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FINRA Public Comments
c/o Marcia Asquith
Office of the Corporate Secretary
1735 K Street, NW
Washington, DC 20006-1506

Ladies and Gentlemen:

I am pleased to comment on **FINRA Rule Proposal 14-52**, *Pricing Disclosure in the Fixed Income Markets*.

Romano Wealth Management is a 53 year old firm having prided itself on an impeccable reputation and no regulatory or customer complaints on record throughout its history. We have managed that feat by treating our clients fairly based on the way we would want to be treated, and believe that the vast majority of broker-dealers operate under this same principal. We oversee $1 billion dollars in client assets and create customized portfolios for retail investors using individual stocks and bonds as opposed to the more common approach of using financial products or third party asset managers. In this capacity, we are extremely active in the fixed income arena for corporate, municipal, and government agency securities, both on the inter-dealer market and in transactions with retail customers.

From the perspective of an active participant in this marketplace, let me state for the record that I find this rule proposal deeply troubling. I think it is misguided, patently unfair, anti-business, anti-free market, and overreaching.

FINRA begins its case stating in the rule proposal that by:

> ...using data from the third quarter of 2013 for corporate bonds, FINRA 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.

My response to this is, so what? Why is this relevant information? Nowhere in the rule proposal can I find an answer to this question.

So I posed this question to FINRA staff, and the discussion began by citing the number of times examiners walk into a firm and see a two or three percent markup for something in inventory for 15 minutes. Again, why is timeframe relevant? By focusing on markup and specifically only *gross* profit, it implies that the greater profit (and not the actual *net* profit) must mean that something nefarious is taking place. In focusing on gross vs. net profit, it avoids all other factors, like expenses (particularly the

increasing of regulatory compliance for one) and the general cost of doing business, like overhead. This is insulting to the plight of any business owner.

In addition, it ignores that in reality the *net* profit margin of the firm might be only 10% of the *gross* profit. Said differently, in this case it implies that the client is receiving meaningless data that overstates the actual profit by 90% or more!

Let me state that I am not an advocate for egregious markups and we would not have the reputation we covet were this the case. Suffice it to say, neither is FINRA, as this proposal is clearly focused (almost solely I might add) on markup transparency. The proposal continues in its background section:

> FINRA also has observed that while many of these trades have apparent mark-ups with a close range, significant outliers exist, indicating that customers in those trades paid considerably more than customers in other similar trades.

First, the real issue here is that of the "outliers", and we would agree that egregious markups are not in the best interest of the investing public, or honest broker dealers for that matter. However, FINRA already has at its disposal the tools necessary to combat such egregious markups. It has a long standing published markup policy and has clarified this rule from time to time to reflect the current market environment.

Second, FINRA already has in place effective market surveillance capabilities. As just one example, one area where firms already receive routine inquiries from FINRA are in regards to pricing on bonds at a slight premium with short term calls involving negative yields to call. This results in the potential for insignificant dollar loss to the client but significant negative yield due to the proximity to the near term call when calculated on a daily compounded basis. While this may not look good on an absolute basis it can have significant upside to the client with limited or insignificant downside. It is an appropriate issue to be flagged at its surface, but easily explained away. I cite this as an example of effective regulatory practices, and representative of the process that already takes place to protect the investing public.

Third, FINRA already has TRACE (and the municipal markets have the equivalent in EMMA), which is intended to give the investing public better trade and pricing transparency. FINRA acknowledges that all of the pertinent information is already disclosed, but then immediately dismisses it stating:

> 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.

This then, becomes the basis for the proposed rule at hand. Presumably because the investing public does not consult readily available TRACE data, the rule proposal cites Mary Jo White's speech given on June 20, 2014 where the proposal summarizes:

> Among other things, Chair White stated that the SEC would work with FINRA and the MSRB to develop rules regarding the disclosure of mark-ups in "riskless principal" transactions for both corporate and municipal bonds ***to help customers asses the reasonableness of their dealer's***

> ***compensation*** [emphasis my own], as riskless principal transactions become more common in the fixed income markets.

And there we have it, as therein lies the genesis for current rule proposal 14-52, which then continues to almost exclusively focus on dealer compensation and markup under the cloak of "additional pricing disclosure" throughout. But I ask bluntly, is it the role of Chairman White, the SEC itself, FINRA, the MSRB or any other regulatory agency for that matter to determine the reasonableness of compensation? Under what authority? And moreover how? By forcing the broker dealer to reveal *gross* profit that ignores expense and as already mentioned the cost of doing business and overhead??? I believe this to be a blatant abuse of authority at its worst and a severe overreach at its best, but that question is left for the attorneys to resolve.

More importantly, this proposed rule is simply misguided and off base. Markup and gross profit is not only out of reach, it is not the most relevant factor. The most relevant and determining factor is the end price to the retail client! This is the basis for which the total return to the client (yield) is determined, including markup, and is the sole basis for which a retail investor can reasonably base the quality of his or her execution when compared to other priced transactions in the same security.

Consider the following simple example, which while fictitious, routinely happens at our trading desk:

Romano Wealth Management's (RWM) fixed income trader sees an offering from another dealer for a $200,000 block of highly rated municipal bonds at a price of 102. After some haggling with that dealer, RWMs fixed income trader is able to bid the bonds back and buy $100,000 of the $200,000 piece at a price of 101. Romano's fixed income trader takes the position into inventory and then notifies it sales force, and RWM's financial advisors contact their clients to explain the offering and sell the bonds. Of course, those advisors know their clients and product suitability rules and after several hours it places all bonds to several different clients it knows would be interested in a bond of such quality and duration at a price of 102, for a markup of one point and a *gross* profit of $1,000 to the firm.

Shortly thereafter, a bond trader from another firm buys the remaining $100,000 piece from the original dealer. However, that trader buys the bonds at the original and still displayed offering price of 102. It then immediately sells the client bonds to Mrs. Smith, a customer of the firm at a price of 102.50, for a *gross* profit $500.

So which client is better off, the clients at Romano where the firm had a *gross* profit of $1,000 or Mrs. Jones, where her firm had *gross* profit of only $500? *Clearly, Romano's clients got better executions than Mrs. Jones even though Romano's client's paid more markup*. Why? Simply because Romano's clients paid 102 while Mrs. Jones paid 102.50. It is also important to note in this example that the length of time that transpired between customer and inter-dealer trade was irrelevant, as was the amount of the markup or *gross* profit. **This simple example shows that what is undeniably the most relevant factor is the end price to the client, as is currently reported on TRACE.**

Luckily, FINRA already has an effective method to do that in TRACE, where an investor can see the price at which bond trades were executed and compare them. However, the mere fact that investors do not look at TRACE does not mean that markup disclosure will give the public investor the necessary tools

and information they need to determine the quality of that execution. Nor does it mean that TRACE data should be abandoned in favor of "additional pricing disclosure" (read markup). As demonstrated, the only way to do so is to compare the price of their execution (which includes markup) on TRACE to the price of other timely executions (which also include markup) on TRACE. **Therefore, alternative methods for better public investor utilization of TRACE are the only answer and should be considered.**

The most obvious would be rather than to disclose only partially relevant (or totally irrelevant) markup information, would be to get better price disclosure. Clearly, price disclosure (not markups) is in the best interest of investors and we would wholeheartedly support this measure. Other comments have considered yield comparisons or "Accredited Benchmarking" to determine the "best available representation of current market price." (See DelphX comment letter, January 7 2015). Another thought is to reveal the end prices at which other trades have been executed. The problem is that while this would increase transparency, it would also be extremely costly, as this would effectively involve rebuilding a system of TRACE magnitude. Not only is the cost a concern, but questions remain in my mind as to just how better a mouse trap we would have built. For example, Bloomberg has a Fair Value estimate for many fixed income securities, but we have found this to be inconsistent with actual pricing in the market place.

It seems therefore that since price disclosure is clearly the best means for determining the quality of an execution and that information is already available in the market place through TRACE but investors aren't accessing it, then a disclosure on the confirmation outlining what TRACE is, and where to access it, and where to access instructions on how to use it would be simplest, most effective, and in order remedy. This would avoid many of the problems raised in this comment letter.

Finally and as an aside, let me address the Eder comment letter dated December 30, 2015. I disagree with his thesis that "[t]here should be full disclosure of the member firms' profit..." and "[the investing public] deserve to receive full disclosure of the member's price" as this is unprecedented. However, should this faulty and troubling proposal go into effect, and while I strongly hope it does not, I do agree that it is inconsistent to hinge this proposal on retail trades of $100,000 or less as he suggests and should affect trades of all sizes. To do otherwise would support age old conspiracies about FINRA serving large firms at the small firm's expense, and age old conspiracies about FINRA and other regulatory agencies desirous to stamp out the small firm. While I don't believe that to be the case, that narrative would only be supported by the $100,000 breakpoint, and would admittedly be suspect.

Many other comment letters have already addressed the anti-business, anti-capitalist, and anti-free market nature of this proposal. I have read in other comment letters and wholeheartedly agree, that by asking the grocer, car dealer, or gas station or any other industry other than the securities industry to reveal their gross profit is not only imponderable and wouldn't happen. What industry is next? This is deeply troubling.

Conclusion

FINRA Rule Proposal 14-52, *Pricing Disclosures in the Fixed Income Market*, is very troubling. It focuses on markup which is not the best method for determining the quality of an execution, and in many cases is irrelevant information that only obfuscates and confuses the client. In some case, it even unnecessarily alarms them. Rather, we have demonstrated that better price transparency is the most effective way for clients to measure the quality of their execution. **Rather than dismiss TRACE and abandon it since "retail clients do not typically consult" it as the proposal states and providing them with meaningless markup information that is not pertinent, the easiest solution is to use and improve price transparency through the existing TRACE system, and investor awareness of it, through well worded and visible disclosures on the confirmation.**

Sincerely,

Joseph R.V. Romano, CFP
President

Disclosure: Although I am the 2015 Chairperson of the Small Firm Advisory Board (SFAB), the views and opinions expressed herein are solely my own, and should not be construed as a formal statement from the SFAB or by corollary as the viewpoint of any other member of the board itself.