

March 31, 2016

Submitted Electronically

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

RE: **MSRB Regulatory Notice 2016-07: Request for Comment on Proposed Amendments to MSRB Rule G-30 (Prices and Commissions)**

Dear Mr. Smith:

On behalf of the Bond Dealers of America (“BDA”), I am pleased to submit this letter in response to Municipal Securities Rulemaking Board Regulatory Notice 2016-07 (the “Notice”), requesting comment on proposed amendments to provide guidance on establishing the prevailing market price related to the calculation of markups and markdowns for principal transactions in municipal securities. BDA is the only Washington D.C. based group representing middle-market securities dealers and banks focused on the U.S. fixed-income markets and we welcome this opportunity to present our comments on the Notice.

BDA appreciates the fact that MSRB has provided this guidance in response to industry comments to Regulatory Notice 2015-16 (Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers). As BDA stated in its comment letter on that proposal, the retail confirmation rule will not function without clear guidance for establishing inter-dealer cost. The notion of putting a subjective estimate of inter-dealer cost on a customer confirm is a very serious concern for dealers. BDA does not believe the guidance, as drafted, provides a guide for dealers to reliably and continuously ascertain inter-dealer cost with enough certainty to incorporate that information on a customer confirmation. Therefore, BDA urges MSRB to re-propose this guidance after assessing industry comment letters because BDA believes this proposed guidance, as currently written, would cause a significant market disruption related to the retail confirmation rule. To minimize market disruption and confusion, it is absolutely essential that workable contemporaneous cost guidance be established before any retail confirmation rule is finalized.

The BDA does not believe FINRA 2121 is the proper basis for an MSRB rule that will apply to the municipal securities marketplace.

The municipal securities marketplace is vastly different than the marketplace for corporate and Agency securities. Therefore, certain rules and guidance, such as FINRA Rule 2121, which provides guidance for establishing contemporaneous cost in the corporate and Agency marketplace, do not provide the proper basis for a comparable MSRB rule for the municipal securities marketplace. BDA appreciates FINRA and the MSRB’s efforts to

harmonize rules generally. However, harmonizing this proposed guidance with FINRA Rule 2121 will not work in practice and may, in fact, create more confusion for dealers and investors. This is because the hierarchical step-by-step “waterfall” scenario, which may work for corporate and Agency securities, is not the most practical approach for establishing contemporaneous cost in the municipal securities marketplace. Furthermore, requiring dealers to draft policies and procedures based on a corporate-bond market model will be extremely burdensome from a compliance standpoint because the proposed guidance is not based on the trading and market dynamics that exist in the municipal securities marketplace.

In the non-municipal marketplace, securities trade with greater frequency. This reality allows for a more standardized uniform procedure as envisioned by the waterfall scenario. For example, identifying contemporaneous cost for a frequently traded corporate bond that is actively trading in the secondary market is a relatively easy task. By contrast, the municipal market contains a significantly greater number of unique bond issues that trade far less frequently. Therefore, it is likely that the proposed guidance, which is based on a corporate-bond model, would be more valuable pricing guidance if it were amended to reflect how municipal bonds trade.

BDA recommends allowing dealers to use one or more of the concepts outlined in the waterfall to identify contemporaneous cost as opposed to requiring rote step-by-step, robotic policies and procedures based on the corporate market waterfall. This would allow for greater flexibility in a market where bonds trade less frequently. For example, if a particular municipal security has not traded in several days and a dealer is offering bonds for sale out of inventory at a price which is based on a spread to a municipal market index, the dealer should not be required to document that it has gone through the unnecessary and cumbersome step-by-step process for establishing that no contemporaneous trades have occurred in the same security when no trades have been reported to EMMA.

This is especially true because, for retail trades, G-18 already requires order-handling procedures to ensure ‘best execution’. Our recommendation to permit a spread-based pricing approach, or another reasonable pricing approach, would not relieve the dealer from having a full understanding of the marketplace, including the markets where municipal securities are trading. However, it would allow a dealer to form a reasonable basis for estimating its contemporaneous cost at a given point in time without having to go through the process of documenting each step in the waterfall, many of which are not always applicable for the municipal market.

BDA believes that the contemporaneous cost guidance would cause major confusion amongst dealers as it relates to compliance with the proposed retail confirmation disclosure rules.

As BDA stated in its December 11, 2015 response to Regulatory Notice 2015-16 (Draft Rule Amendments to Require Confirmation Disclosure of Mark-ups for Specified Principal Transactions with Retail Customers), the biggest uncertainty created by the MSRB’s methodology is the ability to reliably and consistently ascertain inter-dealer cost to compute the prevailing market price for purposes of including that information on a retail-customer confirmation. Having clear guidance on establishing the prevailing market price is absolutely essential for the retail confirmation proposal to become operational and the BDA appreciates that

the MSRB has published this proposed guidance. Unfortunately, the guidance proposed in this Notice is based upon a model of pricing that would not be workable for the municipal securities market.

Requiring a complex, process-specific method to determine prevailing market price is not the optimal method given that there is still no general consensus within the industry or amongst regulators on the single best method for pricing a municipal security. Although BDA continues to believe that providing additional pricing disclosure to retail investors could potentially be beneficial to the marketplace, the MSRB must weigh the substantial costs of compliance and technological infrastructure necessary to implement the proposed guidance and related proposed rules. Furthermore, as the implementation of a retail confirmation disclosure rule is finalized by the MSRB, such a rule should not go into effect before reliable prevailing market price guidance is finalized in a format that is appropriately tailored to the municipal securities marketplace.

BDA does not believe that estimating the cost of compliance for the G-30 Guidance is possible at this point

The BDA represents small-to-medium sized middle market securities dealers and banks. These firms have been disproportionately burdened by the significant increase in regulatory costs over the past several years. This rule represents another significant requirement that will add to compliance personnel, technology, and third-party vendor cost burdens. Consolidation of the municipal securities industry, which is already occurring because of the vast increase in regulatory costs, would have a negative impact on competition, retail investors, and the availability of reasonably priced services in regional securities issues to participants in regional markets.

If this proposed guidance is designed to require dealers to maintain evidence for each trade that would be sufficient to overcome the price established by reference to contemporaneous cost, this would add tremendous new compliance and technology costs. To comply with this requirement, dealers would be required to document the specific considerations that led to a prevailing market price judgment, resulting, perhaps in an inefficient marketplace where no trader wants to be the high or low price to the tape, and which may result in an artificial impact to pricing.

BDA urges MSRB to leverage the pricing data held in EMMA to achieve greater transparency for retail investors.

As stated above, we ask that workable contemporaneous cost guidance be established before any retail confirmation rule is finalized. With that said, we also reiterate our recommendation from our previous comment letter on the retail confirmation disclosure rule proposal, that regulators leverage the transaction data that EMMA and TRACE already hold, to provide the type disclosure the retail confirm proposals are designed to create. This result would deliver the desired additional disclosure to retail customers at a much lower cost to broker-dealers while providing greater clarity and consistency for the retail investor. It would also allow customers to better understand dealer compensation and would provide sufficient information for a customer to contact their dealer to discuss the execution of their trades.

SMMPs should be exempt from Rule G-30

BDA recommends that Rule G-30 be revised to explicitly exempt SMMPs from the fair pricing requirement. The voluminous body of pricing information that now exists should make it clear that SMMPs no longer have to rely on executing dealers to determine if their transactions are being priced fairly. If, as the MSRB has determined, SMMPs may elect to opt out of the protections provided to market participants by MSRB Rule G-18 relating to best execution, it follows that they should also be exempt from Rule G-30 fair pricing protection because the two are so closely related.

Conclusion

The proposed amendments to MSRB Rule G-30 to establish a process to identify a prevailing market price are not appropriately tailored to the municipal securities market. The proposed guidance is entirely too prescriptive and does not take account of the legitimate different methods that various dealers use to establish prevailing market price. Furthermore, the proposed guidance represents an unknowable compliance and technology burden that will fall disproportionately on middle-market dealers.

Thank you for the opportunity to submit these comments.

Sincerely,



Michael Nicholas
Chief Executive Officer