



October 21, 2011

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

Re: Regulatory Notice 11-43, Indications of Interest

Dear Ms. Asquith:

Thank you very much for the opportunity to provide comments on the FINRA proposal contained in Regulatory Notice 11-43 regarding Indications of Interest. This letter responds to the third of the list of four areas for which comments were encouraged:

Is the requirement that a firm has received a customer order before labeling an IOI or quotation in a manner that indicates the interest originated with a customer too limiting? Are there instances in which a customer would not want to place an order with a firm, but would want the firm to label an IOI in that manner? Is there an alternative standard that could achieve the same regulatory purpose? If so, what should that standard be?

There is a legitimate regulatory interest in ensuring that IOI communications are truthful, accurate, and non-misleading. Limiting the definition of a natural IOI to that of an order on the broker's order management system ("OMS"), however, may risk regulatory over-reaching and disrupt some current appropriate business practices. In turn, we feel that such limitations could limit competition and crowd out smaller broker dealers.

The current business practice can be highly effective. Many customers often do not wish to be fully committed on their IOI's, nor to one single brokerage firm. They may wish to give only a partial amount of their full order to a brokerage firm, and indicate verbally that there are additional shares behind, or they may prefer in some cases to give a verbal IOI to various brokers on a "first come, first serve" basis. Those brokers, in turn, send IOIs to their customer base, properly marked as natural. When the broker sees a print go up that isn't theirs, they should be contacting the customer to determine if that was their customer's print and if so, adjust their IOI accordingly. These practices enable customers to use multiple brokers as they see fit, all of which may have differing customer bases to receive their IOIs. These competitive practices afford the customer the ability to seek best execution, which benefits the individual investors behind the funds and other portfolios being traded.

Putting an end to brokers using verbal IOIs from institutional customers to, in turn, send natural IOIs to other customers, would limit competition and potentially thwart best

execution. Harming the market solely to make regulation easier undermines the purpose of regulation. Admittedly a compliance review would be easier under the proposed IOI requirements, but it would not necessarily make natural IOIs more truthful, accurate, and non-misleading. The current natural IOIs that are based upon verbals from customers already are fully truthful, accurate, and non-misleading when used properly.

The current natural IOI proposal would, in our view, crowd-out competition by benefiting the largest brokerage firms to the disadvantage of the medium and boutique brokerage firms. If institutional clients would have to physically place an order with a particular broker in order for that chosen broker to be able to represent a "natural" to the rest of their appropriate customer base, then those clients would have to be willing to expose more of their order than they currently might or may care to, and/or choose a single broker versus multiple brokers competing against one another, in order for any broker to accurately represent their interest to their customer base in the form of a natural IOI. In this proposed environment, customers then would be more likely to select the largest brokerage firms in many instances because, with the competitive factor removed, they would tend to leave their orders with the firms where they owe the largest commissions for other services rendered. Given that brokerage research is often paid for with order flow and given that the largest brokerage firms theoretically have the largest amounts owed to them for their research, customers would be more likely to select one of the largest brokers when forced in the new environment to expose more of their order to be represented at one single broker. Institutional customers would not break up their orders into several smaller pieces and disperse those pieces amongst multiple brokers, if they were trying to develop interest in a piece. The proposal could tend to diminish order flow to the smaller competitors in the brokerage industry and concentrate the volume in a small number of very large firms, crowding-out competition.

As an alternative to the current proposal, we suggest implementing a method which provides greater granularity in terms of distinguishing between various types of natural IOIs. Natural IOIs could be delineated among OMS based IOIs, verbally based IOIs, and "in touch with" based IOIs. OMS based IOIs would be based upon orders in a broker's OMS, verbally based IOIs upon verbal representations made by customers, and the current "in touch with" based IOIs upon recent activity or customer interest. That is, we suggest stratifying natural designations such that an IOI could specify Order Natural or Verbal Natural or In Touch With Natural to distinguish among them. This would preserve the use of the word "natural" in all situations that truly are natural, and it would leave it up to the customer to determine if they want to explore one of those avenues.

One area that we believe could potentially benefit from additional clarity, in any case, is the current natural "in touch with" based IOI designation ("natural ITW"). When a broker has neither a verbal IOI nor an order from a customer, but has been in communication with a customer that either has recently traded with the broker or expressed interest in potentially trading a security with that broker, a broker will often explore interest on the opposite side of the market with an IOI that denotes "natural ITW." It is possible that some brokers use that term for a short period, such as two days, and that other brokers use the same term for a significantly greater number of days. Perhaps it would be useful to provide clarity and level the playing field by specifying that natural ITW applies to the day that the broker had contact with the client regarding such activity or interest, plus the following business day, and that thereafter, without additional contact, the "natural ITW" designation would be inappropriate.

With clearly defined qualifiers on natural IOIs, and with more clarity about what those qualifiers indicate, there would likely be a reduction in instances where buy-side firms contact brokers regarding a natural IOI and end up having their expectations not met. They would be able to select which brokers to contact based upon qualifiers such as Order, Verbal, or ITW and enter into negotiations with brokers with a greater degree of confidence regarding what they might expect.

FINRA should avoid having the regulatory tail wag the industry dog for reasons of regulatory convenience. The ultimate investors in the market, the holders of mutual funds, pension/retirement funds, life insurance policies, etc. are better served by the current IOI practices in the industry. When a broker is representing the interest of a customer based upon a verbal IOI from a customer, the broker is in fact representing natural interest. Having a firm order does not make it any more natural than a verbal IOI. In neither scenario is the broker representing its own interest. The word "natural" has a meaning and it is currently being used in accordance with that meaning. This usage should be preserved.

Firms have internal procedures in place to review the accuracy of their natural IOIs and regulators can review for compliance with the accuracy requirements without requiring the system to be less efficient. Admittedly, it would be easier for regulators to conduct these reviews if the new proposal goes into effect, but such concerns should not drive the workings of the market. The regulatory standard should be that natural IOIs truly reflect customer interest and that firms have reasonable procedures in place to supervise for the accuracy of natural IOIs, such as internally notating the identity of a customer that gave the broker a verbal IOI upon which a natural IOI is based.

Thank you again for this opportunity to provide these comments.

Very truly yours,

Maureen McCarthy
Managing Director