August 3, 2010

Ernesto A. Lanza
General Counsel
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Notice 2010-10

Dear Mr. Lanza:

I apologize for this late response to the Board's request for comment on the Draft Interpretative Guidance on Prevailing Market Prices and Mark-ups for Transactions in Municipal Securities. I feel, however, the need to comment, based upon what I believe the Board will view as the sparse response from the municipal bond community in general.

Many members of the municipal bond community may be of the impression that comment letters from SIFMA and the RBDA adequately express their views and that the MSRB views the trade association letters as representing the opinion of the bond community in general. I realize, of course, that is not the case. This interpretation could be adopted and it will be alleged that the industry was not concerned about the impact as demonstrated by the small number of comment letters. I can assure you that every market participant that I have spoken with about the interpretation is alarmed by the prospect of the negative impact this potential rule interpretation will have on market liquidity.

Forget, for a moment, the pure inequity of the circumstance whereby a dealer that acquires unrated revenue bonds for inventory with a cover bid twenty points back is subject to the same profit restrictions as a dealer that buys a AAA-rated GO where the cover bid was only $1.00 per thousand less. Also ignore the fact that it is patently irrational to require a municipal dealer to adhere to the 3(a) Exchange Act definition to be treated as a market maker. Simply focus on the lost liquidity to issuers and investors that will result from the market's rational reaction to this rule interpretation.

Review the attachment to Ronald Dieckman's letter. Very few of those bonds were non-rated, the most illiquid, yet the "cover" bids on many of those securities were one and a half to three points behind the high bid and the bids widened from there. The Board, however, is now proposing that mark-ups be measured from a "prevailing market price", generally defined in this case as the high bid. This would be penal enough in instances where the second highest bid is 2 to 5 points lower than the bid of the acquiring dealer, but it will suffocate bids in instances where there are 20 to 30 point spreads between bids.

Yes, dealers will place bids on municipal bonds where they are aware that the high bid without them is 20 points or more lower. This is the result of a number of factors, including but not limited to: a fuller understanding of the creditworthiness of the issuer, a desire to support the issuer's securities in the market and a belief that the bonds can be successfully marketed at a price above the bid. It is extremely short sighted to interpret the rules to treat dealers willing to acquire bonds at a price considerably above what is believed to be the next best bid as not acting in the capacity of a market maker and providing a service to the market that commands reward. Rational dealers will begin bidding extremely illiquid municipal bonds as close to the perceived cover bid as possible, removing, in some cases, twenty points or more in liquidity from the market.

It bears repeating that an isolated transaction in a municipal security can easily represent the only trade in that security that year. Furthermore, isolated transactions in story bonds cannot be used to support a determination that contemporaneous cost is not the prevailing market price. However, if the isolated transaction happens to be the dealer's purchase, that is practically the only evidence that a dealer can utilize in determining prevailing market price. I cannot be the only observer that notes a contradiction there.

Surely, the Board cannot be so indifferent to the interests of bondholders and issuers alike that the likely unintended consequence of this interpretation will be ignored. As has been stated many times, the market for Municipal Securities is geometrically more complex than is the quoted equity market, or even the corporate debt market. If the Board desires the most efficient market, considerations must be made for those truly acting as market makers, who are in many cases taking considerably more risk than those that fit within the 3(a) definition. Any interpretation of Rule G-30 that does not take this into account will have a considerably negative impact on market liquidity in general.

Thank you for the opportunity to comment and for your consideration. I apologize again for the tardy response.

Respectfully,

Chris Melton
Executive Vice President