



| asset management group



Managed Funds  
Association



CENTER FOR CAPITAL MARKETS  
COMPETITIVENESS

September 23, 2021

The Honorable Gary Gensler  
Chair, U.S. Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090

**Re: Rule 15c2-11**

Dear Chair Gensler,

The Asset Management Group of the Securities Industry and Financial Markets Association (“SIFMA AMG”), the Investment Company Institute (“ICI”), the Investment Adviser Association (“IAA”), the Managed Funds Association (“MFA”), and the U.S. Chamber’s Center for Capital Markets Competitiveness (“CCMC”), together, “The Associations”<sup>1</sup> write to express our deep concern about the potential application of Rule 15c2-11 (the “Rule”) to the fixed income (“FI”) markets without appropriate notice and opportunity to comment, which would adversely affect the liquidity and transparency of these markets and unnecessarily harm investors in these markets. The Associations’ members include some of the largest and most active participants in the FI markets, including registered and private funds that invest in FI on behalf of retail and institutional investors and advisers that manage separately managed accounts (“SMAs”) on behalf of retail and institutional clients. We urge the Securities and Exchange Commission (“Commission”) not to apply the current Rule to these markets, which would threaten the continued expansion of liquidity and transparency in the FI markets and may increase transaction costs.

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<sup>1</sup> Please see the last page for information about the Associations.

## Introduction

As the Commission is aware, the Rule, which was implemented in 1971, amended in 1991, and amended again in 2020, is and always has been targeted at protecting retail investors from OTC equity market fraud.<sup>2</sup> The Rule prohibits dealers from publishing quotes on securities unless certain information review requirements are met, or certain exceptions are applicable. More specifically, these information review requirements are intended to prevent pump-and-dump and similar schemes that defraud retail investors.

While we support the goals of enhanced transparency in the FI markets, we believe the SEC should not apply the Rule to the FI markets without first adapting the Rule's requirements to the FI markets. Any revisions should be made through the rulemaking process, which would allow the SEC to conduct a cost-benefit analysis, provide an opportunity for public comment, and provide a more complete public policy analysis for the scope of and rationale for application of the Rule to the FI markets. Otherwise, any efforts to apply the existing regulatory framework to FI would risk market participants restricting their quoting activities and reducing liquidity and transparency, which would harm our members' ability to transact efficiently and manage risk for their clients. Further, the application of the Rule to FI markets would risk reversing decades of improvement in FI market transparency by reducing electronic trading volumes and the willingness of dealers to provide pricing information to investors.

If the SEC were to apply the current Rule to the FI markets, we believe that investors--including retail shareholders who invest in FI through registered funds--would be harmed. A rule otherwise intended to protect investors would do the opposite.

We discuss our views in more detail below.

### **The Rule's Focus is the Retail OTC Equity Markets, Which Operate Very Differently than the FI Markets**

We emphasize that the Rule has long been applied to protect retail investors from OTC equity market fraud. The previous Director of the Division of Enforcement noted in connection with the 2020 amendments to the Rule that "[t]he amended rule represents another important step in our tireless and proactive efforts to protect retail investors from being victimized by microcap fraud," and the same press release noted that a goal was "reducing fraud in these markets where retail presence is significant and, unfortunately, pump-and-dump and other frauds are too common."<sup>3</sup> (emphasis added)

The retail OTC equity market focus of the Rule is further evidenced by the construction of many important aspects of the Rule itself and the nature of the cost-benefit analysis performed when the rule has been amended, including most recently in 2020.<sup>4</sup> For example, the amendment to the Rule bases its analysis solely on

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<sup>2</sup> See *Publication or Submission of Quotations Without Specified Information*, SEC Rel. 34-87115 (Sept. 25, 2019) (2019 Proposal), available at <https://www.sec.gov/rules/proposed/2019/34-87115.pdf>; SEC Press Release, SEC Proposes Amendments to Enhance Retail Investor Protections (Sept. 26, 2019), available at <https://www.sec.gov/news/press-release/2019-189>; *Publication or Submission of Quotations Without Specified Information*, SEC Rel. 34-89891 (Sept. 16, 2020) (2020 Amendment), available at <https://www.sec.gov/rules/final/2020/33-10842.pdf>.

<sup>3</sup> See SEC Press Release, SEC Adopts Amendments to Enhance Retail Investor Protections and Modernize the Rule Governing Quotations for Over-the-Counter Securities (Sept. 16, 2020), available at <https://www.sec.gov/news/press-release/2020-212>.

<sup>4</sup> For example, the Rule's most important exemption is for exchange-traded securities; the exemptions such as that for ADTV assume the presence of a centralized tape; and the language of the Rule refers to tickers, but not CUSIPs.

OTC equity markets data.<sup>5</sup> Furthermore, FINRA’s rules related to Rule 15c2-11 apply only to OTC equity securities,<sup>6</sup> and the Commission recently approved amendments related to FINRA Form 211 that are consistent with the OTC equity market scope of FINRA’s rules.<sup>7</sup> We also understand that the Rule has never been applied to, or enforced in, the FI markets throughout its entire 50-year history.<sup>8</sup>

Importantly, we also note that the broad-based exemptions available under the Rule are tailored to the OTC equity market. The most important exemption for equity securities—listing on an exchange—is not available for FI securities. Other exemptions crafted to work for the equity markets similarly are not compatible with the FI markets (e.g., the ADTV exemption, or exemptions premised on a lack of gaps in quoting on a security, given that securities in the FI markets tend to trade far less frequently than equity securities).

The Commission stated in the 2020 Amendment that “[s]ecurities that trade on the OTC market are primarily owned by retail investors.”<sup>9</sup> (emphasis added) This may be true in the OTC equity markets, but is not accurate for the FI markets. Indeed, this statement is footnoted by the Commission to a paper on OTC equity markets.<sup>10</sup> Direct trading participants in the FI markets are overwhelmingly institutional investors that do not wholly depend on dealers as their source for information related to their investments.<sup>11</sup> Some FI markets are exclusively available to institutional or sophisticated investors, such as the Rule 144A securities markets that are limited to QIBs. Currently, FI trading primarily takes place on ATs, other electronic communications platforms (including through chat functions), and by voice methods, but extremely rarely on exchanges. In the FI markets, nearly every “market” made by a dealer is indicative. In other words, there is no guarantee that any specific size can be bought or sold at a specific price until the dealer decides to commit to trade that security. Further, the FI markets are vastly larger than equity markets—for example, FI CUSIPs number over 2.5 million,<sup>12</sup> whereas equity CUSIPs number in the tens of thousands (and the most actively traded equity securities are exempt from the

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<sup>5</sup> See 2020 Amendment at n.640 for reliance on equity market data: “The Commission uses three sources of data on OTC securities. OTC Markets Group’s ‘End-of-Day Pricing Service’ and ‘OTC Security Data File’ provide closing trade and quote data for the U.S. OTC equity market and include identifying information for securities and issuers, as well as securities’ piggyback eligibility. The Commission also uses information from the weekly OTC Markets Group’s ‘OTC Company Data File.’ Company Data Files include information about issuer reporting, shell, and bankruptcy status, as well as the SEC Central Index Key (CIK) identifier and whether an issuer’s financial statements are audited.” (emphasis added)

<sup>6</sup> FINRA Rule 6432 states that “[f]or purposes of [FINRA Rule 6432], the term ‘non-exchange-listed security’ means any equity security, other than a Restricted Equity Security, that is not traded on any national securities exchange.” FINRA Rule 6432, available at <https://www.finra.org/rules-guidance/rulebooks/finra-rules/6432>.

<sup>7</sup> See *Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Granting Approval of a Proposed Rule Change Relating to Members’ Filing Requirements Under FINRA Rule 6432 (Compliance With the Information Requirements of SEA Rule 15c2-11)*, Sec. Rel. No. 34-29-32 (Sept. 10, 2021), available at <https://www.sec.gov/rules/sro/finra/2021/34-92932.pdf>.

<sup>8</sup> We acknowledge that an exemption was added in 1975 for municipal securities, but reiterate our understanding that the Rule has never been applied to or enforced in the FI markets.

<sup>9</sup> See 2020 Amendment at 5.

<sup>10</sup> See 2020 Amendment at n.3, which cites to Andrew Ang et al., *Asset Pricing in the Dark: The Cross-Section of OTC Stocks*, 26 Rev. Fin. Stud. 2985–3028 (2013). This paper begins by stating that “[o]ver-the-counter (OTC) stocks are far less liquid, disclose less information, and exhibit lower institutional holdings than listed stocks. We exploit these different market conditions to test theories of cross-sectional return premiums.” The paper does not appear to discuss “bonds” or “fixed income.”

<sup>11</sup> Retail investors also do participate in the FI markets, but mostly through investment vehicles such as mutual funds and SMAs that are professionally managed by asset managers and other institutional investors.

<sup>12</sup> SIFMA analysis of Bloomberg data.

rule by virtue of their listing on an exchange).<sup>13</sup> Accordingly, the compliance burden would be exponentially greater when applied to FI securities as compared to OTC equity securities.

## **Imposing the Rule on the FI Markets Would Harm Investors**

We are deeply concerned about the disruptive impact and harm to the FI markets should the Commission attempt to apply the Rule, as written, to the FI markets. Specifically, we are deeply concerned about the risk of a potentially significant negative impact on our clients, investor protection, FI market liquidity, and further development and enhancement of electronic trading, which has greatly improved transparency and efficiency over the last decade or more. We are also concerned that it does not appear that the Commission, in its analysis of the costs and benefits of the most recent amendments to the Rule, has explicitly identified and addressed these or other potential costs to FI market participants and how the benefits of applying the Rule would outweigh these consequences. The Rule is not necessary for the FI markets, was not designed for the FI markets, and consequently the SEC should not apply the current Rule to them. Below we address some of our more specific concerns.

### **1. *There Has Been No Analysis of the Application of the Rule to FI Markets***

The Rule has been in place for 50 years. Since the Rule was first implemented and as it was subsequently amended, there has never been any analysis of the consequences of its potential application to the FI markets, including how the Rule would comport with FI market structure, impacts to market efficiency and end investors, cost of implementation, and views of market participants.

Furthermore, many basic definitional questions have not been considered, such as what it means to “publish” a quotation and what a “quotation medium” is in the context of FI market structure. Accordingly, it is not clear to which activities the Rule might apply. There are also many uncertainties about the nature and extent of the review required to be performed by a dealer to determine whether information about an issuer is “current and publicly available” under the Rule. Unlike the OTC equity market, there is no qualified interdealer quotation system in the FI market able to make publicly available determinations. There are no such interpretations, guidance, and quotation system because, in part, neither the SEC nor dealers have applied the Rule to the FI markets. Dealers may struggle to understand how they should apply the Rule as it is currently written to the FI markets, and thus are likely come to different conclusions regarding its implementation, thereby fragmenting the trading markets and introducing risk for no discernable benefit.

### **2. *Application of the Rule to FI Would Not Reduce Fraud or Improve Disclosure***

There is no record of the types of specified fraud that the Rule is designed to mitigate (*e.g.*, pump-and-dump schemes) in the FI markets, nor are we aware of enforcement by the Commission in this regard. If, for some reason, the Commission remains concerned about these types of risks in the FI markets, then addressing this issue warrants its own thoughtful analysis separate and apart from this Rule, and with the requisite opportunity for public notice and comment.

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<sup>13</sup> One company could be the issuer of a single equity CUSIP but hundreds of FI CUSIPs. Furthermore, a single FI transaction, such as a securitization, may involve the issuance of dozens of distinct securities.

Regarding issuer disclosure, institutional investors currently find that they have adequate information to transact in FI securities, even for non-public securities such as Rule 144A securities.<sup>14</sup> If the rule were to apply, the burden on dealers to obtain the required information, determine whether the body of information on each individual CUSIP is reliable, and whether it meets the “current and publicly available” standard under the Rule will be enormous and costly, and impossible in cases such as Rule 144A securities.<sup>15</sup> This could cause dealers to either cease providing quotes in certain FI securities at all or on a timely basis, reducing liquidity, or cause them to pass along such heightened costs to our clients. Further, pricing transparency is already quite high in the FI markets during normal market conditions, and application of the Rule will only serve to reduce that transparency if dealers retreat from providing quotes to asset managers and other investors.

### **3. *FI Market Liquidity May be Reduced***

If dealers are required to apply this Rule, as written, to the FI markets, then given this lack of experience and guidance, we expect dealers to take different views on where and how the Rule applies, leading to inconsistencies in trading activity, and ultimately, harm to overall market liquidity. Dealers unable to comply with the Rule as written may retreat from providing indications of interest that could be considered “quotations” under the Rule. These restrictions to quotation and trading practices could be broad-based across different types of FI instruments or could be concentrated in certain markets such as those for Rule 144A securities. These changes could happen in the near term or in the future depending on the interpretations taken by dealers or future guidance from the Commission, which would make the market less efficient. Additionally, we understand that dealers attempting to comply with this Rule will likely incur significant additional cost and may choose to incorporate such costs into the pricing of securities they trade with buy-side firms and ultimately their individual investor clients.

### **4. *Pricing Discovery and Transparency Could be Impaired***

If dealers choose to curtail their quoting activity due to the Rule, then pricing discovery and transparency could become significantly impaired as it is not practical to expect that FI securities could migrate to an exchange to permit use of the Rule’s “exchange” exemption. This could be an issue of particular importance for bonds that are not registered and do not have “publicly available” information, such as Rule 144A bonds. These bonds make up a significant proportion of the high-yield (“HY”) corporate bond market.<sup>16</sup> In this market, dealers send indicative pricing almost exclusively in communications that are not live to trade. However, it is not clear if dealers would be able to continue this practice in the HY market or any other FI market. If dealers cannot provide these indications, then a critical source of pricing information would be lost, which would severely reduce pricing discovery and efficiency and could lead to less accurate pricing. Reductions in transparency and liquidity lead to higher transaction costs that are ultimately borne by end investors.

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<sup>14</sup> Typical concerns about disclosure in the FI markets do not relate to the total unavailability of issuer information (which is what the Rule addresses), but rather the nature of the disclosure received (which the Rule does not address, but other existing securities laws do address). Despite Rule 144A securities being considered “private placements,” the provision of information to investors is required by the securities laws.

<sup>15</sup> Consequently, issuers may choose to shift their funding from securities to loans if liquidity or pricing deteriorates in their securities offerings, which would also harm investors by reducing the supply of securities in the market. However, this letter is focused on more direct impacts to investors.

<sup>16</sup> For example, Rule 144A bonds comprise two-thirds of the market value of the ML / ICE High Yield Index.

## **5. *Investor Risk Management May Be Impaired***

Given the massive number of FI CUSIPs, the relatively infrequent trading of many of them, and the lack of applicable exemptions, we are concerned that investors' risk management (including liquidity risk management) may be challenged if dealers reduce their quoting and/or trading activity. Especially in stressed markets, the dealers' ability to quickly accommodate client orders may be significantly reduced as dealers would have to locate and review documentation, as well as keep records of these actions to comply with the Rule. As we point out above, there is currently no infrastructure for compliance with the Rule, and in some cases, such as non-public Rule 144A bonds, compliance is not possible regardless of any infrastructure buildout.

## **6. *The Growth of Electronic Trading and Algorithmic Pricing Could be Reversed***

Electronic trading, which promotes greater transparency and price discovery among a broader range of market participants, has become an increasingly large proportion of trading volume in the FI markets.<sup>17</sup> This electronic trading activity may be reduced or even cease in some products if dealers are not permitted to put a bid or offer on a trading platform because of an inability to comply with the Rule. We believe this would reverse years of growth and enhanced transparency, and indeed, run counter to the Commission's efforts to improve FI market structure as shown through the extensive years-long efforts of the Fixed Income Market Structure Advisory Committee,<sup>18</sup> and in recent statements that you have given.<sup>19</sup>

Further, the application of the Rule could negatively impact a dealer's ability to generate algorithmic pricing, which the bond market is becoming more reliant upon for price formation. Algorithmic pricing relies on electronically generated prices as an input; therefore, depending on the interpretation of the Rule, dealers simply may not be able to make algorithmic pricing publicly available in instances where the requisite information is not publicly available, or the dealer is otherwise unable to verify the required information. Many bonds are priced algorithmically and traded based on trading activity in similar and comparable bonds. It is important to note that these algorithms are dependent on pricing data availability and transparency. Advances in technology have brought more clarity to these types of relationships and have led to improvements to pricing transparency. A step backward here would materially jeopardize the advancements made in the past several years to FI market price transparency generally.

## **7. *Investors' Best Execution and Valuation Determinations Will Become More Difficult***

If dealers reduce or eliminate their quotation activity in the FI markets, then it could become more challenging for certain market participants to fulfill some of their legal and contractual obligations and fiduciary duties, such as seeking and determining best execution. Investors use information from trading platforms, dealer runs, and other activity in their best execution determinations. However, it is

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<sup>17</sup> We estimate that approximately 40% of investment-grade corporate bonds are traded electronically, approximately 25% of HY are traded electronically, and 60% of Treasuries trade electronically. A significant proportion of agency MBS also trades electronically.

<sup>18</sup> See, e.g., SEC, Spotlight on Fixed Income Market Structure Advisory Committee (FIMSAC), <https://www.sec.gov/spotlight/fixed-income-advisory-committee>.

<sup>19</sup> See, e.g., SEC Chair Gary Gensler, Testimony Before the United States Senate Committee on Banking, Housing, and Urban Affairs (Sept. 14, 2021), available at <https://www.sec.gov/news/testimony/gensler-2021-09-14>.

not clear at this time whether and to what extent dealers will continue this activity, and the level of activity may vary by market and by dealer.

Valuation is another key function for institutional investors, including registered funds. Among other things, accurate valuation helps ensure fair and equitable treatment of investors (*e.g.*, open-end fund investors buy and sell fund shares daily), as well as accurate performance measurement, and fee calculations. Pricing services and institutional investors alike rely on dealer quotes to inform their valuation estimates and determinations. It is unclear how the Rule would impact dealer information provision at this time, but any reduction would harm FI investors. A reduction in this dealer activity—quoting activity, trading activity, or both—would reduce the overall quantity and quality of information that such entities incorporate, which would make valuation of FI securities more difficult and likely less precise. It would also be at odds with the Commission’s long-standing emphasis on valuation, articulated most recently in the 2020 adoption of Rule 2a-5 under the Investment Company Act.

Accordingly, investment advisers that manage registered funds that calculate net asset value (NAV) daily will need to consider if and how reductions in dealer activity would impact their valuation practices, policies, and procedures. For instance, registered open-end funds must calculate their NAVs daily, and doing so requires them to determine in good faith the fair values of their FI portfolio investments. These valuation practices currently contemplate—and are enriched by—multiple pricing inputs, including dealer quotes.

Open-end registered funds are also subject to liquidity requirements, such that a diminution in dealer quoting or overall trading activity could impact not only compliance with these liquidity requirements, but also portfolio construction if certain FI investments become less liquid. Specifically, reductions of quoting and/or trading activity may cause some instruments to become illiquid or be deemed illiquid that were not previously difficult to trade.

## **Conclusion**

As we have discussed above, the Rule was not designed to apply to the FI markets and, as it is currently written, should not be applied to the FI markets. It would not mitigate fraud or achieve other policy objectives, the costs and benefits of its application to the FI markets have not been analyzed, and it has not been enforced in the FI markets in the 50 years since it was implemented. More importantly, the risks of application are not abstract. The application of the Rule may drive market fragmentation, reduce electronic trading, and reduce price transparency and market efficiency, while increasing costs to retail and institutional investors alike. This harm would come from a Rule that is paradoxically intended to protect investors. The impacts of the imposition of the Rule, as written, go well beyond just the dealers subject to it.

However, if the Commission does decide that the Rule should be applied to the FI markets, then prior to any application or enforcement of the Rule, it is critical that the Commission conduct an analysis of whether there is a need for the Rule to apply to the FI markets, and if so, the attendant costs and benefits; provide an opportunity for public input through the notice and comment process; and revise the Rule in a manner that is consistent with the structure of the FI markets, with workable provisions and exceptions.

The Associations would welcome the opportunity to discuss the views expressed in this letter in more detail and engage with the Commission on important issues related to FI market structure. Please do not hesitate to contact any of the following staff at the Associations: Lindsey Keljo at SIFMA AMG ([lkkeljo@sifma.org](mailto:lkkeljo@sifma.org)), Susan

Olson at ICI ([solson@ici.org](mailto:solson@ici.org)), Monique Botkin at IAA ([monique.botkin@investmentadviser.org](mailto:monique.botkin@investmentadviser.org)), Jennifer Han at MFA ([jhan@managedfunds.org](mailto:jhan@managedfunds.org)), or Kristen Malinconico at CCMC ([kmalinconico@uschamber.com](mailto:kmalinconico@uschamber.com)).

Sincerely,

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CC:

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## Information about the Associations

**SIFMA AMG** brings the asset management community together to provide views on U.S. and global policy and to create industry best practices. SIFMA AMG's members represent U.S. and global asset management firms whose combined assets under management exceed \$45 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds. For more information, visit <http://www.sifma.org/amg>.

The **Investment Company Institute (ICI)** is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US\$31.8 trillion in the United States, serving more than 100 million US shareholders, and US\$10.2 trillion in assets in other jurisdictions. ICI carries out its international work through [ICI Global](#), with offices in Washington, DC, London, Brussels, and Hong Kong.

The **IAA** is the leading organization dedicated to advancing the interests of investment advisers. For more than 80 years, the IAA has been advocating for advisers before Congress and U.S. and global regulators, promoting best practices and providing education and resources to empower advisers to effectively serve their clients, the capital markets, and the U.S. economy. The IAA's member firms manage more than \$25 trillion in assets for a wide variety of individual and institutional clients, including pension plans, trusts, mutual funds, private funds, endowments, foundations, and corporations. For more information, please visit [www.investmentadviser.org](http://www.investmentadviser.org).

**MFA** represents the global alternative investment industry and its investors by advocating for regulatory, tax, and other public policies that foster efficient, transparent, and fair capital markets. MFA's more than 140 member firms collectively manage nearly \$1.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, London, Brussels, and Asia.

The **U.S. Chamber's Center for Capital Markets Competitiveness's (CCMC)** mission is to advance America's global leadership in capital formation by supporting diverse capital markets that are the most fair, transparent, efficient, and innovative in the world. CCMC advocates on behalf of American businesses to ensure that legislation and regulation strengthen our capital markets allowing businesses—from the local flower shop to a multinational manufacturer—to mitigate risks, manage liquidity, access credit, and raise capital.