

January 11, 2021

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1300 I St NW
Washington DC 20005

Dear Mr. Smith

The Bond Dealers of America is pleased to comment on MSRB Notice 2020-19, “MSRB Requests Input on Strategic Goals and Priorities” (the “Notice”). BDA is the only DC-based organization exclusively representing the interests of securities dealers and banks focused on the US bond markets.

We see long-term strategic planning as an important part of the MSRB’s process for determining an agenda and priorities for future action. It has been more than four years since the MSRB last sought public input on strategic goals and priorities, and it is appropriate for the Board to undertake that initiative now. BDA is pleased to participate. Here we outline our responses to the questions posed in the Notice and provide our views on where the MSRB should focus its resources in the coming years.

Key trends in coming years

The municipal securities market is ever evolving. Several trends have emerged in recent years that we believe will continue over the near to medium term.

Private placements—Between 2011 and 2017, annual issuance of municipal securities by private placement went from \$9.6 billion comprising around three percent of long-term issuance to \$40.2 billion comprising nine percent of issuance.¹ While issuance by private placement has waned a bit since 2017, it remains a more important tool for issuers than ever. A large portion of private placement buyers continue to be commercial banks. Over the 12-month period from October 2019 through September 2020, US banks increased their holdings of municipal loans and securities by \$34 billion, an increase of more than seven percent.² We believe this trend will continue in the coming years.

The SEC has responded to the rise in private placements by floating a proposed Exemptive Order which would excuse nearly any Municipal Advisors who solicit private placement investors on behalf of municipal issuers from registering as broker-dealers.³ While that proposal has not been acted on since it was released, the SEC in June 2020 published a Temporary Conditional Exemption on the same issue which, until it expired at the end of December, applied to bank placements of \$20 million or less.⁴ Both

¹ *The Bond Buyer*, “A Decade of Municipal Bond Finance,” www.bondbuyer.com/broker/bond-buyer-data.

² Board of Governors of the Federal Reserve System, “Financial Accounts of the United States,” December 10, 2020, page 121.

³ Notice of Proposed Exemptive Order Granting a Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Registered Municipal Advisors, 84 Fed. Reg. 54062 (October 9, 2019).

⁴ Order Granting a Temporary Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Registered Municipal Advisors, 85 Fed. Reg. 37133 (June 19, 2020).

these actions represent a dangerous departure from decades of rulemaking focused on investor protection.

Retail order periods—MSRB Rule G-11 requires underwriters to comply with issuers’ standards and definitions during retail order periods (ROPs). Issuers define the scope and composition of ROPs, and definitions of retail order vary widely by issuer. ROP definitions often cover natural persons, but beyond that, there is wide disparity in specifying which customers qualify as retail. ROPs sometimes include separately managed accounts and even mutual funds, but sometimes not. Some issuers define retail by the size of the order, while others define it based on the type of customer. The length of ROPs and which maturities are offered during a ROP can also vary.

This wide disparity among ROP standards and the strict rules the MSRB has in place to govern ROPs can result in a higher degree of noncompliance than expected or desired. The variety of ROP standards also contributes to the issue of “flipping” and calls the question of whether retail order periods are as beneficial to issuers as their popularity implies. We recommend that the MSRB explore the issue of ROPs with an eye towards encouraging a greater degree of uniformity in ROP specifications. We would welcome the opportunity to work with you and other stakeholders to address this issue.

Low yield environment—The municipal market is currently experiencing extremely low yields by historical standards. As of the end of 2020, the Bloomberg BVAL 10-year AAA yield stood at 69 basis points,⁵ nearly the lowest level in our lifetimes. While this provides tremendous opportunities for issuers, it creates risks for investors. It is virtually inevitable that yields will begin to rise again in the future. That means the market value of outstanding fixed-rate bonds will fall. While this risk is generally well understood by municipal securities investors, there is a complication unique to the municipal market that may not be well known.

Internal Revenue Code Section 1278⁶ specifies the tax treatment of bonds sold at a market discount. Market discount occurs when an investor acquires a bond on the secondary market at a price below par. (The definition is more complex for bonds that were initially sold with original issue discount.) The difference between a taxpayer’s acquisition price of the bond and par represents the amount of market discount subject to the treatment specified in Section 1278. If the amount of market discount is *de minimis*—defined in the context of dollar price as less than 0.25 point times the number of whole years left to maturity—the discount is taxed as a capital gain in the year the bond is sold or redeemed. If the amount of market discount at acquisition exceeds the *de minimis* amount, the discount is taxed as ordinary income when the bond is sold or redeemed. (Taxpayers also have the option to accrete market discount over the remaining life of the bond and pay the tax annually on the accreted amount.)

It is likely that as municipal yields eventually begin to rise, prices of some bonds issued in the current low-rate environment will fall below par. That could expose some investors who acquire bonds in the secondary market to earning ordinary, taxable income on their otherwise tax-exempt investment. It is an issue worthy of attention, and we would welcome the opportunity to work with the MSRB and other stakeholders to ensure that the possible effects of Section 1278 are known to investors.

⁵ Municipal Securities Rulemaking Board, “Yield Curves and Indices--BVAL® AAA Municipal Curves,” <https://emma.msrb.org/ToolsAndResources/BloombergYieldCurve?daily=False>.

⁶ 26 U.S.C. § 1278

Remote work—The pandemic has significantly altered the way we all do business. More employees of municipal dealers are working from remote locations, and in-person contact with clients and customers has been curtailed. This has created challenges related to communications, data access and security, and other vital functions. We appreciate the MSRB’s response to the crisis. We believe remote work will continue to be a relevant issue for many months, perhaps longer, and we encourage the MSRB to continue to explore ways to support this trend and to coordinate any new rules or amendments with FINRA.

MSRB’s performance

The entire market agrees that the EMMA platform provides tremendous benefits. It is an invaluable resource, and the MSRB does a good job of maintaining and enhancing the system. We also commend the MSRB for your response to the pandemic and the compliance guidance you have provided. The Board has shown sensitivity to the needs of regulated entities during this extraordinary time without threatening the safety and reliability of the market.

There are some areas of the MSRB’s jurisdiction and activities that we believe deserve greater attention.

MSRB finances—There are two points of discussion with respect to finances.

Relative contributions of dealers and MAs: The Dodd-Frank Act, which for the first time brought non-dealer MAs under the MSRB’s regulatory umbrella, was enacted more than ten years ago. Yet the relative financial contributions of dealers and MAs to the MSRB’s revenue remain lopsided. In fiscal 2019, the MSRB collected \$27.6 million from regulated entities—dealers and MAs—in the form of underwriting assessments, transaction fees, technology fees, and Municipal Advisor professional fees.⁷ Dealers paid \$26 million, or 94 percent of the total. And this was in a year when the MSRB temporarily reduced underwriting and transaction assessments for dealers.⁸ Without the temporary fee reductions dealers would have made an even larger contribution.

Volatility in revenues: For fiscal 2020 the MSRB budgeted a \$2.3 million operating deficit.⁹ Instead, the MSRB generated a surplus of approximately \$6 million,¹⁰ or \$8.3 million over budgeted revenue. That means the MSRB’s liquid assets have grown from \$62.4 million at the end of FY 2019¹¹ to approximately \$71 million at the end of FY 2020. The MSRB’s published policy on funding reserves is not specific, so there is no way for stakeholders to know precisely what is the MSRB’s targeted reserve level. But for an

⁷ For the purpose of this calculation, we have disregarded Annual and initial fees because in its financial reporting, the MSRB does not break down the portions of these fees paid by dealers and MAs. The fees cited above represent more than 90 percent of the fees and assessments paid by regulated entities.

⁸ Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend MSRB Rule A–13 to Temporarily Reduce the Rate of Assessment for the MSRB’s Underwriting, Transaction and Technology Fees on Brokers, Dealers and Municipal Securities Dealers, 84 Fed. Reg. 60 (March 28, 2019).

⁹ Municipal Securities Rulemaking Board, “Fiscal Year 2021 Budget for the Fiscal Year Beginning October 1, 2020,” page 4.

¹⁰ Sarah Wynn, “MSRB expects a surplus of up to \$6 million for fiscal 2020,” *The Bond Buyer*, October 27, 2020, www.bondbuyer.com/news/msrb-expects-a-surplus-of-up-to-6-million-for-fiscal-2020.

¹¹ Municipal Securities Rulemaking Board, “Annual Report 2019,” page 16. Includes Cash and cash equivalents and Investments.

organization with \$42 million in operating expenses in FY 2019, \$71 million in idle liquid assets—industry money collected and held by the MSRB—is too much.

The Board has sought to address these issues for at least the last seven years:

- After its February 2014 meeting, the Board stated it “has been working to establish appropriate and equitable assessments on municipal advisors to fairly distribute assessments across all regulated entities.”¹²
- After its August 2015 meeting the Board stated “following more than a year’s analysis of its fees, the Board approved a proposal to adjust several MSRB fees to align the organization’s revenues with operational and capital expenses.”¹³
- At its April 2016 meeting “the Board voted to amend existing policies to address organizational reserves if they rise above or fall below established levels. The Board plans to finalize its decision about current organizational reserves at its July meeting.”¹⁴
- At its January 2019 meeting, the Board “continued its ongoing discussion of the MSRB’s reserve levels, which as previously communicated, are above the organizational target. The Board will continue its evaluation of reserve levels—incorporating input from an outside expert’s reserves analysis—and determine additional steps to responsibly manage reserves to appropriate target levels.”¹⁵
- At its April 2019 meeting the Board discussed “ensuring a fair and equitable balance of fees, responsibly managing expenses and estimating future revenue needs of the MSRB.”¹⁶

And yet, after all these deliberations the MSRB continues to collect more revenue than needed, and the relative contributions of dealers and MAs are still skewed. We strongly urge the Board to take a comprehensive look at its finances with the goal of once and for all establishing a funding mechanism that fairly allocates the MSRB’s expenses among regulated entities and does not assess the industry for more money than the MSRB needs. The solution may involve a major change in the way the Board funds itself. We look forward to working with you on this issue.

Regulatory and compliance guidance—The MSRB spends significant resources on providing regulatory and compliance guidance to regulated entities. This guidance is generally welcome and helpful, but not always. We recommend three changes to the manner in which the MSRB produces and communicates guidance.

First, we urge you to refrain from issuing guidance in areas where you do not have jurisdiction. Two examples illustrate the point. In September 2017 the MSRB issued Regulatory Notice 2017-18, “Market Advisory on Selective Disclosure,”¹⁷ and in April 2018 the MSRB published an issue brief titled

¹² Municipal Securities Rulemaking Board, “MSRB Holds Quarterly Board Meeting” (press release), February 4, 2014.

¹³ Municipal Securities Rulemaking Board, “MSRB Holds Quarterly Board Meeting” (press release), August 3, 2015.

¹⁴ Municipal Securities Rulemaking Board, “MSRB Holds Quarterly Board Meeting” (press release), April 18, 2016.

¹⁵ Municipal Securities Rulemaking Board, “MSRB Holds Quarterly Board Meeting” (press release), February 4, 2019.

¹⁶ Municipal Securities Rulemaking Board, “MSRB Holds Quarterly Board Meeting” (press release), April 29, 2019.

¹⁷ Municipal Securities Rulemaking Board, “Market Advisory on Selective Disclosure (Regulatory Notice 2017-18), September 13, 2017.

“Regulatory Framework for Municipal Market Derivatives.”¹⁸ Both documents seek to provide guidance to market participants on their respective subjects. We believe both documents were well-intentioned, but they raise problems. Most important, neither issuer disclosure nor derivatives regulation are within the MSRB’s authority. Issuer disclosure is regulated by the Securities and Exchange Commission, and the types of derivatives most used in the municipal market are regulated by the Commodity Futures Trading Commission. Issuing documents like this creates more confusion than clarity because it raises questions like whether the agencies with actual jurisdiction agree with the MSRB’s guidance.

Second, we urge you to issue all guidance in draft form for public comment before being finalized. The public comment process gives stakeholders an opportunity to weigh in on guidance which could have significant implications for compliance and enforcement.

Third, we ask in your communication of guidance to the market that you highlight guidance products that are significant to distinguish them from other MSRB communications that are less important. We offer as an example the MSRB’s “Compliance Tip of the Week” email dated November 9, 2020. This email included guidance on the application of MSRB Rule G-20 on gifts and gratuities to online meetings, particularly useful and constructive in the context of the pandemic and remote work. However, labeling this important information as a “compliance tip” and transmitting it via an email subscription channel does not give it sufficient prominence. The MSRB eventually published the same information in a FAQ document,¹⁹ but that came six weeks after the November 9 email. Highlighting important guidance will help ensure stakeholders see and benefit from it.

Data fees—The MSRB operates a market data business.²⁰ We support this initiative. The MSRB collects lots of important and relevant market data, and it is appropriate to make those data available to market participants. We point out, however, that most of market data the MSRB sells is derived from information provided by dealers.²¹ While the pricing for these data is at market rates, dealers receive no benefit from the sale of the information they provide. We urge the MSRB to consider pricing concessions for dealers for the data subscription services to which dealers provide the underlying information.

Cost-benefit analysis—In its publication “Policy on the Use of Economic Analysis in MSRB Rulemaking,”²² the MSRB states “this Policy establishes guidance that the MSRB is to follow in conducting economic analysis when engaged in the rulemaking process.” The Policy provides key elements of economic analysis and provides “guidance for implementing each of these elements and for integrating these elements into MSRB rulemaking.”

While the MSRB’s policy surrounding economic analysis is sound, from a stakeholder’s perspective, the product of that analysis is not always obvious, nor is the consideration the Board may give that analysis

¹⁸ Municipal Securities Rulemaking Board, “Regulatory Framework for Municipal Market Derivatives,” April 9, 2018.

¹⁹ Municipal Securities Rulemaking Board, “Frequently Asked Questions Related to COVID-19 Pandemic Regulatory Relief,” December 22, 2020, msrb.org/regulated-entities/COVID-19-FAQs.aspx.

²⁰ Municipal Securities Rulemaking Board, “Data Subscription Services and Products,” www.msrb.org/Market-Transparency/Subscription-Services-and-Products.aspx.

²¹ These include the MSRB Transaction Subscription Service, the MSRB Short-term Obligation Subscription Service, and the MSRB Primary Market Subscription Service.

²² Municipal Securities Rulemaking Board, “Policy on the Use of Economic Analysis in MSRB Rulemaking,” msrb.org/Rules-and-Interpretations/Economic-Analysis-Policy.aspx.

in its deliberations. We cite as an example the MSRB’s 2018 “Request for Comment on Draft Amendments to 2012 Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities.”²³ The request for comment includes a nine-page discussion of the economic analysis the MSRB intended to produce in support of its consideration of the proposed guidance changes. The economic analysis discussion included requests for information from market participants that would inform its analysis.

On August 9, 2019 the SEC published the MSRB’s transmission of the proposed G-17 guidance amendments.²⁴ The section of the document titled “Self-Regulatory Organization’s Statement on Burden on Competition” incorporates a discussion of the MSRB’s economic analysis of the proposal. The discussion is entirely qualitative in nature. There is little detail as to what data or other inputs the MSRB used in its analysis, what methodology the MSRB used, or what were the quantitative conclusions.

For example, one element of the revised G-17 interpretation requires underwriters to “affirmatively state in their standard disclosures that ‘the issuer may choose to engage the services of a municipal advisor with a fiduciary obligation to represent the issuer’s interests in the transaction.’”²⁵ The economic analysis discussion states “underwriters would incur additional cost associated with revising their policies and procedures (a one-time upfront cost) and delivering the statement in their standard disclosures during a transaction.” However, the analysis does not discuss the cost of these changes, nor does it compare quantitatively the additional costs to underwriters, or costs to issuers who heed the advice of the disclosure may bear, with any quantitative benefits that issuers might achieve as a result of the new disclosure standard. The discussion feels at times like an afterthought.

We urge the MSRB to take a more rigorous, quantitative approach to its economic analysis of rule and guidance proposals. BDA recognizes that stakeholders can help in this regard by providing data and estimates of the costs and benefits that, in our case, dealers might realize from proposed changes. In this respect, we pledge to do our best in our comments on MSRB initiatives to provide as much information as possible to inform the MSRB’s economic analysis.

MSRB Rulebook

Here we discuss two specific recommendations with respect to MSRB rules and the Board’s ongoing retrospective rule review.

MSRB Rule G-17 disclosures—MSRB Rule G-17 and its related interpretive guidance require underwriters to make significant, detailed disclosures to issuers covering issues like the underwriter’s role in the transaction, the underwriter’s compensation, and actual and potential conflicts of interest. Some disclosures must be made “in the earliest stages of the underwriter’s relationship with the

²³ Municipal Securities Rulemaking Board, “Request for Comment on Draft Amendments to 2012 Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities” (

²⁴ Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change To Amend and Restate the MSRB’s August 2, 2012 Interpretive Notice Concerning the Application of Rule G-17 to Underwriters of Municipal Securities, 84 Fed. Reg. 39646 (August 9, 2019).

²⁵ *Ibid.*

issuer”²⁶ and others must be made when the underwriter is engaged to perform underwriting services. For frequent issuers, that means issuer officials likely receive identical disclosures from the same underwriters multiple times per year. The requirement is inefficient and unnecessary. We urge the MSRB to amend the Rule G-17 interpretive guidance so that if an underwriter has provided to an issuer compliant G-17 disclosures in the preceding year and the content of the disclosures has not changed, the requirement would be satisfied and the underwriter would not need to make multiple identical disclosures.

MSRB Rule G-10 disclosure—MSRB Rule G-10 requires dealers annually to “provide in writing (which may be electronic) to each customer” certain information about the dealer’s SEC registration and about the MSRB. The rule does not distinguish between customers who own or have traded municipal securities in the last year and those who have not. The rule results in superfluous disclosures to customers who do not own or trade municipal securities. We ask the MSRB to amend Rule G-10 to specify that it applies to customers who own municipal securities or who have traded municipal securities since the dealer’s last annual disclosure.

EMMA

The MSRB’s Electronic Municipal Market Access (EMMA) platform is an important asset to all market participants. The system has greatly improved municipal market transparency and provides an easy means for investors, issuers, dealers and others to access trade and price information, issuer financial disclosures, and other relevant information. We suggest two improvements to EMMA that would make it even more valuable to stakeholders. Our recommendations generally apply to improving access to and usefulness of issuer disclosure documents.

Naming conventions—Issuer records on EMMA sometimes include different names for the same issuer across various issues. For example, the City of New York might be referenced as City of New York, New York City, NYC, etc. This can make finding information on EMMA cumbersome, and users may miss information relevant to what they are searching for.

Linkage issues—Some issuers’ disclosure information on EMMA is difficult to find because it is not linked to all CUSIPs to which it applies. When an issuer files a financial statement, they may fail to associate the filing with all relevant outstanding CUSIPs. That can cause data to appear to be missing when a user searches for information on a CUSIP to which relevant disclosure filings have been filed but not linked.

These issues are of particular concern to the dealer community, since we rely on the disclosure information contained on EMMA in the context of our due diligence responsibilities in determining whether issuers are in compliance with outstanding continuing disclosure agreements—the “five-year lookback.”

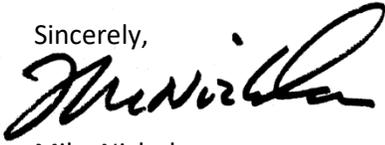
Conclusion

BDA welcomes the opportunity to provide comments on the MSRB’s strategic goals and priorities. We believe the strategic planning process can result in a robust agenda for future MSRB work. We value our

²⁶ Municipal Securities Rulemaking Board, “Interpretive Notice Concerning the Application of MSRB Rule G-17 To Underwriters of Municipal Securities,” August 2, 2012, www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-17.aspx?tab=2.

relationship with the Board and MSRB staff and we look forward to working with you on these and other initiatives to improve the municipal market.

Sincerely,

A handwritten signature in black ink, appearing to read "Mike Nicholas". The signature is fluid and cursive, with a large initial "M" and "N".

Mike Nicholas
Chief Executive Officer
Bond Dealers of America