brian Shaw: Letter dated March 28, 2016

4. Herbert Murez: E-mail dated March 28, 2016

5. Markit: Letter from Marcus Schuler, Head of Regulatory Affairs, dated March 31, 2016

6. Office of the Investor Advocate, U.S. Securities and Exchange Commission: Letter from Rick A. Fleming, Investor Advocate, dated March 31, 2016

7. Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, Municipal Securities Division, and Sean Davy, Managing Director, Capital Markets Division, dated March 31, 2016

8. State of Florida, Division of Bond Finance: Letter from J. Ben Watkins III, Director, dated March 31, 2016

9. Thomson Reuters: Letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, dated March 31, 2016

BDA Bond Dealers of America

1909 K Street NW • Suite 510
Washington, DC 20006
202.204.7900
www.bdamerica.org

March 31, 2016

Submitted Electronically

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

RE: **MSRB Regulatory Notice 2016-07: Request for Comment on Proposed Amendments to MSRB Rule G-30 (Prices and Commissions)**

Dear Mr. Smith:

On behalf of the Bond Dealers of America ("BDA"), I am pleased to submit this letter in response to Municipal Securities Rulemaking Board Regulatory Notice 2016-07 (the "Notice"), requesting comment on proposed amendments to provide guidance on establishing the prevailing market price related to the calculation of markups and markdowns for principal transactions in municipal securities. BDA is the only Washington D.C. based group representing middle-market securities dealers and banks focused on the U.S. fixed-income markets and we welcome this opportunity to present our comments on the Notice.

BDA appreciates the fact that MSRB has provided this guidance in response to industry comments to Regulatory Notice 2015-16 (Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers). As BDA stated in its comment letter on that proposal, the retail confirmation rule will not function without clear guidance for establishing inter-dealer cost. The notion of putting a subjective estimate of inter-dealer cost on a customer confirm is a very serious concern for dealers. BDA does not believe the guidance, as drafted, provides a guide for dealers to reliably and continuously ascertain inter-dealer cost with enough certainty to incorporate that information on a customer confirmation. Therefore, BDA urges MSRB to re-propose this guidance after assessing industry comment letters because BDA believes this proposed guidance, as currently written, would cause a significant market disruption related to the retail confirmation rule. To minimize market disruption and confusion, it is absolutely essential that workable contemporaneous cost guidance be established before any retail confirmation rule is finalized.

The BDA does not believe FINRA 2121 is the proper basis for an MSRB rule that will apply to the municipal securities marketplace.

The municipal securities marketplace is vastly different than the marketplace for corporate and Agency securities. Therefore, certain rules and guidance, such as FINRA Rule 2121, which provides guidance for establishing contemporaneous cost in the corporate and Agency marketplace, do not provide the proper basis for a comparable MSRB rule for the municipal securities marketplace. BDA appreciates FINRA and the MSRB's efforts to

harmonize rules generally. However, harmonizing this proposed guidance with FINRA Rule 2121 will not work in practice and may, in fact, create more confusion for dealers and investors. This is because the hierarchical step-by-step "waterfall" scenario, which may work for corporate and Agency securities, is not the most practical approach for establishing contemporaneous cost in the municipal securities marketplace. Furthermore, requiring dealers to draft policies and procedures based on a corporate-bond market model will be extremely burdensome from a compliance standpoint because the proposed guidance is not based on the trading and market dynamics that exist in the municipal securities marketplace.

In the non-municipal marketplace, securities trade with greater frequency. This reality allows for a more standardized uniform procedure as envisioned by the waterfall scenario. For example, identifying contemporaneous cost for a frequently traded corporate bond that is actively trading in the secondary market is a relatively easy task. By contrast, the municipal market contains a significantly greater number of unique bond issues that trade far less frequently. Therefore, it is likely that the proposed guidance, which is based on a corporate-bond model, would be more valuable pricing guidance if it were amended to reflect how municipal bonds trade.

BDA recommends allowing dealers to use one or more of the concepts outlined in the waterfall to identify contemporaneous cost as opposed to requiring rote step-by-step, robotic policies and procedures based on the corporate market waterfall. This would allow for greater flexibility in a market where bonds trade less frequently. For example, if a particular municipal security has not traded in several days and a dealer is offering bonds for sale out of inventory at a price which is based on a spread to a municipal market index, the dealer should not be required to document that it has gone through the unnecessary and cumbersome step-by-step process for establishing that no contemporaneous trades have occurred in the same security when no trades have been reported to EMMA.

This is especially true because, for retail trades, G-18 already requires order-handling procedures to ensure 'best execution'. Our recommendation to permit a spread-based pricing approach, or another reasonable pricing approach, would not relieve the dealer from having a full understanding of the marketplace, including the markets where municipal securities are trading. However, it would allow a dealer to form a reasonable basis for estimating its contemporaneous cost at a given point in time without having to go through the process of documenting each step in the waterfall, many of which are not always applicable for the municipal market.

BDA believes that the contemporaneous cost guidance would cause major confusion amongst dealers as it relates to compliance with the proposed retail confirmation disclosure rules.

As BDA stated in its December 11, 2015 response to Regulatory Notice 2015-16 (Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers), the biggest uncertainty created by the MSRB's methodology is the ability to reliably and consistently ascertain inter-dealer cost to compute the prevailing market price for purposes of including that information on a retail-customer confirmation. Having clear guidance on establishing the prevailing market price is absolutely essential for the retail confirmation proposal to become operational and the BDA appreciates that

the MSRB has published this proposed guidance. Unfortunately, the guidance proposed in this Notice is based upon a model of pricing that would not be workable for the municipal securities market.

Requiring a complex, process-specific method to determine prevailing market price is not the optimal method given that there is still no general consensus within the industry or amongst regulators on the single best method for pricing a municipal security. Although BDA continues to believe that providing additional pricing disclosure to retail investors could potentially be beneficial to the marketplace, the MSRB must weigh the substantial costs of compliance and technological infrastructure necessary to implement the proposed guidance and related proposed rules. Furthermore, as the implementation of a retail confirmation disclosure rule is finalized by the MSRB, such a rule should not go into effect before reliable prevailing market price guidance is finalized in a format that is appropriately tailored to the municipal securities marketplace.

BDA does not believe that estimating the cost of compliance for the G-30 Guidance is possible at this point

The BDA represents small-to-medium sized middle market securities dealers and banks. These firms have been disproportionately burdened by the significant increase in regulatory costs over the past several years. This rule represents another significant requirement that will add to compliance personnel, technology, and third-party vendor cost burdens. Consolidation of the municipal securities industry, which is already occurring because of the vast increase in regulatory costs, would have a negative impact on competition, retail investors, and the availability of reasonably priced services in regional securities issues to participants in regional markets.

If this proposed guidance is designed to require dealers to maintain evidence for each trade that would be sufficient to overcome the price established by reference to contemporaneous cost, this would add tremendous new compliance and technology costs. To comply with this requirement, dealers would be required to document the specific considerations that led to a prevailing market price judgment, resulting, perhaps in an inefficient marketplace where no trader wants to be the high or low price to the tape, and which may result in an artificial impact to pricing.

BDA urges MSRB to leverage the pricing data held in EMMA to achieve greater transparency for retail investors.

As stated above, we ask that workable contemporaneous cost guidance be established before any retail confirmation rule is finalized. With that said, we also reiterate our recommendation from our previous comment letter on the retail confirmation disclosure rule proposal, that regulators leverage the transaction data that EMMA and TRACE already hold, to provide the type disclosure the retail confirm proposals are designed to create. This result would deliver the desired additional disclosure to retail customers at a much lower cost to broker-dealers while providing greater clarity and consistency for the retail investor. It would also 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.

SMMPs should be exempt from Rule G-30

BDA recommends that Rule G-30 be revised to explicitly exempt SMMPs from the fair pricing requirement. The voluminous body of pricing information that now exists should make it clear that SMMPs no longer have to rely on executing dealers to determine if their transactions are being priced fairly. If, as the MSRB has determined, SMMPs may elect to opt out of the protections provided to market participants by MSRB Rule G-18 relating to best execution, it follows that they should also be exempt from Rule G-30 fair pricing protection because the two are so closely related.

Conclusion

The proposed amendments to MSRB Rule G-30 to establish a process to identify a prevailing market price are not appropriately tailored to the municipal securities market. The proposed guidance is entirely too prescriptive and does not take account of the legitimate different methods that various dealers use to establish prevailing market price. Furthermore, the proposed guidance represents an unknowable compliance and technology burden that will fall disproportionately on middle-market dealers.

Thank you for the opportunity to submit these comments.

Sincerely,

Michael Nicholas
Chief Executive Officer

Comment on Notice 2016-07

from G. Lettieri, Breena Llc

on Tuesday, February 23, 2016

Comment:

A critical component of all Municipal Bonds is the Bond Factor.

Although it may seem obvious, if ignored, it can have disastrous results in all portfolios, Mutual Funds, ETF's etc., if a prevailing price is not at least at or above the Bond Factor.

Also, because Municipals are primarily for long- term holdings, it is not considered a negative or a detriment to the last recorded price, even if that price was recorded many years ago ; in other words, if it has never been bought or sold in many years, but simply held, the prevailing price is the last price or Bond Factor, whichever is greater, at the very least.

Liquidity is a key component to pricing. Brokers and investors need to have the ability to buy or sell the bonds at the above fair prices.

The last component to this scenario, of course , is in the event of a default of the issue which should be a rare occurrence, so that the integrity of the market itself, let alone the pricing, isn't compromised.

In our view, all of the preceding, is not hard to achieve, where all participants needs are met and not harmed by the misalignment of pricing movements.

Comment on Notice 2016-07

from G. Lettieri, Breena Llc

on Thursday, March 10, 2016

Comment:

Municipal pricing is a function of the Duration of the Bond (Maturity) and the Coupon.

Pricing of Municipals is supposed to be simple and stable.

After Issuance, Municipals are not functions of interest rates. Treasuries tend to be functions of interest rates ,not Municipals.

Municipals have a fixed Coupon that doesn't change with Interest Rates and neither does the Duration change. Municipal Bond prices
should be relatively stable.

The current problem for Investors and Dealers is a lack of liquidity in the Municipal Market ,and consequently, this becomes a problem for accurate and stable pricing. There is no proper and stable pricing without liquidity.

Finra rules deal with stocks and unique stock fundamentals; the fundamentals of Municipal Bonds are vastly different from stocks and do not follow the same rules. For that matter, the four major Bond types, Treasuries, Agencies, Municipals and Corporates are each different and unique, so that the same rules for one type do not necessarily apply to the other.

We believe, the challenges of the Municipal Market revolve around Liquidity and Proper Issuance to start. Then pricing with satisfying commissions for Dealers and enticing prices for Investors to buy or sell will follow. In our view, this challenge is not difficult to achieve with no one being fearful ,but all prospering from a stable Municipal market.

Via Electronic Delivery

March 28, 2016

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

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

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:

Determining a Prevailing Market Price (PMP) for any municipal security should not be a complex, formula-based algorithm or a flexible interpretation left up to each dealer to devise on their own. It should be a straightforward calculation reported (or updated) in real time at the time of the last trade. It should be easily observed by a trader or customer based on existing published (reported) trade information. In fact, the PMP at the time of trade should appear in the trade information posted to the Trade Activity on the EMMA website.

Dealer, retail, and institutional trades must all be factored. For this reason I would recommend establishing a "**Net Price**" calculation eliminating any commissions paid. A "Net Price" would be reported to the MSRB on each transaction and form the basis for the PMP calculation. Commissions paid would be subtracted from a Customer Buy trade to arrive at a "Net Price". Commissions paid would be added to a Customer Sell trade to arrive at a "Net Price". Dealer to Dealer trades would not involve commission so the trade price would be the "Net Price". Trades involving two or more Dealers simultaneously and a Broker's Broker would be only reported once, net of commission, to arrive at the "Net Price".

Examples:

Retail client sells $25,000 at $97.50 with $5/bond commission:	Net Price: $98.00
Retail client buys $25,000 at $100 with $20/bond commission:	Net Price: $98.00
Institutional client buys $1,000,000 at $98.33 with $2.00 commission:	Net Price: $98.13

Broker's Broker trades $500,000 between 2 dealers at $98.00 to buyer, $97.95 to the seller (50 cents commission) One $500,000 trade is reported Net Price: $98.00

Broker's Broker trades $2,000,000 between 1 dealer selling at $99.20 (50 cents commission), 3 other dealers buying at $99.25 One $2,000,000 trade is reported Net Price $99.25

Prevailing Market Price should not weigh all trade quantities equally. Smaller trades of $5,000 or $10,000 par value should not carry the same influence on the "Average Net Price" as larger par value trades. Therefore, the PMP calculation will be a current "**Weighted Average Net Price**".

Prevailing Market Price should be calculated over a specific period of time to reflect current market conditions. I would recommend using a calculation period of 72 hours (from the time of the first trade) but continue calculating on a **forward** rolling basis using "Weighted Average Net Price". If no trades have been reported for over 72 hours then there would be no Prevailing Market Price, and the process would start over with the next trade on that particular CUSIP. Trades that occurred more than 72 hours ago would no longer be included in the current "Weighted Average Net Price" (PMP).

However, a trader or customer could view PMP on a historical basis on the EMMA website in the Trade Activity section. PMP at the time of trade would be displayed on the same line as the reported transaction price. It would be helpful to most market participants if Bloomberg also displayed the **current** Prevailing Market Price on the front Security Description page.

In conclusion, I strongly believe the same PMP calculation should be applied industry-wide for the most consistent representation by all dealers, whether it's the one mentioned above or something different. It should not be left up to each firm to devise it as they see fit. I have worked in the municipal market since 1986 and have learned that fairness and consistency are the keys to investor confidence and understanding. Please feel free to contact me with questions or further inquiries.

Brian Shaw

Municipal Bond trader

2204 Merrick Rd

Louisville, KY 40207

Comment on Notice 2016-11

from herbert murez,

on Monday, March 28, 2016

Comment:

I invest in munibonds. Brokers typically act as principals. They make a spread between what he issuer gets and what the investor pays. I think that spread should be disclosed, as should other sales to other investors. At times there is a lag between a trade and public disclosure of the terms of that trade. I submit that stale information is useless. Regulation should require the terms of the trade to be publicly available forthwith, not to exceed three market hours in any case, or by the time the market reopens next morning, whichever is less.

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March 31, 2016

By Electronic Mail

Re: Municipal Securities Rulemaking Board Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price, Feb. 18, 2016

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities
Rulemaking Board
1300 I Street NW, Suite 1000
Washington, DC 20005

Dear Mr. Smith,

Markit appreciates the opportunity to comment on the Municipal Securities Rulemaking Board ("MSRB" or "Board")'s Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price ("RFC").[1]

I. About Markit

Markit[2] is a leading global diversified provider of financial information services. Founded in 2003, we employ over 4,000 people in 11 countries, including over 1,600 in the U.S., and our shares are listed on Nasdaq (ticker: MRKT). Markit's products and services enhance transparency, reduce risk and improve operational efficiency of financial market activities. Our customers include banks, hedge funds, asset managers, central banks, regulators, auditors, fund administrators and insurance companies. By setting common standards and facilitating market participants' compliance with various regulatory requirements, many of our services help level the playing field between small and large firms and foster a competitive marketplace.

Markit has been actively and constructively engaged in the debate about regulatory reform in financial markets, including topics such as the implementation of G20 commitments for OTC derivatives and the design of a regulatory regime for benchmarks. Over the past years, we have submitted more than 140 comment letters to regulatory authorities around the world and have participated in numerous roundtables.

Markit Pricing Data for bonds provides broker-dealers, buyside firms, and other market participants independent pricing, transparency and liquidity data on bonds across the universe of corporate and sovereign securities, municipal bonds as well as European and US securitized products. Markit's bond data uses price inputs from a variety of sources that are either aggregated to calculate composite levels or fed into a dynamic model to produce a price

[1] Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price, Feb. 18, 2016, http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2016-07.ashx.
[2] See www.Markit.com for more details.

validated against a number of parameters. The service also includes full transparency on the depth of price sources used, a liquidity score reflecting the frequency and breadth of pricing and comprehensive analytics.

Markit Pricing Data provides comprehensive insight into the municipal bond market, delivering pricing and liquidity data for more than 1.1 million municipal bonds.[3] Data from our parsing technology and the MSRB's EMMA is fed directly into our pricing engine to support rapid updates to municipal bond prices. The pricing methodology also incorporates the financial condition of each state and municipality, uses of proceeds and other factors at the issue level to drive movements in price, regardless of the credit rating.

II. Executive summary

We recommend generally that the Board focus on ensuring that the "prevailing market price disclosure" reflect prices that exist in the *current market* for a municipal bond rather than a price that is developed as a function of a strict hierarchy of factors. For reasons described in further detail below, we recommend the Board:

- eliminate the step-based hierarchy in favor of an approach whereby all of the factors in the hierarchy could be considered if the firm has a reasonable basis to believe that considering all of the factors for a particular security and similar securities would lead to a more accurate prevailing market price;
- make its hierarchy of factors non-exclusive or amend it to include new factors, e.g., trade size, or provide a means for firms to consider other factors when the firm has a reasonable basis to believe that the additional factor would make the prevailing market price more accurate; and
- should work with the Financial Industry Regulatory Authority (FINRA) to ensure that it too updates its policy for debt securities under its oversight to harmonize with the prevailing market price guidance developed by the Board. This is particularly important for FINRA securities most similar to most municipal bonds, e.g., infrequently traded corporate debt securities.

Finally, we believe that the threat of a disclosure violation would ensure that firms use the most accurate methodology for determining a prevailing market price under the more flexible approach we have recommended.

III. Discussion

1. The Board should eliminate the step-based hierarchy in favor of an approach whereby all of the factors in the hierarchy could be considered if the firm has a reasonable basis to believe that considering all of the factors for a particular security and similar securities would lead to a more accurate prevailing market price

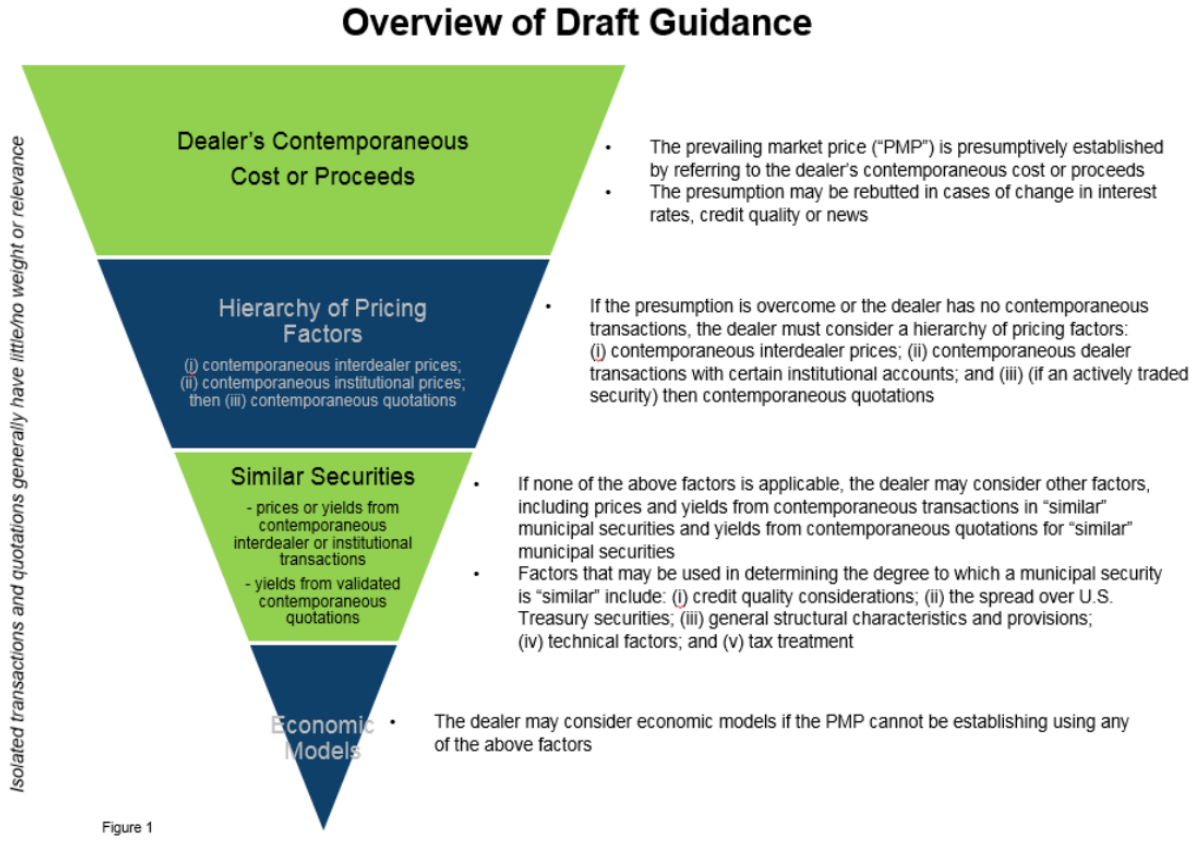
While a prevailing market price standard has been used historically to ensure fair and reasonable pricing to customers, under securities law broker-dealers have never been required to disclose a specific prevailing market price.[4] This new disclosure requirement has led many of

[3] See Municipal, https://www.markit.com/Product/Pricing-Data-Bonds-Municipal.

[4] We note that the disclosure of a specific prevailing market price in customer confirmations exposes firms to disclosure-related legal liability, e.g., Rule 10b-5.

our customers to rethink what a "prevailing market price" means precisely in the context of municipal (and corporate) bonds.

The RFC models its guidance on prevailing market prices based on existing FINRA guidance, finalized in 2007.[5] The below chart from the RFC summarizes the hierarchy of factors:



Importantly, a subsequent factor may be considered only if previous factors in the hierarchy are inapplicable. We call this approach a "step-based" hierarchy whereby a set of factors may only be considered if and only if factors in a previous step in the hierarchy are inapplicable.

We think that this In a 1984 Securities and Exchange Commission administrative proceeding involving *Alstead, Dempsey, and Co*., the SEC described the general principle underlying the concept of "prevailing market price."[6] The SEC explained that "[t]he prevailing market price means the price at which dealers trade with one another, i.e., the current inter-dealer market."[7] The SEC explained further:

> Where there is an active, independent market for a security, and the reliability of quoted offers can be tested by comparing them with actual interdealer transactions during the period in question, such quotations may provide a proper basis for computing markups. Thus, if inter-dealer sales occur with some frequency, and on the days when they occur they are consistently effected at prices at or around the quoted offers, it may properly be

[5] FINRA Rule 2121, including Supplementary Material .01, Mark-Up Policy, and Supplementary Material .02, Additional Mark-Up Policy for Transactions in Debt Securities, Except Municipal Securities Supplementary Material .02 (2007).
[6] *Alstead, Dempsey & Co.,* Exchange Act Release No. 34-20825, 47 S.E.C. 1034 (April 5, 1984).
[7] Id. at 1035.

> inferred that on other days such offers provide an accurate indication of the prevailing market.[8]

We recommend the Board focus on prices that exist in the *current market* for a municipal bond rather than a strict hierarchy of factors. A step-based hierarchy can lead to misleading and inaccurate prevailing market price disclosures. For example, a given municipal bond may not have a "contemporaneous cost" (step one of the hierarchy) or have contemporaneous pricing factors (step two of the hierarchy) but there may be transactions in similar securities, but those transactions by themselves may not result in a prevailing market price disclosure that would be as accurate as one including the results of an economic model.[9]

Accurately determining the current price of a particular municipal security is what drives Markit's (and other data vendors') municipal bond pricing services and to do so, we do not limit our data set to particular factors when other factors are relevant. Certain factors may be weighed more heavily, of course, e.g., data relating to the particular municipal security, but other data lower in the RFC's hierarchy may still relevant to determining price, as is size (see section 2 below).

We therefore recommend the Board either:

> (1) eliminate the step-based hierarchy in favor of an approach whereby all of the factors in the hierarchy could be considered if the firm has a reasonable basis to believe that considering all of the factors for a particular security and similar securities would lead to a more accurate prevailing market price or
>
> (2) provide a safe harbor for firms disclosing a prevailing market price for an infrequently traded municipal if they have a reasonable basis to believe that relying on all of the hierarchy factors for their municipal bond or similar securities would lead to a more accurate prevailing market price. The Commission could condition this allowance based on periodic back-testing to ensure that the prevailing market price methodology (or source) that they use tends to be more accurate than a strict application of the step-based hierarchy.

2. The Board should make its hierarchy of factors non-exclusive or amend it to include new factors, e.g., trade size, or provide a means for firms to consider other factors when the firm has a reasonable basis to believe that the additional factor would make the prevailing market price more accurate

The RFC does not include trade size as a factor to consider in determining the prevailing market price. Large trades, particularly for illiquid securities, are more likely to have greater price variation from the current market price. This is because such trades often include a larger liquidity premium, i.e. the cost or risk a market-maker would bear for offsetting the transaction in one or multiple trades is greater. The markets ability to absorb trades with minimal impact diminish as trade size increases, thus, large trades should therefore be interpreted and weighted in this light. On the other hand, small or odd-lot transactions may be more expensive for a customer because smaller or odd-lot trades incur the same fixed costs of trading as larger trades and therefore have fewer willing dealers to provide liquidity, resulting in higher prices (if the customer is buying) and vice-versa.

[8] Id.

[9] Under the RFC, firms may use economic models to determine a "prevailing market price," taking into account factors such as credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value, and may consider all applicable pricing terms and conventions used.

The prevailing market price for a trade therefore varies based on the size of the trade. Accordingly, we recommend the Board allow firms to adjust the prevailing market price to the size of a trade in order to ensure that the comparison of the executed and prevailing market prices are done on "apples to apples" basis. The best approach the Board should take is to make the hierarchy of factors as non-exclusive when a firm has a reasonable basis to believe additional factors would make the prevailing market price disclosure more accurate. While we think this more flexible approach is more likely to produce more accurate prevailing market price disclosures, an alternative to consider is one whereby trade size becomes a factor included in the hierarchy. We think it should be a part of the first three steps of the hierarchy in this case.

3. **The Board should work with the Financial Industry Regulatory Authority (FINRA) to ensure that it too updates its policy for debt securities under its oversight to harmonize with the prevailing market price guidance developed by the Board. This is particularly important for FINRA securities most similar to most municipal bonds, e.g., infrequently traded corporate debt securities**

We believe that the Board will likely have to differentiate its approach to prevailing market price from that used by FINRA in FINRA Rule 2121. We make this suggestion because, most importantly, (1) FINRA didn't develop its rules to result in a specific prevailing market price disclosure and (2) the idiosyncratic characteristics of the municipal bond markets will likely yield a focus at the Board in 2016 different than the approach taken by FINRA some ten+ years ago. We think that the policy the Board develops for municipal bonds will lead to guidance that will improve FINRA's guidance, particularly for those FINRA securities most similar to municipal bonds, e.g., infrequently-traded securities. Accordingly, we recommend the Board work with FINRA to develop a modernized and harmonized approach to prevailing market prices.

4. **The threat of a disclosure violation would ensure that firms use the most accurate methodology for determining a prevailing market price under the more flexible approach we have recommended**

We understand the Board's use of a step-based and exclusive hierarchy of factors may be based on a desire to reduce the risk of opportunistic, false, or misleading prevailing market price disclosures. This risk is low, we think, because of the risks associated with such a disclosure in the form of legal liability that would attach from a false or misleading prevailing market price disclosure. This risk, we think, would incentivize firms to produce accurate prevailing market price disclosures and the flexible approach we've recommended above would give firms the tools they need to determine more accurate prevailing market price disclosures.

*** *** ***

Markit appreciates the opportunity to provide these comments to the Board. We would be happy to elaborate on or further discuss any of the points addressed above. If you have any questions, please do not hesitate to contact the undersigned or Salman Banaei at salman.banaei@markit.com.

Yours sincerely,

Marcus Schüler
Head of Regulatory Affairs Markit
marcus.schueler@markit.com

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

OFFICE OF THE
INVESTOR ADVOCATE

March 31, 2016

Submitted Electronically

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street NW, Suite 1000
Washington, D.C. 20005

RE: Regulatory Notice 2016-07
Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price

Dear Mr. Smith:

The Office of the Investor Advocate[1] appreciates this opportunity to provide comments in regard to Regulatory Notice 2016-07, Request for Comment on Draft Amendments to Municipal Securities Rulemaking Board ("MSRB" or "Board") Rule G-30 to Provide Guidance on Prevailing Market Price ("MSRB Request for Comment").[2] The MSRB Request for Comment broadly establishes the manner in which the prevailing market price (the "PMP") for municipal securities is calculated.[3]

[1] This letter expresses solely the views of the Investor Advocate. It does not necessarily reflect the views of the Securities and Exchange Commission ("Commission" or "SEC"), the Commissioners, or staff of the Commission, and the Commission disclaims responsibility for this letter and all analyses, findings, and conclusions contained herein.

[2] Pursuant to Section 4(g)(4) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78d(g)(4), the Office of the Investor Advocate at the Securities and Exchange Commission is responsible for, among other things, analyzing the potential impact on investors of proposed rules of self-regulatory organizations. In furtherance of this objective, we routinely review and examine the impact on investors of significant rulemakings of the Municipal Securities Rulemaking Board. As appropriate, we make recommendations and utilize the public comment process to help ensure that the interests of investors are considered while rulemaking decisions are made; MSRB, Regulatory Notice 2016-07, *Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price* (Feb. 18, 2016), http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2016-07.ashx?n=1.

[3] MSRB, Regulatory Notice 2016-07, *Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price* (Feb. 18, 2016), http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2016-07.ashx?n=1.

In prior comment letters, the Office of the Investor Advocate voiced its support for the adoption of rules requiring the disclosure of same-day mark-ups in fixed income retail trades.[4] We acknowledged that either a price reference approach or mark-up approach based on PMP is an improvement over the *status quo*.[5] The Office of the Investor Advocate specifically endorsed a move to disclosure of a mark-up based upon PMP over a price reference approach, noting that the move to mark-up disclosure based upon PMP, among other things, reflects market conditions and has the potential to provide a more accurate benchmark for calculating transaction costs.[6]

Consistent with our earlier comments, the Office of the Investor Advocate continues to believe that investors would be poorly served by inconsistency between MSRB and the Financial Industry Regulatory Authority's ("FINRA") rules and guidance relating to confirmation disclosure.[7] We acknowledge the deliberative approach taken by the MSRB to harmonize the manner in which the PMP is determined for purposes of municipal securities with the FINRA guidance for determining the PMP for other fixed income securities.[8] In the interest of consistency between FINRA and the MSRB, the MSRB's proposal to adopt FINRA's PMP guidance appears reasonable. However, the context in which the PMP guidance would be applied will be expanded, raising significant concerns for fixed income investors as it relates to price disclosure.

FINRA's PMP guidance was originally adopted, and has been historically applied, only in the context of preventing mark-ups that are so excessive as to be deemed unethical. However, if PMP guidance is adopted for confirmation disclosure purposes as well, the same PMP guidance would be applied in a much different context – namely, as a disclosure of compensation paid to dealers by retail customers. Under this new context, precision and accuracy in the calculation of PMP becomes more important. Given the increased importance of calculating PMP, the Office of the Investor Advocate stresses the need for the MSRB to take a fresh look at the guidance. The MSRB should carefully scrutinize the guidance and its application to potential confirmation disclosure rules to prevent manipulation of the PMP calculation for confirmation disclosure purposes. We believe that misleading disclosure would be worse than no disclosure at all.

In particular, the Office of the Investor Advocate has a significant concern with how the PMP may be determined under the current guidance in circumstances involving non-arm's length affiliate transactions. We believe the guidance should seek to ensure that the PMP reflects the true market price and, in our view, there are several possible ways to accomplish this goal. The Office of the Investor Advocate urges the MSRB to consider addressing our concern before

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[4] *See* Comment Letter, Rick. A. Fleming, Investor Advocate, SEC, *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* (Dec. 11, 2015), http://www.finra.org/sites/default/files/15-36_SEC_comment.pdf.

[5] *Id.*

[6] *Id.*

[7] Consistent MSRB and FINRA proposals and guidance would work in tandem to provide retail investors with better price transparency in corporate and municipal bond transactions. *Supra* note 4 at 2.

[8] *Id.* Modifications to the FINRA Guidance intended to tailor the determination of PMP to the municipal securities market are included in the proposed language of the MSRB's Request for Comment. *Id.*

filing a proposed rule change with the Commission. A more detailed discussion, along with several potential solutions, is set out below.

MSRB's Proposed Guidance on Prevailing Market Price

The MSRB Request for Comment proposes guidance for municipal securities dealers to determine the PMP of a municipal security. Specifically, the proposed guidance establishes a rebuttable presumption whereby the PMP is presumed to be the municipal securities dealer's contemporaneous cost (or proceeds).[9] This presumption is rebuttable in cases of change in interest rates, credit quality, or news.[10] To the extent the presumption is rebutted, or a dealer has no contemporaneous transaction, a hierarchy of pricing factors will be considered, in successive order.[11] These factors are: (i) contemporaneous interdealer prices; (ii) contemporaneous dealer transactions with certain institutional accounts; and (iii) if an actively traded security, contemporaneous quotations.[12] In the event the presumption is overcome, or inapplicable, and none of the hierarchy of pricing factors is applicable, the dealer is permitted to consider other factors including prices and yields from contemporaneous transactions in "similar" municipal securities.[13] Finally, if the dealer is unable to determine the PMP using any of the above factors, the municipal security dealer may consider economic models.[14]

The MSRB Request for Comment largely follows the existing FINRA guidance for calculating the PMP of other fixed income securities. The Request for Comment suggests that the proposed guidance on the PMP and calculating mark-ups and mark-downs for principal transactions in municipal securities "may promote consistent compliance by brokers, dealers and municipal securities dealers with their existing fair-pricing obligations under MSRB rules, in a manner that would be generally harmonized with the approach taken in other fixed income markets."[15] Further, the MSRB sought to balance the essential harmony between the municipal securities market and all other fixed income markets for purposes of determining PMP with the need to account for the unique characteristics of the municipal securities markets.[16]

The MSRB Request for Comment broadly asks whether the "generally harmonized approach and, particularly, whether the modifications are appropriate and whether additional modifications should be made" to account for the unique characteristics of the municipal securities market.[17] The MSRB Request for Comment also generally seeks comment on the

[9] *Id.* at 5-6, 17-18.
[10] *Id.* at 10, 17-18.
[11] *Id.* at 10, 18.
[12] *Id.*
[13] *Id.* at 10, 18-19. Factors used in determining the degree to which a municipal security is "similar" include: (i) credit quality considerations; (ii) the spread over U.S. Treasury securities; (iii) general structural characteristics and provisions; (iv) technical factors; and (v) tax treatment. *Id.* at 10, 20.
[14] *Id.* at 10, 19.
[15] *Id.* at 1 .
[16] *Id.* at 5. Some unique characteristics of the municipal securities market include "the large number of issuers and outstanding securities, the infrequency of trading in the secondary market, the differing tax rules and treatment, and the different credit structures, enhancements and redemption features that may not be applicable to or prevalent for other fixed income securities." *Id.*
[17] *Id.*

subjects of PMP and mark-up calculation, any competitive or anticompetitive effects, and efficiency and capital formation effects of the proposed guidance on market participants.[18]

The Office of the Investor Advocate's Concerns Relating to Affiliate Transactions

The Office of the Investor Advocate supports efforts to augment price transparency and provide retail customers with useful, consistent, clear pricing information. The MSRB's guidance, when combined with mark-up disclosure, would be an important step forward in this regard. Unfortunately, the MSRB's proposed guidance may lend itself to loopholes and slippage when applied to transactions between affiliates, thereby resulting in misleading and inconsistent pricing disclosures to retail customers. More specifically, the Office of the Investor Advocate is concerned that there may be a loophole in non-arm's length affiliate transactions in the municipal securities market, which the Office believes needs to be resolved in the interest of fairness and consistency.

It is unclear whether the proposed guidance takes into account that, in a *non-arm's length transaction between affiliates*, the contemporaneous price resulting from the transaction is more likely to reflect a markup instead of the PMP. To illustrate this ambiguity, first, assume that Dealer A1, a market-facing dealer, and Dealer A2, a retail customer-facing dealer, are affiliates both owned by Company A. On the same trading day, the following three transactions occur:

- First, Dealer A1 purchases Bond Y from an unaffiliated third-party for $90 ("Transaction 1");
    - Dealer A1 displays Bond Y for sale for $93 on Dealer A2's customer-facing platform;
    - During the day, no other dealers display any price for Bond Y.
    - Retail Customer sees Bond Y listed for $93 and places an order with Dealer A2 to purchase Bond Y at the displayed price;
- Second, Dealer A2 purchases Bond Y from Dealer A1 at $93 ("Transaction 2"); and
- Third, Dealer A2 sells Bond Y to Retail Customer for $93 + $1 trading fee.

In this scenario, under the MSRB's proposed guidance, it is possible that Dealer A2 may determine that the PMP would be $93 – the contemporaneous cost to Dealer A2 as evidenced by Transaction 2 between affiliates. Based on that determination, any mark-up disclosure provided to the retail customer would indicate that the customer had only paid $1 on the municipal securities transaction above the PMP. Instead, the Office of the Investor Advocate strongly believes that, in this scenario, Transaction 1 should determine the PMP. Dealer A2 should be required to look through Transaction 2, a non-arm's length transaction with Dealer A1, and use Transaction 1 in determining the PMP. Under such an approach, the PMP for the bond would be $90 and the affiliate transaction would not mask the overall cost paid by customer to the two affiliates of Company A.

[18] *Id.* at 14-15.

If transactions with affiliates are allowed to set the PMP, this practice could easily become the industry norm. This is particularly true if—as we hope—mark-up disclosure is later expanded to include *all* transactions with retail customers, not just same-day transactions. Should this legal structure become a reality for most brokerage firms, mark-up disclosure to retail customers may become meaningless and misleading. Essentially, rulemaking to increase post-trade price transparency through mark-up disclosure will have been for naught because every trade could show an identical mark-up of $1.

Importantly, we note that although the above example assumes a series of transactions that all occur on the same trading day, the Office of the Investor Advocate believes that requiring dealers to look through non-arm's length affiliate transactions should immediately extend beyond the one-day window, where appropriate. Specifically, the Office of the Investor Advocate believes that dealers should, absent strong supporting evidence, always be required to look through non-arm's length affiliate transactions for purposes of determining whether a mark-up is excessive, regardless of whether the affiliate transaction occurred on the same trading day.

In order to ensure a true and consistent pricing disclosure by all municipal securities dealers to all customers, the Office of the Investor Advocate encourages the MSRB to make clear that no such loophole exists for non-arm's length affiliate transactions. To do so, the Office of the Investor Advocate proposes three alternative solutions or a combination thereof. First, textual changes could be made to PMP guidance; second, adjustments could be made to a harmonized mark-up rule to be filed with the Commission; or third, clarification could be provided in the text of a Notice to the Commission. Each potential solution is discussed below.

Proposed Solutions

Textual Changes Clarifying PMP Guidance

The Office of the Investor Advocate believes that one possible solution[19] to prevent a loophole for non-arm's length affiliate transactions would be to make textual changes to the MSRB's proposed PMP guidance by clarifying the definition of "contemporaneous cost (proceeds)." The MSRB's proposed guidance currently states that "[a] dealer's cost is (or proceeds are) considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the municipal security."[20] Under this current definition, it is possible that the customer-facing municipal securities dealer in the earlier illustration might improperly view Transaction 2 as its contemporaneous cost, and ultimately determine the PMP using that transaction.

To ensure that the proper transaction is used to calculate the dealer's costs, the current definition of contemporaneous cost (proceeds) could be enhanced to make clear that the concept applies to truly arm's-length transactions. Absent additional market information, the definition would require a dealer to look through affiliated transactions to determine its contemporaneous cost (proceeds) and ultimately the PMP. In essence, the definition of contemporaneous cost

[19] It is possible that other textual changes could achieve the same result, and we could support alternative proposals.
[20] *Id.* at 17.

(proceeds) cannot allow a dealer to ignore the cost incurred in a third-party, arms-length transaction in favor of the cost incurred in a subsequent affiliated transaction.

The Office of the Investor Advocate strongly supports efforts to create a uniform determination of PMP in all fixed income markets. Thus, it is important to note that any textual changes to the MSRB's proposed guidance may also require amendments to FINRA's relevant supplementary material, to the extent FINRA did not already believe its guidance prevented such exploitation.[21]

Adjustments to a Harmonized Mark-up Rule

In September 2015, the MSRB published 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 Regulatory Notice 2015-16").[22] In October 2015, FINRA sought comment on FINRA Regulatory Notice 15-36, Pricing Disclosure in the Fixed Income Markets ("FINRA Regulatory Notice 15-36").[23] In response to the MSRB's and FINRA's requests for comment, commenters, among other things, stressed the need for a coordinated and consistent approach to confirmation disclosure and some commenters expressed a need for additional guidance on PMP.[24]

Consistent with our comment in response to MSRB Regulatory Notice 2015-16 and FINRA Regulatory Notice 15-26, the Office of the Investor Advocate continues to maintain that investors would be poorly served by pricing disclosures that are different for corporate bonds as compared to municipal bonds.[25] The Office of the Investor Advocate believes that to avoid investor confusion, it is important for FINRA and the MSRB to adopt rules and guidance related to pricing disclosure that are consistent. We also continue to maintain that combining the MSRB's mark-up disclosure methodology with FINRA's same day window would best serve the interest of investors.[26] Such an approach would provide the MSRB and FINRA an opportunity to jointly address the loophole in non-arm's length affiliate transactions directly in their harmonized mark-up rules before filing their final rule proposal notices with the Commission.

MSRB Regulatory Notice 2015-16 proposes to define the term "inventory-affiliate model" to mean "a business model in which the dealer, *on an exclusive basis*, acquires municipal

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[21] In order to achieve a harmonized approach to determining PMP with the MSRB, FINRA would need to amend Supplementary Material .01 Mark-Up Policy and/or Supplementary Material .02 Additional Mark-Up Policy For Transactions in Debt Securities, Except Municipal Securities.

[22] MSRB, Regulatory Notice 2015-16, *Request for Comment on Draft rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transaction with Retail Customers* (Sept. 24, 2015), http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2015-16.ashx?n=1.

[23] FINRA, Regulatory Notice 15-36, *Pricing Disclosure in the Fixed Income Markets* (Oct. 2015), http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-15-36.pdf.

[24] *Supra* note 2 at 3; *See* FINRA, Comment Letters, Regulatory Notice 15-36, *Pricing Disclosure in the Fixed Income Markets*, http://www.finra.org/industry/notices/15-36; MSRB, Comment Letters, Regulatory Notice 2015-16, *Request for Comment on Draft rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transaction with Retail Customers*, http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2015/2015-16.aspx?c=1.

[25] *Supra* note 4.

[26] *Id.*

securities from or sells municipal securities to an affiliate dealer that holds inventory in municipal securities and transacts with other market participants." Municipal securities dealers that use this inventory-affiliate model would be required to look through the transaction with the affiliate dealer and substitute the affiliate's trade with the outside party to determine whether mark-up disclosure would be required. According to MSRB Regulatory Notice 2015-16, this ensures "that the disclosed mark-up is a more accurate indication of the compensation paid by the customer when affiliated dealers effectively function as a single entity for purposes of executing the retail customer's transaction."[27] We agree. However, such rationale should be applied regardless of whether a dealer transacts with an affiliate on an exclusive or non-exclusive basis.

To be clear, the Office of the Investor Advocate supports the inclusion of "inventory-affiliate model" language in the final harmonized proposal and believes that certain textual changes to the definition of this term could adequately address its concerns relating to non-arm's length affiliate transactions. However, we believe that the term "inventory-affiliate model" should not be limited to business models in which dealers, on an exclusive basis, acquire or sell municipal securities to an affiliate. Instead, the Office of the Investor Advocate strongly encourages the MSRB and FINRA to expand the meaning of the term inventory-affiliate model to include business models in which the dealer, on an exclusive or non-exclusive basis, acquires or sells securities to an affiliate dealer that holds inventory and transacts with other market participants.

The impact and importance of applying an expanded definition is evident when put into context using our earlier illustration. Dealer A1 and Dealer A2 do not transact on an exclusive basis. Accordingly, under the narrow definition set out in MSRB Regulatory Notice 2015-16, Dealer A2 would not be required to look through its transaction with Dealer A1 to Dealer A1's transaction with a third party to determine whether mark-up disclosure would be required. On the other hand, if a broader definition of inventory-affiliate model were implemented, Dealer A2 would be required to look through its transaction with Dealer A1 and substitute Dealer A1's transaction with a third party. An expanded definition of the term inventory-affiliate model to include municipal securities dealers transacting on any basis with an affiliate dealer effectively closes the loophole for non-arm's length affiliate transactions by requiring all affiliate dealers to comply with a look-through requirement.

Adjusting the harmonized mark-up rule would, similar to making the suggested textual changes to the proposed PMP guidance, reduce the potential for market gaming. Beneficially, choosing to make necessary adjustments to a harmonized mark-up rule could eliminate the need for FINRA to take separate regulatory action, as would be required to harmonize PMP guidance if the MSRB made the suggested textual changes to its proposed guidance.

The Office of the Investor Advocate believes that making necessary adjustments to a harmonized mark-up rule provides a direct and efficient path forward for purposes of determining the PMP without creating unnecessary regulatory burdens or substantially slowing the progress towards adoption of harmonized fixed income confirmation disclosure regulation.

[27] *Supra* note 22 at 10-11.

However, while it would address the shortcomings of the PMP guidance for purposes of mark-up disclosure, it would not solve the previously described loophole for purposes of excessive mark-ups. We are concerned that the existing PMP guidance could still allow a dealer to use affiliated transactions to establish a higher PMP and avoid liability for excessive markups. We would encourage you to further consider that issue.

Clarification in Notice

In the final alternative, the loophole in non-arm's length affiliate transactions could be addressed by including a description in the Notice for MSRB's proposed guidance regarding how the MSRB would expect a dealer to calculate its contemporaneous costs under such circumstances. The MSRB could provide an example demonstrating that, under the proposed definition, dealers will likely need to look through non-arm's length transactions with affiliates and instead determine the contemporaneous cost (and likely the PMP) using the third-party transaction. Should the MSRB's proposed rule change be approved by the Commission, the Commission would publish an order granting approval of the MSRB's proposed rule change and we would expect that the Commission would make note of the clarification provided by the MSRB and rely on that example in finding the proposal to be consistent with the Exchange Act.

While this could achieve a similar result to the two previous proposed solutions, the Office of the Investor Advocate believes this is the least desirable approach. An example alone may not carry the same legal authority as the textual rule, and a clarification contained only in the Notice is not the best resource for interpreting and understanding ambiguous rule text.

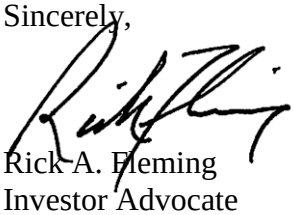
Conclusion

The Office of the Investor Advocate recognizes the MSRB's action in response to commenters' strong desires for a coordinated and consistent approach to confirmation disclosure in fixed income securities markets and their responsiveness to commenters' call for additional guidance on prevailing market price to support a possible mark-up disclosure. The Office of the Investor Advocate applauds the MSRB's efforts to enhance bond market price transparency and to provide investors and other market participants with useful, clear, and consistent guidance.

While the Office of the Investor Advocate regards the MSRB's proposed guidance on the determination of PMP as generally useful, clear, and consistent with FINRA's, we believe that a potential loophole exists for non-arm's length affiliate transactions, which may cause misleading and inconsistent pricing disclosures to investors. The Office of the Investor Advocate advises the MSRB to close the loophole in the interest of fairness and consistency in the fixed income securities markets. Although any of the proposed solutions would be helpful, the Office of the Investor Advocate believes that a combination of guidance and rule text would be the most effective solution.

Thank you, again, for the opportunity to submit our comments regarding this important guidance. Should you have any questions, please do not hesitate to contact me or Senior Counsel Ashlee E. Connett at (202) 551-3302.

Sincerely,



Rick A. Fleming
Investor Advocate

cc (electronically): Lynnette Kelly, MSRB, Executive Director
Michael L. Post, MSRB, General Counsel – Regulatory Affairs
Margaret Blake, MSRB, Associate General Counsel
Saliha Olgun, MSRB, Assistant General Counsel
Robert Colby, FINRA, Executive Vice President and Chief Legal Officer
Patrick Geraghty, FINRA, Vice President, Market Regulation

sifma

Invested in America

March 31, 2016

BY ELECTRONIC MAIL

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street NW, Suite 1000
Washington, DC 20005

Re: MSRB Regulatory Notice 2016-07,
Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price

Dear Mr. Smith:

The Securities Industry and Financial Markets Association[1] ("SIFMA") appreciates this opportunity to comment on the Municipal Securities Rulemaking Board's ("MSRB's") Regulatory Notice 2016-07 (the "Proposal"), in which the MSRB requests comment on draft interpretive guidance on prevailing market price, amending MSRB Rule G-30. SIFMA submits this letter as a supplement to its submission of June 7, 2010 regarding MSRB Notice 2010-10, in which the MSRB proposed similar interpretive guidance, and we incorporate by reference our prior comment in this proceeding.[2]

[1] SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over $2.5 trillion for businesses and municipalities in the U.S., serving clients with over $20 trillion in assets and managing more than $67 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.

[2] Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA, to Ernesto Lanza, General Counsel, MSRB, regarding MSRB Notice 2010-10 (June 7, 2010), *available at* http://www.msrb.org/~/media/Files/RFC/2010/2010-10/SIFMACommentLetter.ashx?la=en.

SIFMA understands that the MSRB's draft guidance is designed to harmonize the manner in which the "prevailing market price" for municipal securities is determined with the manner established by FINRA for purposes of other types of fixed income securities, thereby supporting the development of a possible future mark-up disclosure requirement.[3] We strongly support the MSRB's objective to enhance bond market price transparency for retail investors. To this end, we have urged both the MSRB and FINRA to adopt a uniform approach to confirmation disclosure and have asked for additional guidance from both the MSRB and FINRA on how to ascertain prevailing market price with the necessary specificity to support a mark-up disclosure proposal. We greatly appreciate the engagement with our members by both the MSRB and FINRA regarding this issue, and thank the MSRB for its efforts to consider some of the specific concerns that we have raised in its Proposal.

Although a prevailing market price standard has been used historically to ensure fair and reasonable pricing to customers, firms have never been required to delineate an exact prevailing market price on a customer confirmation. In this regard, the MSRB should recognize in the text of any rule or guidance that, although the core waterfall methodology can serve as a reasonable starting point of factors to consider, it cannot be applied in a mechanical fashion and is not necessarily determinative of an exact prevailing market price calculation.

Within the goal of achieving relative consistency in approach, regulators must acknowledge that the determination of prevailing market price is not an exact science. Accordingly, SIFMA believes that it should be reasonable and understood that firms may calculate different prevailing market prices with the same set of facts, and any anticipated disclosure regime should account for this acceptable variance. In particular, regulators should permit firms to rely on reasonably designed policies and procedures to determine, in a routine and potentially automated fashion, an estimated prevailing market price for the purpose of confirmation disclosure. This calculation and the factors behind the disclosure should indeed be reasonably determined and in good faith, however, the prevailing market price used for any confirmation disclosure requirement should be largely delinked from the regulatory evaluation of the end price to the customer and the requisite fair pricing and mark-up policy requirements. The practicalities of generating the disclosure may necessitate policies and procedures outside, in whole or in part, the direct control of the trader or broker making the determination of the end price to the customer and as such the two requirements (*i.e.*, disclosure and fair pricing) should remain distinct.

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[3] We focus this letter on the MSRB's draft interpretive guidance on prevailing market price, with the understanding that such guidance may be used to support a possible future mark-up disclosure requirement. For the reasons we have emphasized in prior comment letters, we continue to believe such a requirement would impose unjustified costs and burdens and that investors would be better served by alternatives that focus on increasing usage of the abundance of market data and investor tools already available on EMMA and TRACE.

Should some version of a prevailing market price disclosure framework proceed, we urge the MSRB and FINRA to coordinate and provide consistent guidance to address this issue. As this effort proceeds, we would welcome the opportunity to engage further with both the MSRB and FINRA regarding how to achieve our shared objective to provide retail investors with greater insight into their transactions.

With this overarching concern in mind, SIFMA generally supports the MSRB's efforts to harmonize its guidance on prevailing market price with that of FINRA, subject to our comments below. Given the broader context of this effort as well as the unique characteristics of the municipal bond market, we request that the MSRB clarify or alter several aspects of its proposed guidance to ensure greater consistency in approach across firms, and strongly urge both the MSRB and FINRA to coordinate a consistent standard for confirmation disclosure.

DISCUSSION

I. THE MSRB AND FINRA SHOULD ACKNOWLEDGE THAT THERE IS INHERENT VARIABILITY IN THE DETERMINATION OF A PREVAILING MARKET PRICE AND PERMIT FIRMS TO RELY ON REASONABLY DESIGNED POLICIES AND PROCEDURES FOR THE PURPOSE OF CONFIRMATION DISCLOSURE.

One of the primary regulatory objectives associated with requiring enhanced price disclosure on retail customer confirmations is to allow investors to understand and compare their transaction costs across dealers.[4] In light of this objective, regulators should provide specific guidance to ensure increased consistency in approach across the industry such that any potential prevailing market price disclosure is relatively comparable across firms, with enough flexibility to incorporate the understanding that prevailing market price is ultimately a subjective determination with some level of inherent variability. Furthermore, regulators should clarify that estimating a prevailing market price in a short timeframe for the purpose of confirmation disclosure is not necessarily determinative of the prevailing market price for the purpose of scrutinizing a fair and reasonable mark-up.

In its Proposal, the MSRB emphasizes that firms "currently have in place policies, procedures and systems necessary to exercise diligence in determining the

[4] *See* MSRB Regulatory Notice 2015-16 at 15 (suggesting 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"); *see also* FINRA Regulatory Notice 15-36 at 6 (stating that "investors in fixed income securities currently are limited in their ability to understand and compare transaction costs associated with their purchases and sales").

prevailing market price of a security and assure that their mark-ups charged are reasonable when effecting a transaction," however, the MSRB does not acknowledge that this standard has never required firms to print an exact prevailing market price on a customer confirmation.[5] As the Securities and Exchange Commission ("SEC") has noted, "determining the prevailing market price for municipal securities, particularly those that are illiquid, can be a complex task."[6] In particular, the "specific degree of accuracy, as well as the specific actions that a dealer may need to take to assess market value, will vary with the facts and circumstances."[7] This complexity is heightened, in particular, for firms that carry inventory.

Accordingly, regulators should acknowledge that two firms looking at the same set of facts may reasonably come to two different determinations of the prevailing market price for a particular security given the variety of factors that may inform such a determination. Given the significance of Rule 10b-10 confirmation disclosure, firms need explicit assurance that a reasonable and good faith calculation of a prevailing market price for the purpose of confirmation disclosure, based on the information available at the time of a transaction and guided by reasonable policies and procedures, will not be deemed incorrect by regulators in hindsight in the absence of clear error.

As a practical matter, should a prevailing market price disclosure proposal proceed, some level of automation in measuring prevailing market price and generating a corresponding confirmation in a timely manner will be necessary, particularly for firms that engage in a high volume of trades. As an alternative to contemporaneous cost or proceeds, firms should be permitted to adopt policies and procedures that are reasonably designed to generate an estimated prevailing market price for the purpose of confirmation disclosure. For example, regulators should provide guidance that would permit firms to rely on the use of third-party pricing vendors to calculate prevailing market price for the purpose of confirmation disclosures, if firms reasonably determine that such vendors' calculations are sufficiently accurate for this purpose. Nevertheless, there will be an inherent subjectivity involved in reaching an exact prevailing market price determination.

In this regard, both the MSRB and FINRA should provide clear guidance to permit, for the purpose of confirmation disclosure, firms to reach a determination of prevailing market price based on information available at the time of the transaction that is guided by policies and procedures reasonably designed to inform such a calculation. To avoid the risk of misleading investors, firms should be permitted to describe any prevailing market price on a customer confirmation as an "estimated" measure or to otherwise provide a brief disclaimer explaining that prevailing market

[5] MSRB Regulatory Notice 2016-07 at 12.

[6] U.S. Securities and Exchange Commission, Report on the Municipal Securities Market, 148 (July 31, 2012) [hereinafter SEC Municipal Report].

[7] SEC Municipal Report at 129.

price is a subjective measure with some inherent level of variability across firms. In addition, to minimize investor confusion, firms should be permitted to state on customer confirmations that the difference between the price to the customer and the prevailing market price does not necessarily reflect the firm's exact commission, profit, or mark-up on the transaction.

In sum, firms should be permitted to adopt and rely on policies, procedures, and systems reasonably designed to reach a prevailing market price determination. If a firm applies reasonably designed policies, procedures, and systems in good faith in order to generate a prevailing market price, there should be a rebuttable presumption that the dealer has complied with its confirmation disclosure requirement. Nevertheless, an estimated prevailing market price generated for the purpose of confirmation disclosure should not be considered determinative for the purpose of scrutinizing fair and reasonable mark-ups. Regulators should acknowledge that the operational reality of automating a prevailing market price disclosure on a customer confirmation may in some cases overwhelm the theoretical considerations involved in evaluating a fair and reasonable mark-up, where some level of flexibility in interpretation may be required in hindsight. Although there are factors unique to the municipal and corporate bond markets, firms will face similar subjective determinations, as well as system and operational challenges, in the context of any confirmation disclosure requirement. Accordingly, SIFMA strongly urges the MSRB and FINRA, to the greatest extent possible, to adopt harmonized guidance in this regard.

To assist firms with the creation of such policies and procedures and to encourage greater consistency in approach across firms in determining prevailing market price, the MSRB should clarify or revise several aspects of its Proposal as described below. We further suggest that FINRA issue guidance to clarify many of the same interpretative issues that arise from FINRA Rule 2121.

II. TO ENSURE GREATER CONSISTENCY IN APPROACH ACROSS FIRMS, THE MSRB SHOULD CLARIFY OR REVISE SEVERAL ASPECTS OF ITS PROPOSED GUIDANCE.

A. The Definition Of "Contemporaneous" Cost Or Proceeds Should Be Clarified

As a preliminary matter, the MSRB should confirm that, absent other market prices, contemporaneous cost is the first and most representative piece of evidence to prevailing market price, however, contemporaneous cost is not and should not necessarily be considered equal to prevailing market price. Under the draft guidance, "the prevailing market price for a municipal security is established by referring to the

dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained."[8] The MSRB should clarify that prevailing market price is not "established" by referring to the dealer's contemporaneous cost or proceeds; rather, contemporaneous cost is the *most representative* evidence of prevailing market price.

Rather than imposing a rigid standard, the MSRB should allow firms to adopt and rely on a more flexible approach in determining prevailing market price, guided by reasonable policies and procedures that recognize that pricing is based on a myriad of factors. In this context, the MSRB should recognize in the text of any rule or guidance that the waterfall serves as a descriptive list of factors to consider, and is not in all cases controlling or determinative in calculating an exact prevailing market price.

In addition, the MSRB should clarify the meaning of the term "contemporaneous." The Proposal states that a dealer's cost is (or proceeds are) "considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the municipal security."[9] In other words, a "contemporaneous" transaction is one that occurs "close enough in time" to the subject transaction. This definition is circular and is difficult for dealers to apply in practice with any degree of consistency. Moreover, this definition implies that the passage of time is the only factor in determining whether or not a prior trade is considered contemporaneous with a subject trade. The MSRB needs to clarify that timing is a factor and the amount of time it believes is sufficiently long so that a trade would not be deemed contemporaneous. At a minimum, the MSRB should confirm that trades that do not occur on the same day will not be considered contemporaneous.

The MSRB should clarify that the "most recent" transaction is not necessarily the most representative evidence of the "prevailing market," even if that transaction is deemed by the MSRB or as applied by FINRA as "contemporaneous" for purposes of the traditional waterfall analysis. For example, if the most recent transaction is 20 days ago, changes to the facilities or operations that support the security, or changes in a municipal issuer's financial condition, may make the old, but "most recent," transaction inappropriate for determining the prevailing market for a security.[10] Similarly, in a highly volatile market (*e.g.*, the trading on October 15, 2014), the "most recent" transaction may not be the most representative evidence of the prevailing market. Accordingly, the MSRB should recognize that firms will have to implement policies and procedures reasonably designed to determine the most representative evidence of the prevailing market even when the "most recent" transaction is not the most representative evidence of the prevailing market.

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[8] MSRB Regulatory Notice 2016-07 at 17.

[9] MSRB Regulatory Notice 2016-07 at 17.

[10] As we have noted, we urge the MSRB to confirm that trades that do not occur on the same day will not be considered contemporaneous.

B. Firms Should Be Permitted To Consider The Size Of Transactions And Side Of The Market As Relevant Factors In Determining Prevailing Market Price

Under the draft guidance, a dealer may be able to show that its contemporaneous cost or proceeds are not indicative of the prevailing market price in instances where: "(A) interest rates changed after the dealer's contemporaneous transaction to a degree that such change would reasonably cause a change in municipal securities pricing; (B) the credit quality of the municipal security changed significantly after the dealer's contemporaneous transaction; or (C) news was issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the municipal security after the dealer's contemporaneous transaction."[11]

Nevertheless, the draft guidance does not address the size of a transaction as a relevant factor in determining prevailing market price. As we noted in our 2010 comment letter, given the economic reality that market values and spreads can differ widely for small trades and institutional-size trades, transaction size is a critical factor in determining prevailing market price of a particular security. SIFMA is concerned that, under the Proposal, dealers will be required to use the prices resulting from institutional-size trades as the prevailing market price from which they would be required to compute mark-ups on subsequent small bond trades. Absent further clarity, the Proposal may have the unintended consequence of impairing liquidity for retail investors.

Accordingly, the MSRB should revise its draft guidance to acknowledge the differences in market values and spreads between small trades and institutional-size trades. In particular, the MSRB should permit transaction size to be taken into account and allow dealers to adjust to account for, for the purposes of determining prevailing market price, the discount or premium inherent in pricing small or institutional-size transactions.

In addition, the MSRB should provide more explicit guidance permitting firms to adjust to account for the side of the market (*i.e.*, bid or offer) in reaching a prevailing market price determination. The Proposal suggests that "whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction" may impact the consideration of comparison transactions, but does not explicitly state that the MSRB expects dealers to adjust for this factor.[12] Similarly, FINRA rules recognize that, although the interdealer market is the natural point of reference for calculating prevailing market price, the side of the market is also a

[11] MSRB Regulatory Notice 2016-07 at 17-18.

[12] MSRB Regulatory Notice 2016-07 at 19.

relevant factor in the analysis.[13] It follows that the prevailing market price should be adjusted from any price reference point to reflect any differences between the characteristics of the transactions, including side of the market, whether the transaction involves an interdealer or customer trade, and size of the transaction. For example, when an observed interdealer offer is the only available price reference and the dealer needs to determine the prevailing market price for a bid in that same security, it would be reasonable for the dealer to adjust the observed interdealer offer by a commercially-acceptable spread to determine the dealer bid prevailing market price, from which it then determines its final price inclusive of any mark-down. Similarly, if the only price reference available is a dealer's contemporaneous cost from its round lot purchase in an interdealer transaction, the dealer should be able to adjust its prevailing market price by a commercially-acceptable spread to reflect an interdealer odd lot bid in the same security, and then, in turn, determine its final price inclusive of any mark-down. To ensure greater consistency across firms, the MSRB should provide explicit guidance clarifying that these sorts of market price adjustments are anticipated in evaluating the various factors of the waterfall.

C. The Definition Of "Similar" Securities Should Be Clarified

The MSRB should provide greater clarity regarding the meaning of "similar," confirming that it is ultimately a subjective determination. Under the MSRB's draft guidance, dealers may often need to consult factors further down the waterfall, such as trades related to "similar" municipal securities, as indicia of prevailing market price. According to the Proposal, a "similar" municipal security "should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor."[14] The draft guidance instructs dealers to take into account measures including credit quality, spread, general structural characteristics, technical factors, and federal and/or state tax treatment, but leaves the direction regarding how each of these factors should be assessed or weighed against one another to the dealers.

The MSRB should explicitly recognize that firms will assess these and other factors based on the facts and circumstances, market conditions, and securities involved in a particular transaction and accordingly may weigh these factors differently in different cases.

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[13] FINRA Rule 2121, Supplementary Material .07 (explaining that the relative weight of certain pricing information for the purpose of calculating prevailing market price "depends on the facts and circumstances of the comparison transaction or quotation (*i.e.*, such as whether the dealer in the comparison transaction was on the same side of the market as the dealer is in the subject transaction and timeliness of the information)").

[14] MSRB Regulatory Notice 2016-07 at 19.

D. The Terms "Isolated Transactions" And "Isolated Quotations" Should Be Defined

The Proposal states that "isolated transactions or isolated quotations generally will have little or no weight or relevance in establishing prevailing market price," however, the terms "isolated transactions" and "isolated quotations" are not defined.[15] The MSRB notes that its treatment of "isolated transactions and quotations" is intended to track existing FINRA guidance, while acknowledging that "in the municipal securities market, the existence of only isolated transactions or quotations may be a more frequent occurrence than in other fixed income securities markets."[16]

SIFMA requests further guidance from the MSRB regarding its view of "isolated transactions and quotations." In particular, we note that "isolated" should not imply a strictly temporal consideration; for example, a trade that was not at market should be treated as an "isolated" transaction. Determining whether or not a transaction or quote is "isolated" will require firms to undertake a facts and circumstances analysis and the MSRB should delineate some of the factors to consider in making such a determination. Consistent with any such further guidance, firms should be permitted to rely on policies and procedures reasonably designed to identify such isolated transactions and isolated quotations for the purpose of a prevailing market price calculation.

E. The Proposed Guidance Should Be Applied Solely In The Context Of The Proposed Retail Disclosure Requirement Or Otherwise Limited Solely To Retail Investors

We commend both the MSRB and FINRA for their proposals to limit any future confirmation disclosure requirement to retail customer accounts, requiring disclosure on confirmations for non-institutional accounts only.[17] Specifically, under the MSRB's most recent proposal, disclosure would be limited to transactions for an account other than an "institutional account," as defined in MSRB Rule G-8(a)(xi).[18]

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[15] MSRB Regulatory Notice 2016-07 at 19.

[16] MSRB Regulatory Notice 2016-07 at 8.

[17] MSRB Regulatory Notice 2015-16; FINRA Regulatory Notice 15-36.

[18] MSRB Regulatory Notice 2015-16 at 9. Rule G-8(a)(xi) defines the term "institutional account" as "the account of (i) a bank, savings and loan association, insurance company, or registered investment company; (ii) an investment adviser registered 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

Similarly, FINRA's most recent proposal would exclude transactions that involve an institutional account, as defined in FINRA Rule 4512(c).[19] In drawing a clear retail/institutional distinction, the MSRB noted that the SEC Municipal Report showed that "retail municipal securities investors pay higher transaction costs than institutional investors or investors in other asset classes, and attributing these differences, in part, to a lack of information, support the potential benefit of additional disclosure."[20] FINRA noted that limiting the disclosure requirement to non-institutional accounts "may lessen some of the costs and complexity associated with [confirmation disclosure] by allowing firms to use an existing distinction that already is integrated into their operations."[21] In that regard, it is clear that this draft MSRB guidance has originated as a necessary technical clarification solely in the context of the proposed retail disclosure requirement. Accordingly, the draft guidance should be adopted solely as part of the proposed retail disclosure requirement rather than as general guidance under Rule G-30. The fair pricing provisions under Rule G-30 have served as the underpinning or foundation to pricing in municipal securities for over 35 years and have generally been an effective means to define a dealer's obligations given the particular structure of the municipal marketplace. We do not believe that the guidance is necessary or constructive with respect to the broader fair pricing obligations and provides no regulatory benefit while increasing operational complexity, especially in relation to institutional clients. In any event, should the MSRB proceed to adopt any prevailing market price guidance under Rule G-30, we believe that institutional accounts should be excluded from the definition of customer in the guidance to limit the scope to transactions with retail clients.

F. As A General Matter, The MSRB Should Provide Specific Examples Regarding How To Determine And Disclose A Prevailing Market Price In Various Scenarios

In MSRB Notice 2010-10, the MSRB offered a number of examples intended to clarify its expectations regarding how to determine the prevailing market price in a variety of scenarios. Although SIFMA requested clarifications regarding some of

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entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least $50 million."

[19] FINRA Regulatory Notice 15-36 at 3. FINRA Rule 4512(c) defines "institutional account" as "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."

[20] MSRB Regulatory Notice 2015-16 at 14.

[21] FINRA Regulatory Notice 15-36 at 10.

these examples in our 2010 comment letter, overall we found the examples helpful to understanding the MSRB's expectations more clearly.

For this reason, we urge the MSRB to provide additional examples and explanations regarding how to calculate prevailing market price in various complex scenarios under its latest draft guidance. In particular, we request specific examples regarding how and when a prevailing market price calculation should appear on customer confirmations. As we have emphasized, firms should be afforded a level of flexibility in calculating a prevailing market price given the inherent subjectivity involved in reaching such a determination. Nevertheless, we believe that clear examples would provide invaluable guidance on how the MSRB expects firms to reach and disclose on customer confirmations their prevailing market price determinations.

To this end, we have provided below four relatively straightforward examples designed to illustrate how some firms may approach a confirmation disclosure requirement under various scenarios. We would appreciate the MSRB's views on these initial examples and request that the MSRB provide additional examples reflective of a wide range of market conditions and complex scenarios. We have offered only a few examples due to the time constraints of the comment period, however, we would emphasize that there are clearly more complex scenarios that will require firms to make difficult judgments about how to evaluate the information available to them in the context of the waterfall (*e.g.*, where a firm buys a large block and sells in considerably smaller pieces throughout the day, or if the market moves significantly during the day and there are trades before, during, and after the market movement). We would welcome the opportunity to discuss our concerns in greater detail with the MSRB and to submit additional examples at a later date.

Illustration 1. A common market scenario involves a retail customer who wishes to sell a municipal security. A dealer working with the customer uses an alternative trading system ("ATS") and/or the services of a broker's broker to solicit bids for the securities.[22] After receiving information on the bids received through the ATS or by the broker's broker, the dealer ascertains the best bid available to it. If the customer wishes to proceed with the transaction, the customer's order is taken and the dealer executes simultaneous or near-simultaneous principal transactions with the customer and the ATS/broker's broker.[23] The dealer's price on the ATS/broker's broker transaction must be used as the prevailing market price for the purpose of

[22] Although we refer to use of an ATS for the purpose of this and other examples, we note as a general matter that dealers may determine there are better ways to establish price for a particular trade depending on market conditions.

[23] *See generally* MSRB, Report on Secondary Market Trading in the Municipal Securities Market (July 2014) at 24 (Figure III.F) (noting that the vast majority of all trades that were followed by another trade in the same municipal security on the same day had the second trade occur within 15 minutes).

calculating the mark-down. The dealer's price would be disclosed on the customer confirmation as the prevailing market price, along with the mark-down.

Illustration 2. In this scenario, a dealer is working with a retail customer who wishes to buy municipal securities of a particular type, quantity, and price. The dealer locates securities meeting the customer's requirements via an ATS or among posted inter-dealer offerings or "bid-wanted lists." After obtaining the customer's commitment to effect a transaction in one of the securities located, the dealer takes the customer's order and effects simultaneous or near-simultaneous principal transactions in which the securities are purchased in the market and sold to the customer. The dealer's purchase price must be used as the prevailing market price for the purpose of calculating the mark-up. The dealer's price would be disclosed on the customer confirmation as the prevailing market price, along with the mark-up.

Illustration 3. A dealer acquires a position in a municipal security through a single transaction with another dealer early in the trading day without having any existing customer orders for the security. The dealer immediately reoffers the security and shortly thereafter receives a customer order for the security and sells the entire position in a single sale to the customer. Absent countervailing evidence, the inter-dealer purchase transaction would be considered a contemporaneous transaction with respect to the sale transaction to the customer.

While the dealer's purchase price would be considered the contemporaneous cost pursuant to the proposed guidance and should be considered the most representative evidence of the prevailing market price for the purposes of determining the price for any same day customer sale, unlike the transaction described in Illustration 2 above, the sale price to the customer would not be the same price (dealer cost) at which the dealer purchased the security earlier in the day. Instead, the re-offer price would be adjusted from the dealer's purchase transaction to account for the different sides of the market.[24] The dealer's re-offer price must be used as the prevailing market price for the purpose of calculating the mark-up. The dealer's re-offer price would be disclosed on the customer confirmation as the prevailing market price, along with the mark-up.[25]

Illustration 4. A retail customer (Customer A) wishes to sell a particular security. The dealer solicits bids for the security via an ATS and also submits their own bid. After collecting and reviewing several external bids, it is determined that the dealer's own bid resulted in the best price for customer A. The security is purchased

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[24] *See supra* Part II.B regarding the need to consider side of the market as a relevant factor in determining prevailing market price.

[25] To continue this example, we would welcome the MSRB's guidance regarding how it would expect firms to approach confirmation disclosure operationally should a second purchase transaction in the same security occur later that same day at a different price.

from Customer A at the best bid less the dealer mark-down. The dealer's bid price must be used as the prevailing market price for the purpose of calculating the mark-down. The dealer's bid price would be disclosed on the customer confirmation as the prevailing market price, along with the mark-down.

Similar to Illustration 3 above, the dealer immediately reoffers the security and shortly thereafter receives a customer order for the security and sells the entire position in a single sale to the customer (Customer B). Absent countervailing evidence, the dealer's purchase transaction from Customer A would be considered a contemporaneous transaction with respect to the sale transaction to Customer B.

While the dealer's purchase price from Customer A would be considered the contemporaneous cost pursuant to the proposed guidance and should be considered the most representative evidence of the prevailing market price for the purposes of determining the price for any same-day customer sale, unlike the transaction described in Illustration 2 above, the prevailing market price to Customer B would not be the same price (dealer cost) at which the dealer purchased the security earlier in the day from Customer A. Instead, the re-offer price would be adjusted from the dealer's purchase transaction to account for the different sides of the market. The dealer's re-offer price must be used as the prevailing market price for the purpose of calculating the mark-up. The dealer's re-offer price would be disclosed on the customer confirmation as the prevailing market price, along with the mark-up.

III. THE MSRB SHOULD COORDINATE THE ADOPTION OF ANY FUTURE PREVAILING MARKET PRICE CALCULATION AND DISCLOSURE REQUIREMENTS AND PROVIDE, AT MINIMUM, A SYNCHRONIZED IMPLEMENTATION PERIOD OF THREE YEARS.

The MSRB should coordinate the adoption and implementation of any guidance on establishing prevailing market price with that of any confirmation disclosure requirement. Imposing new requirements relating to the calculation of prevailing market price in the short-term, followed by a longer timeline for the adoption and implementation of any future confirmation disclosure requirement, would present overlapping challenges and unnecessary costs. Accordingly, the MSRB should adopt such requirements at the same time and should provide, at minimum, a synchronized three year implementation period. This approach would be most consistent with the MSRB's desire to "reduce dealer implementation and compliance costs," particularly "with respect to a possible future mark-up disclosure requirement."[26]

[26] MSRB Regulatory Notice 2016-07 at 4-5.

As noted above, firms already have policies and procedures in place designed to ensure compliance with their obligation to provide fair and reasonable prices under current MSRB Rule G-30, however, firms have never been required to calculate an exact prevailing market price for every retail customer transaction, in a short timeframe, for the purpose of confirmation disclosure. Requiring firms to estimate a prevailing market price to an exact decimal point and to print this calculation on all retail customer confirmations would introduce substantial operational complexity and new programming challenges for all impacted firms.

Programming firm systems for this type of disclosure will be extraordinarily complex. To enable programmers to build the proper controls, firms will be required to make certain assumptions about their disclosure obligations across a variety of fact patterns and market conditions. To the extent the MSRB provides additional guidance regarding how to implement prevailing market price confirmation disclosure in the manner we have described above, firms will be more readily able to code for and implement such a regime.

As we emphasized in our comment letter regarding MSRB Regulatory Notice 2015-16 and FINRA Regulatory Notice 15-36, the same technology and operational experts working to implement a two-day settlement cycle (T+2) and other major regulatory objectives will be necessary to any effort to implement a new confirmation disclosure requirement. Accordingly, given the substantial technical and programming challenges to implementation and the multiple regulatory demands firms must address, the MSRB should provide, at minimum, three years to program, test, and implement such a complex technology project.

For these reasons, any guidance on establishing prevailing market price should be coordinated with the adoption of any confirmation disclosure requirement.

IV. THE MSRB MUST CONDUCT A ROBUST COST-BENEFIT ANALYSIS THAT DEMONSTRATES THAT ITS PROPOSAL IS NEEDED, THAT THE COSTS ASSOCIATED WITH IT ARE NECESSARY, AND THAT NO OTHER LESS BURDENSOME ALTERNATIVE WOULD MEET THE OBJECTIVE.

The MSRB must conduct a robust cost-benefit analysis that demonstrates that its Proposal is needed, that the costs associated with it is necessary, and that no other less burdensome alternative would meet its regulatory objective. As we have emphasized in the context of any future confirmation disclosure requirement, the costs and burdens associated with implementation and ongoing compliance are substantial. With respect to confirmation disclosure, our initial estimates suggest that technology costs for introducing firms would range from $500,000 for smaller firms to as much as $2.5 million for large diverse organizations, not including any of the significant ongoing costs related to additional surveillance, personnel, and system maintenance, or any of the substantial implementation and ongoing legal and compliance costs associated with such a requirement. In addition, we note that the risks of a small

reduction in retail bond market liquidity could easily injure investors far more seriously than any benefit to be gained by the implementation of a prevailing market price confirmation disclosure requirement. We continue to believe that the MSRB and FINRA have not addressed the significant costs that a confirmation disclosure requirement would impose on introducing firms, clearing firms, and front-end vendors, and we urge both the MSRB and FINRA to undertake meaningful and rigorous economic analyses in order to justify their rulemaking.[27]

CONCLUSION

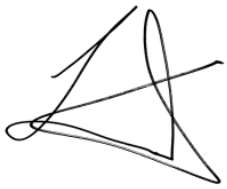
SIFMA thanks the MSRB for the opportunity to comment on this draft interpretive guidance. We appreciate the MSRB's efforts to address the concerns that we have raised regarding a prevailing market price disclosure requirement.

Should a prevailing market price disclosure framework proceed, we urge the MSRB and FINRA to coordinate to the greatest extent possible to resolve the concerns we have raised in this letter and to adopt a clear and consistent standard. In particular, regulators should acknowledge that there is an inherent variability in the determination of a prevailing market price and permit firms to rely on reasonable policies and procedures for the purpose of confirmation disclosure. Regulators should also recognize that estimating a prevailing market price in a short timeframe based on information available at the time of the transaction for the purpose of confirmation disclosure is not necessarily determinative of the prevailing market price for the purpose of scrutinizing a fair and reasonable mark-up.

[27] While we recognize the differences inherent in SEC and SRO rulemaking, we think it is important that the MSRB justify its rulemaking with the same level of rigorous cost-benefit analysis. We note that, in recent years, some members of the Commission have questioned openly whether SROs "have the resources – and, just as importantly, the willingness – to perform sufficiently rigorous analyses to support their rulemaking" and have emphasized that "SROs must be committed to ensuring that the rules they send to the Commission for approval are the result of the same degree of rigorous analysis as the Commission applies to its own rules." *See* Daniel M. Gallagher, Commissioner, SEC, "Market 2012: Time for a Fresh Look at Equity Market Structure and Self-Regulation" (Oct 4, 2012).

Should you have any questions, please do not hesitate to contact the undersigned or Brandon Becker and Bruce Newman, SIFMA's outside counsel at Wilmer Cutler Pickering Hale and Dorr LLP, at (202) 663-6000.

Respectfully submitted,



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March 31, 2016

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street NW, Suite 1000
Washington, DC 20005

Re: Comment on Draft Amendments to MSRB Rule G-30

Dear Mr. Smith:

This letter is in response to the request for comments on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price. Comments were requested on whether it is appropriate to tailor the Draft Guidance on Prevailing Market Price to the FINRA Guidance on prevailing market price for non-municipal fixed income securities. As an issuer and routine market participant, our concerns are whether there is a need for this regulation and the specificity used in defining "prevailing market price" in the absence of some abuse or clear benefit to the market, neither of which is present.

The adoption of this guidance will not produce the expected efficiencies due to the unique nature of the municipal market. By virtue of its 65,000 issuers, the CUSIP numbers created for every serial maturity, and the different kinds of securities, the municipal market will always require consideration of additional factors by dealers in determining prevailing market price. Because of how municipal bonds price and trade, the administrative burden imposed on dealers by this method of determining prevailing market price outweighs any potential efficiency in developing pricing guidelines consistent with those for other fixed income securities.

Overregulation of dealers in the municipal market may adversely affect liquidity or lead to unwillingness for dealers to trade on behalf of retail customers. There has already been a contraction of the number of participating dealers in the market as casualties of the financial crisis. New regulations have also discouraged financial institutions from investing in municipal bonds through various vehicles. Imposing additional costly regulatory burdens on the firms that still participate in the municipal market will impact their willingness to risk capital, which diminishes the amount of support for and the liquidity of the municipal market.

Ultimately, these regulations provide no benefit to the market or to investors. The municipal market investor base is fundamentally different from other markets, and greater transparency is

unlikely to improve market efficiency or attract new investors. In the absence of any articulated benefits to the market or to investors and when there is no existing problem to address, such stringent definitions and interpretations of rules only burden the market rather than improve it.

Thank you for your consideration.

Sincerely,

J. Ben Watkins III, Director
Division of Bond Finance

THOMSON REUTERS

Via Electronic Delivery

March 31, 2016

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

Re: MSRB Regulatory Notice 2016-07 - Request for Comment on Draft Amendments to MSRB Rule G-30 to Provide Guidance on Prevailing Market Price

Dear Mr. Smith:

Thomson Reuters appreciates the opportunity to comment on MSRB Regulatory Notice 2015-07 (the "notice"). Thomson Reuters[1] 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. Our clients are active participants in the municipal market and we provide decision support tools and processing in support of their municipal trading activities.

We applaud MSRB for seeking comment on prevailing market price guidance as requested in our comment letter on MSRB Regulatory Notice 2015-16.[2] The proposed guidance provided in the notice included request for comment on several key aspects of the proposed guidance. Please see our feedback on several of these issues below.

Hierarchical Approach/Presumption of Contemporaneous Cost

The notice asks for comment on whether the hierarchical approach suggested for determining the prevailing market price is appropriate for the municipal market. This approach includes a presumption that a dealer will initiate their determination of prevailing market price by considering contemporaneous cost. We believe that a number of factors should be considered in evaluating the appropriateness of the hierarchical approach for a municipal security: (1) trading volume, (2) frequency of trading, and (3)

[1] 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.

[2] See letter from Manisha Kimmel, Chief Regulatory Officer, Wealth Management, Thomson Reuters, dated December 11, 2015

trade size. Given the findings of MSRB's July 2014 report on secondary trading in the municipal market which indicated that 50% of municipal securities do not trade more than once in the same day, we believe that the presumption of contemporaneous cost as the primary method of determining prevailing market price may not be an appropriate starting point for the hierarchical approach.[3] Instead, we would suggest that dealers be allowed to consider trading volume, trading frequency and trade size and then choose the most appropriate methodology.

It is our belief that economic models considering the three factors mentioned as well as other objective and subjective attributes are used during the pre-trade process. The use of economic models at the onset should be recognized as a valid methodology for determining prevailing market price. Firms that trade municipals are often looking for a municipal security that meets a certain set of characteristics including yield, tax treatment and use models to identify and price those securities. Additionally, available liquidity is a determinant of prevailing market price that is incorporated into economic models and may have a material impact on pricing.

To that end, we recommend specific guidance to help firms in determining prevailing market price:

- Establish a rebuttable presumption of contemporaneous cost within reason. For example, allow firms to consider other approaches for municipal securities that have not traded more than once in the same day.
- Allow intervening changes in yield to overcome the presumption of contemporaneous cost. Changes in yield or spread to benchmarks are often associated with interest rate changes but firms may be looking at the benchmark rather than interest rates when determining the prevailing market price.
- Add liquidity measures such as trade size, frequency of trading, and trade volume as considerations for overcoming the contemporaneous cost presumption.
- Acknowledge that firms may use economic models earlier in the process.

Other Considerations

- **Similar Securities**: Given the number of municipal securities and the relative illiquidity of the municipal market compared to other fixed income markets, we suggest consideration of additional attributes in identifying similar securities. These attributes include tax status, obligor, security type, sector, use of proceeds, coupon rate, optionality, and settlement date.
- **Isolated Transactions:** Isolated transactions can include off-market transactions including swaps or other type of derivative-based transactions. We suggest additional guidance or identifiers could reference these types of transactions.
- **Implementation time:** As MSRB seeks to operationalize prevailing market guidance, we would respectfully request that MSRB offer firms sufficient implementation time. While firms are required to determine prevailing market

[3] MSRB Report on Secondary Market Trading in the Municipal Securities Market, July 2014

price today, the processes for determining prevailing price may require alignment with final guidance. Similar to the changes proposed in MSRB 2015-16, firms will also need time to integrate the policies and procedures developed in adherence with final guidance into trading and ancillary systems. It is worth noting that both institutional and retail trading systems and workflows will need to accommodate changes required by this proposed guidance.

We appreciate the opportunity to provide comments on this important issue and look forward to commenting on future rule-making in this area.

Regards,

Manisha Kimmel
Chief Regulatory Officer, Wealth Management
Thomson Reuters

EXHIBIT 5

Rule G-15: Confirmation, Clearance, Settlement and Other Uniform Practice Requirements with Respect to Transactions with Customers

(a) *Customer Confirmations.*

(i) At or before the completion of a transaction in municipal securities with or for the account of a customer, each broker, dealer or municipal securities dealer shall give or send to the customer a written confirmation that complies with the requirements of this paragraph (i):

(A) Transaction information. The confirmation shall include information regarding the terms of the transaction as set forth in this subparagraph (A):

(1) No change.

(2) Trade date and time of execution. The trade date and time of execution shall be shown; provided that, for a transaction in municipal fund securities, a statement that the time of execution will be furnished upon written request of the customer may be shown in satisfaction of the obligation to disclose the time of execution on the confirmation. [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.]

(3) – (8) No change.

(B) – (C) No change.

(D) Disclosure statements:

(1) – (3) No change.

(4) The confirmation for a transaction (other than a transaction in municipal fund securities) executed for or with a non-institutional customer shall include a reference, and hyperlink if the confirmation is electronic 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.

(E) Confirmation format. All requirements must be clearly and specifically indicated on the front of the confirmation, except that the following statements may be on the reverse side of the confirmation:

(1) – (2) No change.

[(3) The statement concerning time of execution that can be provided in satisfaction of subparagraph (A)(2) of this paragraph.]

(F) Mark-ups and Mark-downs.

(1) General. A confirmation shall include the dealer's mark-up or mark-down for the transaction, to be calculated in compliance with Rule G-30, Supplementary Material .06 and expressed as a total dollar amount and as a percentage of the prevailing market price if:

(a) the broker, dealer or municipal securities dealer ("dealer") is effecting a transaction in a principal capacity with a non-institutional customer, and

(b) the broker, dealer or municipal securities dealer purchased (sold) the security in one or more transactions in an aggregate trading size meeting or exceeding the size of such sale to (purchase from) the non-institutional customer on the same trading day as the non-institutional customer transaction. If any such transaction occurs with an affiliate of the dealer and is not an arms-length transaction, the dealer is required to "look through" to the time and terms of the affiliate's transaction(s) with third parties in the security in determining whether the conditions of this paragraph have been met.

(2) Exceptions. A dealer shall not be required to include the disclosure specified in paragraph (F)(1) above if:

(a) the non-institutional 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 the dealer had in place policies and procedures reasonably designed to ensure that the functionally separate principal trading desk through which the dealer purchase or dealer sale was executed had no knowledge of the customer transaction;

(b) the customer transaction is a "list offering price transaction" as defined in paragraph (d)(vii) of Rule G-14 RTRS Procedures; or

(c) the customer transaction is for the purchase or sale of municipal fund securities.

(ii) – (v) No change.

(vi) Definitions. For purposes of this rule, the following terms shall have the following meanings:

(A) – (H) No change.

(I) The term "arms-length transaction" shall mean a transaction that was conducted through a competitive process in which non-affiliate firms could also participate, and where the affiliate relationship did not influence the price paid or proceeds received by the dealer.

(J) The term "non-institutional customer" shall mean a customer with an account that is not an institutional account, as defined in Rule G-8(a)(xi).

(vii) – (viii) No change.

(b) – (g) No change.

* * * * *

Rule G-30: Prices and Commissions

(a) – (b) No change.

Supplementary Material

.01 General Principles.

(a) Each broker, dealer or municipal securities dealer (each, a "dealer," and collectively, "dealers"), whether effecting a trade on an agency or principal basis, must exercise reasonable diligence in establishing the market value of the security and the reasonableness of the compensation received on the transaction.

(b) – (c) No change.

(d) Dealer compensation on a principal transaction with a customer is considered to be a mark-up or mark-down that is computed from the [inter-dealer market price]prevailing market price at the time of the customer transaction, as described in Supplementary Material .06. As part of the aggregate price to the customer, the mark-up or mark-down also must be a fair and reasonable amount, taking into account all relevant factors.

(e) No change.

.02 – .05 No change.

.06 Mark-Up Policy

(a) Prevailing Market Price

(i) A dealer that is acting in a principal capacity in a transaction with a customer and is charging a mark-up or mark-down must mark-up or mark-down the transaction from the prevailing market price. Presumptively for purposes of this Supplementary Material .06, the prevailing market price for a municipal security is established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained, consistent with applicable MSRB rules. (See, e.g., Rule G-18).

(ii) When the dealer is selling the municipal security to a customer, other evidence of the prevailing market price may be considered only where the dealer made no contemporaneous purchases of the security or can show that in the particular circumstances the dealer's contemporaneous cost is not indicative of the prevailing market price. When the dealer is buying the municipal security from a customer, other evidence of the prevailing market price may be considered only where the dealer made no contemporaneous sales of the security or can show that in the particular circumstances the dealer's contemporaneous proceeds are not indicative of the prevailing market price.

(iii) A dealer's cost is (or proceeds are) considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the municipal security.

(iv) A dealer that effects a transaction in municipal securities with a customer and identifies the prevailing market price using a measure other than the dealer's own contemporaneous cost (or, in a mark-down, the dealer's own proceeds) must be prepared to provide evidence that is sufficient to overcome the presumption that such contemporaneous cost (or proceeds) provides the best measure of the prevailing market price. A dealer may be able to show that such contemporaneous cost is (or proceeds are) not indicative of prevailing market price, and thus overcome the presumption, in instances where: (A) interest rates changed after the dealer's contemporaneous transaction to a degree that such change would reasonably cause a change in municipal securities pricing; (B) the credit quality of the municipal security changed significantly after the dealer's contemporaneous transaction; or (C) news was issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the municipal security after the dealer's contemporaneous transaction.

(v) In instances where the dealer has established that the dealer's cost is (or, in a mark-down, proceeds are) not contemporaneous, or where the dealer has

presented evidence that is sufficient to overcome the presumption that the dealer's contemporaneous cost (or proceeds) provides the best measure of the prevailing market price, such as those instances described in (a)(iv)(A), (B) and (C), the dealer must consider, in the order listed and subject to (a)(viii), the following types of pricing information to determine prevailing market price:

(A) Prices of any contemporaneous inter-dealer transactions in the municipal security in question;

(B) In the absence of transactions described in (A), prices of contemporaneous dealer purchases (sales) in the municipal security in question from (to) institutional accounts with which any dealer regularly effects transactions in the same municipal security; or

(C) In the absence of transactions described in (A) and (B), for actively traded municipal securities, contemporaneous bid (offer) quotations for the municipal security in question made through an inter-dealer mechanism, through which transactions generally occur at the displayed quotations.

(A dealer may consider a succeeding category of pricing information only when the prior category does not generate relevant pricing information (e.g., a dealer may consider pricing information under (B) only after the dealer has determined, after applying (A), that there are no contemporaneous inter-dealer transactions in the same security).) In reviewing the pricing information available within each category, the relative weight, for purposes of identifying prevailing market price, of such information (i.e., a particular transaction price or quotation) depends on the facts and circumstances of the comparison transaction or quotation (e.g., whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction and timeliness of the information). Because of the lack of active trading in most municipal securities, it is not always possible to establish the prevailing market price for a municipal security based solely on contemporaneous transaction prices or contemporaneous quotations for the security. Accordingly, dealers may often need to consider other factors, consistent with (a)(vi) and (a)(vii) below.

(vi) In the event that, in particular circumstances, the above factors are not available, other factors that may be taken into consideration (not in any required order or combination) for the purpose of establishing the price from which a customer mark-up (mark-down) may be calculated, include but are not limited to:

• Prices, or yields calculated from prices, of contemporaneous inter-dealer transactions in a “similar” municipal security, as defined below;

• Prices, or yields calculated from prices, of contemporaneous dealer purchase (sale) transactions in a "similar" municipal security with institutional accounts with which any dealer regularly effects transactions in the "similar" municipal security with respect to customer mark-ups (mark-downs); and

• Yields calculated from validated contemporaneous inter-dealer bid (offer) quotations in "similar" municipal securities for customer mark-ups (mark-downs).

The relative weight, for purposes of identifying prevailing market price, of the pricing information obtained from the factors set forth above depends on the facts and circumstances surrounding the comparison transaction (i.e., whether the dealer in the comparison transaction was on the same side of the market as the dealer in the subject transaction, timeliness of the information, and, with respect to the final factor listed above, the relative spread of the quotations in the similar municipal security to the quotations in the subject security).

(vii) Finally, if information concerning the prevailing market price of the subject municipal security cannot be obtained by applying any of the above factors, dealers (and the regulatory agencies responsible for enforcing MSRB rules) may consider as a factor in assessing the prevailing market price of a municipal security the prices or yields derived from economic models (e.g., discounted cash flow models) that take into account measures such as reported trade prices, credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value; and consider all applicable pricing terms and conventions (e.g., coupon frequency and accrual methods).

(viii) Because the ultimate evidentiary issue is the prevailing market price, isolated transactions or isolated quotations generally will have little or no weight or relevance in establishing prevailing market price. For example, in considering the pricing information described in (a)(v), a dealer may give little or no weight to pricing information derived from an isolated transaction or quotation, such as an off-market transaction. In addition, in considering yields of "similar" municipal securities, except in extraordinary circumstances, dealers may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" municipal securities taken as a whole.

(b) "Similar" Municipal Securities

(i) A "similar" municipal security should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor. At a minimum, the municipal security or securities should be sufficiently similar that a market yield for the subject security can be fairly estimated from the

yields of the "similar" security or securities. Where a municipal security has several components, appropriate consideration may also be given to the prices or yields of the various components of the security.

(ii) The degree to which a municipal security is "similar," as that term is used in this Supplementary Material .06, to the subject security may be determined by all relevant factors, including but not limited to the following:

(A) Credit quality considerations, such as whether the municipal security is issued by the same or similar entity, bears the same or similar credit rating, or is supported by a similarly strong guarantee or collateral as the subject security (to the extent securities of other issuers are designated as "similar" securities, significant recent information concerning either the "similar" security's issuer or subject security's issuer that is not yet incorporated in credit ratings should be considered (e.g., changes to ratings outlooks));

(B) The extent to which the spread (i.e., the spread over U.S. Treasury securities of a similar duration) at which the "similar" municipal security trades is comparable to the spread at which the subject security trades;

(C) General structural characteristics and provisions of the issue, such as coupon, maturity, duration, complexity or uniqueness of the structure, callability, the likelihood that the municipal security will be called, tendered or exchanged, and other embedded options, as compared with the characteristics of the subject security;

(D) Technical factors such as the size of the issue, the float and recent turnover of the issue, and legal restrictions on transferability as compared with the subject security; and

(E) The extent to which the federal and/or state tax treatment of the "similar" municipal security is comparable to such tax treatment of the subject security.

(iii) When a municipal security's value and pricing is based substantially on, and is highly dependent on, the particular circumstances of the issuer, including creditworthiness and the ability and willingness of the issuer to meet the specific obligations of the security, in most cases other securities will not be sufficiently similar, and therefore, pricing information with respect to other securities may not be used to establish the prevailing market price.