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April 21, 2011

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

Re: MSRB Notice 2011-18:

Dear Mr. Smith:

Hartfield, Titus & Donnelly, LLC ("Hartfield") appreciates this opportunity to submit comments on the Municipal Securities Rulemaking Board's ("Board") Notice 2011-18[1] (the "Notice") in which the Board requests comment on draft Rule G-43, and associated amendments to Rules G-8, G-9, and G-18 (the "Proposed Rule") regarding municipal securities broker's brokers ("MSBBs"). Hartfield also is participating in the drafting of the comment letter on the Proposed Rule to be submitted by the Securities Industry and Financial Markets Association ("SIFMA") (the "SIFMA Letter"), and will support the views expressed therein. However, we believe that certain aspects of the Proposed Rule pose substantial risks to the efficient operation of the municipal securities secondary market (the "Market"), and are thus submitting these additional comments.

We are taking the opportunity in this letter to reiterate our concerns regarding the aspects of the Proposed Rules that we believe are the most: (i) harmful to maintaining liquidity in the Market; (ii) inconsistent with the efficient operation of bid-wanteds in the Market; and (iii) anti-competitive. We also wish to reiterate the concerns that we raised in our comment letter and the SIFMA comment letter (the "Prior Letters") regarding MSRB Notice 2010-35[2] (the "Proposed Guidance"), as the bulk of the Proposed Guidance is reflected in the Proposed Rule without significant modification. We believe that both the Proposed Guidance and the Proposed Rule will inflict costs on the Market that will greatly outweigh whatever regulatory benefit is perceived by the Board.

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[1] MSRB Notice 2011-18 (Feb. 24, 2011).

[2] MSRB Notice 2010-35 (Sept. 9, 2010).

Rule G-43(a)(iv)

Section (a)(iv) of the Proposed Rule is perhaps the most problematic provision. It requires that MSBBs review the results of each bid-wanted to determine whether the resulting highest bid represents a "fair and reasonable" price "within a reasonable degree of accuracy." By its terms this new requirement would effect every bid-wanted conducted in the Market every day, and require that MSBBs analyze the results of every one. On any given day an MSBB can have over 3,000 items, with 3,000 to 15,000 bids, that must be analyzed. (This is virtually impossible without significant increase in staff, systems and market data analysis.) On the other hand, a dealer (who has the direct responsibility to a customer for such analysis) might put 20 or 30 items out for the bid and have only those items to analyze. Thus, an MSBB as an individual firm, who has no direct responsibility for determining fair market value for retail customers, has a significant burden when compared with an individual dealer. Since the dealer still has the responsibility to make their own determination of fair market value, this "double" requirement is repetitive and unnecessary.

MSBBs are like exchanges, we match sides on trades. To our knowledge no exchange is required to assess the market value of the securities they match. As a matter of fact, we are registered with the SEC as an ATS, because they consider our function to be similar to that of an exchange. Also, to our knowledge, no Inter Dealer Broker (IDB) brokering corporate bonds, Treasury bonds, Federal Agency bonds or Mortgage bonds (even with the problems in the mortgage market) is required to assess the value of the securities they broker. Even in such esoteric markets as emerging markets, CDS, medium-term swaps and others, to our knowledge, the IDB is not required to asses the fair market value of the securities.

This Section also requires that in instances where an MSBB is unable to conclude that the price is fair and reasonable, it is required to notify the selling dealer of this fact and require the dealer to provide written notice that it acknowledges the disclosure and still wants to effect the transaction. We believe that this notice and acknowledgement procedure is the practical equivalent of simply prohibiting such transactions. The time it will take for the analysis, notification, communication and discussion with seller and seller's providing written acceptance and authorization will be an impediment to liquidity in the Market.

We again reiterate our proposal in response to the Proposed Guidance on this point that as an alternative to the higher fair price standard and the proposed written notice procedure, MSBBs could be required to inform the dealer if we have reason to believe that a bid is either above or below certain parameters which we would establish for this purpose, and disclose in our procedures under proposed Rule G-43(d)(ii), and follow the seller's directions on the actions to take. We would keep as part of our documentation of the transaction a notation of the analysis and communication. Thus we would have the RECORD necessary for documentation, even though it may not be written.

Further, we ask the Board to apply the requirements of this section equally to all MSBBs, including to those who operate electronic trading systems. Otherwise this could be seen as anti-competitive.

Rule G-43(c)(ii)

Section (c)(ii) requires that, in cases of bid-wanteds for issues of "limited interest . . . the [MSBB] **MUST** reach dealers with specific knowledge of the issue or known interest in the securities of the type being offered." Here we would like to reiterate the general point that bid-wanteds should be allowed to continue to be conducted subject to the direction and control of the selling dealer. Our relationship with selling dealer is like being a temporary employee. It is as if we were sitting on their trading desk for the specific transaction and, as such, we follow their instructions. Sometimes the instructions are very thorough and other times very general. In particular, a seller may restrict the manner in which we perform the bid-wanted, such as directing us to seek bids from only certain dealers. It is their bid-wanted and we follow their instructions. Thus, we note that this provision is particularly problematic by requiring that the MSBB **MUST** reach certain dealers. This requires that (a) the MSBB know bidders who meet the criteria, (b) have permission to contact the bidders, and (c) that such bidders are interested in discussing the issue. We believe that the standard in this provision should be changed to "should make reasonable effort to reach" from "must reach."

Further, we ask the Board to apply this requirement to all MSBBs, including those who operate electronic trading systems. Absent any regulatory limitations, in order for such systems to improve the probability of receiving bids that reflect fair and reasonable prices, the requirements of this Section should be met.

Rule G-43(c)(iv)

We agree on the proposed Rule's restriction on giving preferential information (such as "last looks", directions on what to bid, suggestions on lowering a bid or raising a bid) to bidders. However, the role of the MSBB is to facilitate liquidity and the efficient functioning of the Market. To do this, the dissemination of market, and certain bid, information, in a manner consistent with maintaining anonymity, is an appropriate communication with dealers. It is generally required of us by dealers. In addition to general market information and prior execution prices for the same or similar securities, communications should be allowed regarding clearly erroneous bids, whether high or low, and, after the bidding is closed, a bidder's position in the bidding process. (Please refer to our comments on G-43(d)(i)(H) below.) Informing bidders on their position in the bidding process ("where they stand") will allow bidders, who do not have the high bid, to deploy their capital elsewhere and/or place bids on other items.

Rule G-43(c)(vi)

We agree that if an MSBB believes a bid has been submitted in error, before notifying the bidder, they should either get permission from the seller, or provide prior notice to the seller of their procedure on erroneous bids. The latter option is in line with Section (d) of proposed Rule G-43.

However, contacting all bidders to allow them to adjust their bids, will lower prices for the seller and introduce greater inefficiency and delay into the Market. Since the only bid in question is the erroneous bid, which will be much higher than the other bids, the bidder will remove their bid and put it on the correct item. Then the "cover bid" will be the high bid. Allowing all bidders to re-bid will provide them an opportunity to lower their bids and place delays in the bid-wanted system. Our experience with bids on the same item over several days shows that providing a bidder an opportunity to re-bid will result in lower bids in general and a lower price received by the seller. This is unfair to the seller, our client, since the cover bid is probably a fair and reasonable bid.

We are registered as an Alternative Trading System (ATS) with the SEC. This registration requires that we monitor and report trading volume to the SEC. Our records show that any single municipal security (as identified by a single CUSIP number), in one year, trades through us 1.31 times.

Approximately 25% of the single securities we trade, trade more than once. These are generally new issue municipal securities. 75% trade only once. Thus, there may be very little simultaneous or current pricing information on this 75%. Therefore, a bid reduced by \$1.50 or \$3.00 still could be considered fair and reasonable, yet will translate into a lower price to the seller and ultimately the investor. It is not worth this reduced value just to allow all bidders to re-bid when the high bidder made a mistake and the other bidders are in line.

Rule G-43(c)(vii)

Section (c)(vii) requires that an erroneous bid may not be adjusted without the bidders "written instruction." We believe that this requirement is unnecessary given Section (c)(vi). An erroneous bid is clearly a wrong bid. If a bidder removes or changes their bid it will be recorded due to MSRB Rule G-8(a)(xxv). By requiring the bidder to provide written instructions the Board is introducing an onerous restriction on bidders. This means the bidder has the choice of leaving in their erroneous bid or taking time to notify the MSBB in writing to change the bid. This only delays the process and burdens the bidder with no improvement in liquidity, efficiency or price transparency. There clearly is no benefit to the seller, MSBB or bidder.

We currently record every bid received. If a single bidder changes its bid, we record both the first and the second bid. Since such recordkeeping will be required of all MSBBs in their bid-wanted process, we suggest that with the addition of information on the name of the party at a bidder that authorizes a change in a bid and their reason for the change it would provide sufficient documentation to allow Market regulators to review the propriety of any changed bid on a bid-wanted.

Rule G-43(d)(i)(F)

Section (d)(i)(F) requires that MSBBs disclose their compensation on matched transactions to each counter-party in those transactions. We note that the compensation on MSBBs transactions is very small, relative both to the size of the transactions, and to the compensation earned by dealers on these transactions. Our analysis, using MSRB's reported trade prices, has shown that, on average, dealers involved in our trades make 5 times our commission. This analysis includes a dealer's purchase from a customer, sale to us, our sale to another dealer and that dealer's sale to a customer. Further, we are unaware of any concern in the dealer community regarding the compensation paid to MSBBs. Given this, we do not perceive any industry demand for, or regulatory benefit, from this information on a transaction by transaction basis.

We suggest that MSBBs be required to provide to their trading counter-parties a copy of their commission schedules for transactions, and that such schedules be required to reflect the maximum charge that MSBB could impose on a given transaction. We believe that publishing such a schedule provides Market participants information sufficient to allow them to address any concerns they may have with MSBB compensation.

In addition, since NSCC has no facility for such disclosure and 100% of MSBB transactions are reported and matched at NSCC, this disclosure would require industry wide modifications to trade reporting, matching and clearance. These modifications by dealers, MSBBs and NSCC will be very costly and provide no demonstrated benefit to the industry. Also, this would require modifications to the Board's RTRS infrastructure and reporting of transactions.

If an industry participant wanted to verify the commission an MSBB received on a trade (two or more matched transactions) they could easily review the Board's record of the prices on the transactions. This is generally available within 15 minutes of trade from the Board on their EMMA System or SIFMA on their Investing in Bonds website.

<u>Rule G-43(d)(i)(H)</u>

Section (d)(i)(H) prohibits disclosure of bid information received in a bid-wanted (except to the winning bidder, who may receive the cover bid, and the seller, who may receive all bids) unless the MSBB makes this information available "to all market participants on an equal basis at no cost" and also discloses that such bids may not reflect the fair value of the securities in question. On the day an item is out for the bid, we provide the seller with all bids and the winning bidder, their cover bid. In addition, after the bidding is "closed" (i.e. when we "put up" the high bid to the seller), we provide the other bidders information on where they stand in the bidding. For example in a bid-wanted where the high bid is 99.500, the second bid is 99.400, the third bid is 99.300 and the forth bid is 99.200. If the third bidder (99.300) asks where they stand, we will tell then that they were third and "out by" 20 basis points. This is very valuable information to the bidders. It provides information on current pricing which they use for future analysis of levels on other securities in the market, offerings or bid-wanteds. We do not provide non-bidders with bid information. On the day after the item was "out-for-the-bid", we provide all participants on our system (HTDonline.com), bidders and non-bidders, all bids on all items. We feel this practice provides value to the bidders and encourages dealers to bid on items. In our experience, this has worked well and contributed to secondary market liquidity.

In the release, the Board suggests that the bidding information be made available to the "Public". We interpret this to mean anyone, even retail investors. This is something we have no facility to do. We are registered as an Alternative Trading System with the SEC and have strict requirements on access to our system. Thus we make bidding information only available to those permissioned to access our system. This access is strictly controlled and monitored. In particular, if someone has been permissioned to access the system and does not access it for 30 days, their permission is removed. Further, this disclosure to the public will have an onerous burden on MSBBs who have limited automation in their systems. They would be required to provide paper information on all their bid-wanteds to anyone who contacted them. This will be very costly.

The Board has stated that a disclosure be made that bids may not reflect the fair value of the securities in question. We expect that this requirement can be satisfied by a single disclosure on any page which displays all the bids on our items. If our understanding is in error, please specify the detail requirement in the Rule.

<u>Rule G-43(d)(i)(I)</u>

Section (d)(i)(I), which prohibits the disclosure of certain non-public information, is already directly addressed by MSRB Rule G-24. Since this is simply a restatement of a Rule the MSBB must already comply with, it is duplicative and does not further industry regulation or benefit the Market in any way. We ask that it be removed.

Rule G-43(d)(i)(J)

Section (d)(i)(J) requires that if MSBBs have customers, they must disclose this fact to sellers and bidders in writing. The Board provides no explanation on the rational for this Section. Further there is no history of enforcement from either the SEC or FINRA that would suggest the need for this disclosure. There is an abundance of enforcement actions in other sections of the Market showing abuses attributable to customer relationships, yet there is no similar disclosure requirement for these other segments. If it is the intention of the Board to label certain MSBBs in order to "red brush" them and create an impression of quality different from an MSBB without customers, in this they will succeed. This disclosure only creates an impression of inequality with no attendant Market benefit. It may even be a determent to the MSBB with customers, not because it fundamentally matters in brokering, but only because the Board, by including this Section, leaves the impression that there is something "wrong" with such MSBBs. Also, the Board leaves an impression that such MSBBs have conflicts of interest without actually describing what these conflicts are and how they differ from the conflicts faced by any other municipal securities broker or dealer that has a wide variety of client types. In summary, without further justification being offered, we believe that this provision creates an impression that an MSBB that has customers should be viewed as suspect, and as such, this distinction remains inappropriately anti-competitive among MSBBs. We ask that this Section also be removed.

Rule G-43(d)(ii)

Section (d)(ii) requires that MSBBs must disclose the policies and procedures adopted in order to comply with Section (d)(i) of the Proposed Rule annually in writing to sellers and bidders, and also post them "in a prominent position" on their website. We support the disclosure of an MSBB's policies and procedures as related to the operation of its bid-wanted function. Any other disclosure, such as Written Supervisory Policies and Procedures should not be included in this disclosure. These are proprietary documents, created through significant effort and expense and unique to each MSBB. They relate the firm's method of insuring compliance with various Rules and Regulations of the Board, SEC, FINRA and other regulatory bodies. There is no requirement in any regulatory scheme that would suggest the publication of these documents. We request the Board add specificity to the Rule by limiting the disclosure to those policies and procedures that specifically relate to the operation of the bid-wanted process and not its regulatory compliance.

Request for Comment Regarding Electronic MSBBs

We expect that SIFMA's comment regarding the extent to which the rules for electronic MSBBs should be more permissive than for traditional or voice MSBBs will be that it is anti-competitive on its face. We agree with this position. The Board should provide a detailed explanation of how excluding electronic MSBBs from certain provisions of the Proposed Rule would be a benefit to the Market and the investing public. And in doing so, we would ask the Board to specifically address the issue of electronic MSBBs that are owned directly by dealers or a group of dealers. Providing competitive advantage to one type of market participant through regulation should always be avoided, as it violates the principle of a level playing field as further discussed in our response above to Section (d)(i)(J).

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As a final comment, we noticed that the Board, in its April report on its Quarterly Meeting, said that they would consider rebalancing its assessments. We would like to remind the Board of our comments on their 2010-10 filing with the SEC on Proposed Fee Increases. We support the Board's desire that the fees it levies on ". . . each dealer reflect the extent of its municipal securities activities." We believe that, in order to allocate its fees in a manner consistent with its stated goal, the Board should transition away from fees on transactions to a fee model based on the *revenue* that any municipal securities dealer derives from its municipal securities activities. Schedule I of each broker-dealer's fiscal year end FOCUS Report requires reporting annual municipal income. We suggest the assessment of transaction fees should be based on this income rather than transactions.

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We thank you again for the opportunity to comment on this important matter.

Very truly yours,

Mark J. Epstein
President and Chief Executive Officer