



P.O. Box 2600
Valley Forge, PA 19482-2600

February 19, 2013

Submitted electronically

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Notice 2012-63: Request for Comment on MSRB Rules and Interpretive Guidance

Dear Mr. Smith:

Vanguard¹ appreciates the opportunity to respond to the request of the Municipal Securities Rulemaking Board (“MSRB”) for comments on MSRB rules and interpretive guidance.² We commend the MSRB for seeking comments to determine whether any of its rules or guidance should be revised or restated and for considering evolving market conditions in its rulemaking. On behalf of our clients, who currently invest approximately \$44 billion in Vanguard funds through Section 529 college savings plans (“529 Plans” or the “Plans”), we are pleased to provide our views.

As the primary distributor of certain 529 Plans, Vanguard is subject to regulation by the MSRB. Vanguard believes that the MSRB can take steps to enhance the efficiency and clarity of its rulemaking and rule interpretations in cases where the MSRB intends such rules or interpretations to apply to the primary distributors of 529 Plans. Unlike other municipal securities offerings, 529 Plans do not have “underwriters” as that term is commonly understood in the context of municipal bond offerings. As referenced below, the term “primary distributor”³ is frequently used in place of “underwriter” for 529 Plan offerings. This term is used to reflect that, unlike traditional bond offerings, 529 Plans do not have “new issues” and are continuously offered in a manner similar to mutual funds.⁴

¹ The Vanguard Group, Inc. (“Vanguard”) manages approximately \$44 billion in 529 plan assets invested in 28 college savings plans and five prepaid tuition plans in 30 states. Vanguard Marketing Corporation, a Vanguard subsidiary, is a registered broker-dealer and municipal securities dealer that serves as the primary distributor for five states’ direct-sold 529 plans. Vanguard manages \$2 trillion in U.S. mutual fund assets, including \$245 billion in ETF assets. The firm offers more than 170 funds to U.S. investors and more than 70 additional funds to non-U.S. markets.

² See Request for Comment on MSRB Rules and Interpretive Guidance (MSRB Notice 2012-63), dated December 18, 2012.

³ The MSRB has, itself, used the term “primary distributor” recently. See Request for Comment on Draft Proposal to Collect 529 College Savings Plan Data (MSRB Notice 2012-40), dated August 6, 2012, and Second Request for Comment on Draft Rule Requiring Underwriters to Submit 529 College Savings Plan Information to the MSRB (MSRB Notice 2012-59), dated November 23, 2012.

⁴ See MSRB Interpretation Relating to Sales of Municipal Fund Securities in the Primary Market (January 18, 2001). In this interpretive notice, the MSRB recognized this and several other important differences between primary distributors of 529 Plans and municipal bond underwriters.

We are concerned that the MSRB has not been clear about when it intends its rule interpretations to apply to primary distributors of 529 Plans. For instance, in the MSRB's recent interpretive notice on Rule G-17 relating to duties of underwriters (the "Notice")⁵, the MSRB stated that the Notice, "does not apply to selling group members and, unless otherwise specified, applies only to negotiated underwritings and not to competitive underwritings."⁶ Based on an analysis of these terms, the Notice would not seemingly apply to primary distributors of 529 Plans. While not composed of "official" definitions, the MSRB's glossary (the "Glossary"), defines "Underwriter" to mean "a broker-dealer that purchases a new issue of municipal securities from the issuer for resale in a primary offering." The Glossary does not contain a specific definition of "negotiated underwriting" but defines "Negotiated Sale" to mean, "the sale of a new issue of municipal securities by an issuer directly to an underwriter or underwriting syndicate selected by the issuer.... The sale of a new issue of securities in this manner is also known as a negotiated underwriting." Unlike municipal bond underwriters, primary distributors of 529 Plans do not purchase the issue directly from the issuer (*i.e.*, in a typical 529 Plan offering, a state trust). Given this distinction, the Notice did not appear to apply to primary distributors of 529 Plans. It became clear that the MSRB intended the Notice to apply to primary distributors of 529 Plans only after the MSRB provided informal guidance on this point.

More importantly, we are concerned that the MSRB has not appropriately considered the role of primary distributors in its rulemaking process. For example, the MSRB recently sought comment on a concept release (the "Release") on the disclosure of financial incentives paid or received by dealers and municipal advisors that represent potential conflicts of interest.⁷ Specifically, the Release suggested that underwriters could be required to disclose: (i) financial incentives received by the underwriter from any third party for recommending a municipal securities financing; (ii) financial incentives received by the underwriter from any third party payor in connection with a new issue transaction; and (iii) any financial incentives paid by the underwriter to any third party recipient in connection with a new issue transaction, including those paid for the purpose of obtaining or retaining any such new issue transaction. As noted in the Investment Company Institute's ("ICI") letter responding to the Release (the "ICI Letter")⁸: (i) there is no "financing" that is recommended to an issuer of 529 Plans; (ii) 529 Plans are not subject to issuer default or dependent on external or third-party sources of revenue to pay investors; and (iii) existing 529 Plan disclosures currently provide investors material information regarding the Plan, including Plan fees and expenses. As with the Notice, the MSRB informally advised that it intended for the Release to apply to primary distributors of 529 Plans. However, the potential conflicts of interest of apparent concern to the MSRB in the Release do not seem to be present with 529 Plans. Instead, the Release appears to focus on issues relating to potential conflicts that underwriters may have relating to municipal bond offerings.

These examples support that the MSRB should take greater care in determining what regulatory requirements are needed and appropriate for the activities of primary distributors of 529 Plans. Beyond clarifying the applicability of future rulemaking and interpretations, we urge the MSRB to thoughtfully consider whether future proposals and interpretations should be applicable to primary distributors. As illustrated in the second example above, concerns relating to primary distributors of 529 Plans are materially different from those of underwriters of municipal bonds.

⁵ See Securities and Exchange Commission Approves Interpretive Notice on the Duties of Underwriters to State and Local Government Issues (MSRB Notice 2012-25), dated May 7, 2012.

⁶ *Id.* at pg. 1.

⁷ See Request for Comment on Concept Proposal to Provide for Public Disclosure of Financial Incentives Paid or Received by Dealers and Municipal Advisors Representing Potential Conflicts of Interest (MSRB Notice 2012-28), dated May 31, 2012.

⁸ See Letter from Tamara K. Salmon, Senior Associate Counsel, ICI to Ronald W. Smith, Corporate Secretary, MSRB, dated July 30, 2012 (responding to MSRB Notice 2012-28).

Accordingly, we agree with the ICI's suggestion in its current letter that the MSRB develop a definition of "primary distributor" and refer to such a definition when determining whether to include primary distributors in future proposals and interpretations. We believe that such a definition, if adopted, would assist the MSRB in achieving more efficient and effective regulation of primary distributors of 529 Plans, while still protecting investors.

* * * * *

We appreciate the opportunity to provide the MSRB with our comments on the MSRB's rules and guidance. If you have any questions about our comments or would like any additional information, please contact me at (610)-669-6741 or Lance Barrett at (610) 669-2616.

Sincerely,

/s/ John C. Heywood

Principal, Retail Investor Group
Vanguard