



December 11, 2015

*Submitted electronically*

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Financial Industry Regulatory Authority  
1735 K Street, NW  
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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<sup>1</sup> (“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”).<sup>2</sup> 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<sup>3</sup> (the “initial Proposals”) on which Fidelity provided comments.<sup>4</sup>

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<sup>1</sup>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.

<sup>2</sup>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](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.

<sup>3</sup>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.<sup>5</sup> 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.<sup>6</sup>

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<sup>4</sup>Fidelity comment letter available at:

[http://www.finra.org/sites/default/files/notice\\_comment\\_file\\_ref/Fidelity\\_Investments\\_FINRA\\_RN14-52.pdf](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>

<sup>5</sup>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](http://Fidelity.com/commissions) for details.

<sup>6</sup>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 is discussed in further detail below.

### The FINRA and MSRB Proposals Must Be Harmonized.

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

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<sup>7</sup>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 electronic, to TRACE publicly available data.

<sup>8</sup>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.

<sup>9</sup>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<sup>10</sup> as well as different approaches to new issues<sup>11</sup>, and material changes in the price of a security.<sup>12</sup> 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.<sup>13</sup>

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.

<sup>10</sup>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.

<sup>11</sup>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.

<sup>12</sup>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.

<sup>13</sup>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.<sup>14</sup> 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.<sup>15</sup>

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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<sup>14</sup>*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)*

<sup>15</sup>*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.<sup>16</sup> 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.<sup>17</sup>

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

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<sup>16</sup>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.

<sup>17</sup>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.<sup>18</sup> 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.<sup>19</sup> A proposed VWAP or VWAS approach does not address the issue of fairness or reasonableness of dealer compensation because it does not provide trade specific information to investors which would highlight dealer prices significantly higher than others in the industry. The approach also presents significant operational difficulties in that if regulators or dealers were to calculate a VWAP or VWAS for each security after the end of each trading day, the process a broker-dealer uses to generate confirmation statements for retail investors could be delayed.

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

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<sup>18</sup>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>

<sup>19</sup>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.<sup>20</sup> 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.

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<sup>20</sup>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.<sup>21</sup> 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.

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<sup>21</sup>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).<sup>22</sup> SEC Commissioners Prowar and Stein have expressed support for the move to T+2 along with SEC Chair Mary Jo White.<sup>23</sup> Moreover, the MSRB has published a request for comment on changes to MSRB Rules to facilitate shortening the securities settlement cycle.<sup>24</sup>

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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<sup>22</sup>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).

<sup>23</sup> Commissioners Michael S. Prowar 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).

<sup>24</sup>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

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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.

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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  
Mr. Robert Colby, Chief Legal Officer, FINRA

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