bondwave
Imagine that

June 11, 2019

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

Re: FINRA Regulatory Notice 19-12 – FINRA Requests Comment on a Proposed Pilot Program to Study Recommended Changes to Corporate Bond Block Trade Dissemination

Dear Ms. Asquith:

BondWave LLC, a provider of financial technology solutions for the fixed income market, appreciates the opportunity to respond to FINRA's request for comment on a proposed pilot program to study recommended changes to corporate bond block trade dissemination.

Impact of Proposal on Mark-Up Disclosure

BondWave is one of only four commercial providers of Prevailing Market Price (PMP) calculations for satisfying FINRA's Mark-Up Disclosure Rule (FINRA Rule 2232). As such we rely heavily on reported trade sizes and prices to perform accurate and precise calculations so that our broker/dealer clients can accurately and precisely report to their retail investors the difference between the Prevailing Market Price for a bond and the retail investor's trade price, where required. To perform this calculation, we are required by the rule to follow a waterfall calculation method. A waterfall calculation method implies that information higher in the waterfall is of greater value than information lower in the waterfall.

The proposal would remove certain reported trades from each of the first seven levels of the waterfall calculation. The proposal also has the potential to affect the eighth, and final, level of the waterfall (economic model) for any economic model based on an evaluated price, as evaluated prices typically prioritize large trades in their calculations. Under this proposal mark-up disclosure calculations for the subject

CUSIP and related CUSIPS will become less precise and less accurate whenever a large block trade dissemination is delayed.

BondWave would also like to point out the proposal appears to be in direct conflict with both the purpose and the spirit of the Mark-Up Disclosure Rule. When proposing the change to FINRA Rule 2232 in SR-2016-032 FINRA states:

> "FINRA believes that requiring disclosure for retail customers, i.e., accounts that are not institutional accounts, is appropriate because retail customers typically have less ready access to market and pricing information than institutional customers."

The proposal would make pricing information even less readily available.

Importance of Large Block Trade Prices

One of the subtexts of the mark-up disclosure rule is that not all fixed income prices are alike. The presence of a waterfall means that there is a rank applied to the data. Some prices rank higher than others when determining the PMP of a bond. The largest trades typically involve the most informed counterparties and are, therefore, most likely to be the most accurate reflection of a bond's true value. By removing both dealer to dealer trades and dealer to institutional customer trades that are very large, FINRA would be removing the most informed opinion about a bond's market value.

BondWave measures bid/ask spreads for fixed income trades based on reported trades. Examining bid/ask spreads on dealer to dealer trades shows there is a correlation between trade size and spread width. Tighter bid/ask spreads are associated with more efficient pricing.

Corporate Bond Dealer to Dealer Average Bid/Ask Spread

June 11, 2018 through June 10, 2019

Trade Size	Bid/Ask Spread
100,000 or less	0.34%
100,000 to 1,000,000	0.23%
1,000,000 or more	0.13%

Source: BondWave QTrades database.

Notes: Trade size categories apply to both sides of a spread calculation. QTrades Corporate Bid/Ask Spread Index covers registered corporate bonds with ratings between A+ and BBB- (representing 68.6% of trading volume).

There is also a correlation between trade size and the amount of mark-up or mark-down paid for the trade:

Corporate Bond Average Mark-Down and Mark-Up

June 11, 2018 through June 10, 2019

Rating	Mark-Down ≥ 5,000,000	Mark-Down < 5,000,000
AAA	0.07%	0.14%
AA+	0.06%	0.11%
AA	0.05%	0.15%
AA-	0.05%	0.12%
A+	0.05%	0.14%
A	0.05%	0.15%
A-	0.05%	0.12%
BBB+	0.05%	0.18%
BBB	0.08%	0.18%
BBB-	0.06%	0.23%

Source: BondWave QTrades database.

Rating	Mark-Up ≥ 5,000,000	Mark-Up < 5,000,000
AAA	0.12%	0.31%
AA+	0.17%	0.25%
AA	0.12%	0.19%
AA-	0.15%	0.18%
A+	0.14%	0.21%
A	0.12%	0.27%
A-	0.10%	0.24%
BBB+	0.13%	0.35%
BBB	0.17%	0.40%
BBB-	0.14%	0.51%

Source: BondWave QTrades database.

Rating	Mark-Down ≥ 1,000,000	Mark-Down < 1,000,000
B	0.12%	0.29%
B-	0.14%	0.29%
B+	0.11%	0.27%
BB	0.13%	0.27%
BB-	0.09%	0.26%
BB+	0.10%	0.26%
C	0.12%	0.55%
CC	0.28%	0.40%
CCC	0.18%	0.34%
CCC-	0.24%	0.39%
CCC+	0.15%	0.36%
D	0.49%	0.58%

Source: BondWave QTrades database.

Rating	Mark-Up ≥ 1,000,000	Mark-Up < 1,000,000
B	0.22%	0.44%
B-	0.20%	0.46%
B+	0.19%	0.43%
BB	0.21%	0.56%
BB-	0.16%	0.48%
BB+	0.16%	0.56%
C	0.43%	0.56%
CC	0.26%	0.33%
CCC	0.25%	0.34%
CCC-	0.21%	0.36%
CCC+	0.23%	0.37%
D	0.35%	0.46%

Source: BondWave QTrades database.

The data supports the view that large trades offer the most efficient representations of the market value of a bond because they have the tightest bid/ask spread at the dealer to dealer level and the smallest mark-up at the dealer to customer level.

Questions for Prevailing Market Price Calculations

The proposal does not address how it will interact with existing rules. If the proposal is adopted FINRA will need to answer a number of questions for how prevailing market price calculations will be performed. Below is a non-comprehensive list of such questions:

1. Will delayed block trade dissemination also impact the mark-up disclosure obligation? In other words, will a broker no longer be obliged to disclose their mark-up to retail investors when dissemination of their principal trade is delayed?
2. If a broker does a block trade that is subject to delayed dissemination and leads to a mark-up disclosure requirement, will they delay mark-up disclosure by two days?
    a. If no, will the delayed dissemination trade be used in the calculation of PMP?
        i. If yes, how will the retail investor know what was used to calculate PMP between the time of receipt of the confirm and expiration of the dissemination delay given that the required URL will presumably not display the information used in calculating the prevailing market price?
        ii. If no, will the broker proceed down the waterfall to calculate PMP?
            1. In this case, will the broker need to issue a new trade confirmation after the expiration of the dissemination delay using the previous delayed dissemination block trade to calculate the Prevailing Market Price?
3. If a broker has issued a trade confirmation with a mark-up based on a Prevailing Market Price that later changes by the expiration of a dissemination delay on a trade that was not their own, do they need to issue a new confirm with a new mark-up based on a new Prevailing Market Price reflecting the newly disseminated trade?
    a. If no, will the broker be required to change the description of the mark-up calculation placed on retail client confirms to specify that the value can change based on when the retail investor accesses the attached URL?

Summary

BondWave is concerned that delayed dissemination of block trades will remove the most valuable information for calculating the Prevailing Market Price. BondWave is also concerned that disseminating trade information with variable timing can lead to retail investor confusion. BondWave recommends that FINRA addresses the impact the proposal would have on its existing rules prior to implementing the proposal.

Sincerely,

Paul Daley
Managing Director, Head of Fixed Income Lab