# SUTTER SECURITIES INCORPORATED

January 20, 2015

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

Re; Regulatory Notice 14-52 - Pricing Disclosure in the Fixed Income Markets

Dear Ms. Asquith:

FINRA has requested comment on a proposed rule requiring confirmation disclosure of pricing information in fixed income securities transactions. My comments would apply to most fixed-income securities but my emphasis is primarily on municipal securities.

In setting forth the "*Need for the Rule*", FINRA states that the new disclosure *"will provide customers with meaningful and useful information*". Further, FINRA states that *"this additional pricing information will better enable customers to evaluate the cost and quality of the services firms provide…."*

I do not agree with these statements for reasons set forth below.

The municipal market is a $3.8 trillion market and there are about 60,000 different municipal bond issuers. Although the overall municipal market is very liquid, most issues trade infrequently. Within a given rating and maturity, a municipal bond will trade based upon its yield to maturity ("YTM"). YTM is currently provided to all customers on their trade confirmation and is calculated after all costs, including mark-ups. Understanding a bond's structure, call features and risk often requires the broker to do far more "homework" than required in recommending an equity security.

In most cases when a retail customer purchases an equity security their objective is to eventually sell the security at a higher price. Clearly, knowing the commissions are an important factor in the "buy/sell" decision. In addition, it is relatively easy for a retail customer or a broker to get in-depth information on an equity security. (OTC-BB aside).

This is not the case with the overwhelming majority of municipal bonds.

When the retail customer purchases a municipal bond they are rarely buying with the intent of selling it at a higher price. Municipal bonds are bought with the intent of holding the bond until they are called or to maturity. In concluding that disclosing the "mark-up" or "mark-down" on a fixed-income trade would provide meaningful and useful information, FINRA is treating these costs in the same manner as the commissions charged on an equity trade.

A mark-up of $500 on the purchase of 50 bonds with three years to maturity has a higher cost to the customer than a mark-up of $500 on the purchase of 50 bonds with ten years to maturity! Merely highlighting the mark-up can be misleading.

Let's look at a two hypothetical examples:

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Example 1: Firm A buys 50 XYZ bonds from a dealer with a 3.0 % coupon and a maturity of 1-15-2018 (3 years) at a price of 100. The same day, Firm A sells the bonds to one customer at 101. The confirmation will show a yield to maturity of 2.64%. If the bonds were sold at 102, the yield to maturity would be 2.30%. The difference is 0.34%.

Example 2: Firm A buys 50 XYZ bonds from a dealer with a 3.0 % coupon and a maturity of 1-15-2025 (10 years) at a price of 100. The same day, Firm A sells the bonds to one customer at 101.The confirmation will show a yield to maturity of 2.88%. If the bonds were sold at 102, the yield to maturity would 2.77%. The difference is a relatively small, 0.11%.

As shown in this example, the true "cost to the customer" is not determined by the mark-up alone but by the impact of the yield to maturity calculation!

In addition to not providing truly useful information, I believe there may be significant unintended consequences from the current proposal. Whenever feasible, firms will establish "inventory accounts" so that they may hold bonds overnight. How has the retail customer benefited by having the broker wait one day before offering the bond to the customer?

In addition, there is now an incentive for the broker to concentrate a client's holdings by acquiring positions in excess of $100,000 at a time. Where a client may be better served by holding six $50,000 positions, they may be offered two $150,000 positions so as to avoid the additional disclosure.

Finally, the impact of this proposal will be most significant on the small firm. It is estimated that the number of small firms has decreased by more than 1000 in the past 5+ years. In part, this was caused by the dramatic drop in equity commissions. It is the rare broker that can make a living at $.01/share (or less). Hence the dramatic increase in the number of managed accounts where no one questions a one percent annual management fee. Today, by doing research and working closely with a retail client, a broker can still make a reasonable living with a municipal bond clientele. This can be accomplished with reasonable mark-ups, not exceeding three percent – and usually far lower. If there is a required disclosure of mark-ups, the most likely result will be significantly lower income to the broker-dealer and the broker. Many smaller firms are likely to merge or go out of business. More brokers will opt to become Registered Investment Advisors.

Is the public really better served by having fewer firms and brokers available to service the small retail account?

In spite of my compelling arguments against this proposal, I fear that this train has already left the station. Consequently, if disclosure is going to be required, I would suggest a modification to the current proposal. Namely, I would propose that disclosure be based upon a combination of the bond maturity and the mark-up. For example, disclosure might be required in the following cases:

1. Any mark up of 1.0% or more on a bond maturing in less than three years
2. Any mark up of 2.0% or more on a bond maturing in less than ten years
3. Any mark-up of 3.0% or more.

The specific numbers may be adjusted based upon trading and mark-up statistics available to FIRNA. Because many municipal bonds require significant analysis to understand their credit risk, likelihood of an early call and bond structure, there will be transactions where a higher mark-up is justified.

Sincerely,

Robert A. Muh
Chief Executive Officer