

VIA ELECTRONIC MAIL

October 7, 2013

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

Re: MSRB Notice 2013-16: Request for Comment on Whether to Require Dealers to Adopt a “Best Execution” Standard for Municipal Securities Transactions

Dear Mr. Smith:

On August 6, 2013, the Municipal Securities Rulemaking Board (MSRB) published its request for public comment on whether to require a broker, dealer, or municipal securities dealer (collectively “dealers”) to seek “best execution” of customer orders for municipal securities and provide detailed guidance to dealers on how “best execution” concepts would be applied to municipal securities transactions (Request for Comment).¹ The MSRB is also seeking specific comment from dealers on the application of their existing best execution requirements to transactions in other types of fixed income securities under FINRA Rule 5310. The purpose of the Request for Comment is to elicit input on the benefit and impact of this requirement including the costs, burdens, any operational concerns, as well as any alternatives for the MSRB to consider.

The Financial Services Institute² (FSI) appreciates the opportunity to comment on this important proposal. In principle, FSI supports MSRB efforts that will provide retail investors with better execution and more fair and efficient pricing for municipal securities. However, we foresee several challenges in implementing best execution in the municipal securities market due to the semi-active liquidity, diversity, and fragmentation in the market. A proposal that properly balances the laudable goals with the accompanying challenges must be properly vetted and would require an extended comment and implementation period to develop and test. We provide preliminary thoughts on addressing these concerns and challenges, and look forward to offering additional comments to any MSRB proposed rule in the future.

Background on FSI Members

The independent broker-dealer (IBD) community has been an important and active part of the lives of American investors for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD firms also share a number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; primarily engage in

¹ Request for Comment on Whether to Require Dealers to Adopt a “Best Execution” Standard for Municipal Securities Transactions, MSRB Notice 2013-16, available at: <http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2013/2013-16.aspx?n=1>.

² The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has over 100 Broker-Dealer member firms that have more than 138,000 affiliated registered representatives serving more than 14 million American households. FSI also has more than 35,000 Financial Advisor members.

the sale of packaged products, such as mutual funds and variable insurance products; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered investment adviser firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial advisers are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their financial goals and objectives.

In the U.S., approximately 201,000 independent financial advisers – or approximately 64 percent of all practicing registered representatives – operate in the IBD channel.³ These financial advisers are self-employed independent contractors, rather than employees of the IBD firms. These financial advisers provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisers are typically “main street America” – it is, in fact, almost part of the “charter” of the independent channel. The core market of advisers affiliated with IBDs is comprised of clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisers are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other centers of influence.⁴ Independent financial advisers get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisers have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisers. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is committed to preserving the valuable role that IBDs and independent advisers play in helping Americans plan for and achieve their financial goals. FSI's primary goal is to ensure our members operate in a regulatory environment that is fair and balanced. FSI's advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

Comments

FSI appreciates the opportunity to provide a response to the Request for Comment. While a best execution standard for municipal securities can provide benefits to retail investors, the implementation of this standard to the municipal securities market presents a variety of challenges. We also urge the MSRB to make full use of its recently adopted Policy for Integrating Economic Analysis in MSRB Rulemaking in pursuing a best execution standard.⁵ We believe that the approach to cost-benefit analysis described in the adopted policy represents a very high quality commitment to additional transparency and more effective rulemaking. FSI supports regulatory initiatives that enhance transparency and improve pricing for retail investors, and we look forward to providing further comment in the event that the MSRB advances a specific proposal that achieves the promise of best execution while avoiding the pitfalls. In the meantime, we provide the following thoughts:

- **Approach must be process-based:** A proposed rule with regard to best execution should be process-based. Because of the unique characteristics of the municipal securities market, a number of factors must be weighed in establishing whether a dealer has fulfilled his or her obligations to the customer. Because the market for municipal securities lacks the systemized infrastructure for equity markets (Reg NMS, for example), pricing alone cannot serve as the prime factor when assessing whether a dealer has fulfilled his or her obligation. Recognizing this reality, we

³ Cerulli Associates at <http://www.cerulli.com/>.

⁴ These “centers of influence” may include lawyers, accountants, human resources managers, or other trusted advisers.

⁵ Municipal Securities Rulemaking Board, “Policy on the Use of Economic Analysis in MSRB Rulemaking,” available at <http://msrb.org/About-MSRB/Financial-and-Other-Information/Financial-Policies/Economic-Analysis-Policy.aspx>.

encourage the MSRB to develop a specific and tailored process that identifies when and whether a dealer has complied.

- **“Execution-with-diligence” standard:** SIFMA’s Recommendation to Improve Customer Execution⁶ through an “execution-with-diligence” standard reflects a thoughtful and reasonable approach to alleviating many challenging issues with respect to implementation of a best execution standard in the municipal securities market. The framework advanced in the Recommendation contains a non-exhaustive list of factors that would be considered when determining whether a dealer has used “reasonable diligence” with respect to customer execution of municipal securities. Such an approach properly balances the concerns for additional transparency while recognizing the unique characteristics of the municipal securities market and their accompanying challenges.
- **Extended development process:** Because of the many challenges accompanying this proposal, we suggest the MSRB provides an extended comment period and implementation period. Industry participants will require sufficient time and resources to properly review the impacts and procedures required to comply with any proposed rule. We recommend a period of at least 12 months for the implementation period and 90 days for the comment period.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with the MSRB on this and other important regulatory efforts.

Thank you for your consideration of our comments. Should you have any questions, please contact me at (202) 803-6061.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "D. T. Bellaire". The signature is fluid and cursive, with a large initial "D" and "T" and a stylized "Bellaire".

David T. Bellaire, Esq.
Executive Vice President & General Counsel

⁶ Securities Industry and Financial Markets Association, “SIFMA Submits Recommendation to the MSRB on ‘Execution With Diligence’ Standard for Municipal Trading,” available at <http://www.sifma.org/issues/item.aspx?id=8589944578>.