



April 29, 2011

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

Re: MSRB Notice 2011-18: Request for Comment on MSRB Draft Rule G-43 and Associated Amendments to Rules G-8, G-9, and G-18

Dear Mr. Smith:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ appreciates this opportunity to respond to Notice 2011-18² (the “Notice”) issued by the Municipal Securities Rulemaking Board (the “MSRB”) in which the MSRB 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”). The concepts embodied in the Proposed Rule were first proposed by the MSRB in September 2010³ (the “Proposed Guidance”).

Please note: We are taking the extraordinary step of submitting two comment letters regarding the Proposed Rule. As explained more fully below, this letter was drafted with significant input from a variety of broker-dealers (wire houses, mutual fund affiliates, and others) who regularly trade with MSBBs to meet their municipal securities trading needs (the “Retail Dealers”). Our other comment letter was drafted with significant input from MSBBs responsible for over 90% of the inter-dealer trading in municipal securities (the “SIFMA MSBB

¹ The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

² MSRB Notice 2011-18 (Feb. 24, 2011).

³ MSRB Notice 2010-35 (Sept. 9, 2010).

Letter”). Given the potential impact of the Proposed Rule, we ask that each of these letters be given careful consideration.

SIFMA supports effective and efficient regulation of the municipal securities markets that helps to aid market liquidity in a manner consistent with customer protection. However, we have become extremely concerned about the MSRB’s commitment to adopting, through the Proposed Rule, the concepts embodied in the Proposed Guidance. In our comment letter on the Proposed Guidance we sought to identify what we believed were the potentially serious negative consequences that many aspects of the Proposed Guidance could have on the business of MSBBs, and therefore on the municipal securities secondary market (the “Market”). We respectfully submit that the concerns noted in our comment letter regarding the Proposed Guidance persist with equal force in connection with the Proposed Rule.

Having had the opportunity to consider the Proposed Rule, we have come to question whether any new MSRB rule directed solely at MSBBs is warranted. As discussed more fully below, we do not believe that the enforcement actions cited by the MSRB as supporting the need for additional rules are sufficient to that purpose. In addition, we are concerned that the Proposed Rule could have a significant unintended negative impact on retail transactions and transactions in thinly-traded issues. As described more fully below, these parts of the Market are among the less liquid, and we are concerned that what may appear to be minor impediments to liquidity when considered individually against the breadth of the Market as a whole may have severe consequences for the less liquid, but very important, retail and thinly-traded segments of the Market.

We therefore respectfully request that the MSRB withdraw the Proposed Rule, and continue to focus its resources on efficient coordination with the Financial Industry Regulatory Authority (“FINRA”) on the enforcement of existing MSRB rules.

SIFMA is Submitting Two Comment Letters on the Proposed Rule

SIFMA’s comment letter on the Proposed Guidance (the “Proposed Guidance Letter”) purposefully analyzed the Proposed Guidance from the perspective of the MSBBs, as they were the parties most directly impacted by it. And through that perspective SIFMA also sought to highlight the likely impacts of the Proposed Guidance on the Market in general. We believe that this may have given the impression that these concerns were not shared outside of the MSBB community. If so, that impression is false.

In order to demonstrate the seriousness of the securities industry’s concerns regarding the Proposed Rule, SIFMA is filing today two comment letters

regarding the Proposed Rule, this letter and the SIFMA MSBB Letter. SIFMA hopes that by submitting both of these letters the breadth and seriousness of the concerns in the securities industry regarding the Proposed Rule will be clearly demonstrated.

Background

The Retail Dealers reviewed both the Proposed Guidance Letter and the SIFMA MSBB Letter in connection with participating in the drafting of this letter. While this letter does not necessarily adopt every position set forth in those letters, it agrees with their overriding conclusion: the Proposed Rule has the potential to do unintended, but significant, harm to the Market. Therefore, we also agree that the Proposed Rule should be withdrawn, and the trading of municipal securities between MSBBs and Retail Dealers should continue to be judged under existing MSRB rules. We also believe that, should the MSRB decide to move forward with a rule focused on the activities of MSBBs, the aspects of the Proposed Rule *most* potentially harmful to the efficient operation of the Market should not be included.

Prior Enforcement Actions

The MSRB places great emphasis in the Notice on the importance of the prior enforcement actions against MSBBs.⁴ As the primary trading counterparties with MSBBs, we echo the concerns of the MSRB regarding the conduct that led to these enforcement actions. But these enforcement actions lead us to draw a much different conclusion than does the MSRB: we believe that they demonstrate that existing standards of conduct were not being met, and that the MSBBs had been in need of regulatory-enforcement attention. We believe that such attention should appropriately continue, just as it should regarding other broker-dealers, to ensure that the investing public continues to be able to rely on the integrity of the municipal securities market. We do not believe, however, that these enforcement actions provide sufficient justification for rulemaking directed solely at MSBBs, especially when the Proposed Rule may significantly impede the operation of the Market, to the ultimate detriment of the retail investing public.

Principal Objections to the Proposed Rule

The following comments set forth our principal objections to the Proposed Rule. We note that the fact that we do not discuss other provisions should not be

⁴ Notice, footnote 1.

read as an endorsement of those provisions. The provisions discussed below are intended to provide the MSRB with additional, specific input to help illuminate what the Retail Dealers believe are the substantial risks inherent in these aspects of the Proposed Rule.

We also hope that the following comments will be read in the proper context. The Market is characterized by an extremely large number of issuers, many of whom issue securities on an infrequent basis. On any given day, a Retail Dealer that is active in the Market can have between 2,000 to 5,000 items to potentially bid upon, and therefore review, and may eventually bid upon hundreds of these items. That same Retail Dealer also could have a number of items out for bid, for which it will need to devote additional attention. Therefore, we believe that any impediments to trading in what is already a labor-intensive market must be carefully reviewed to ensure that the burdens to liquidity are justified.

Written Notice/Acknowledgement Provisions

We cannot overstate the concern that we have with the provisions of the Proposed Rule that impose new pre-trade written notice and/or acknowledgement requirements on certain transactions in the Market.⁵ Such requirements are inconsistent with the efficient operation of the Market, *especially when applied to retail-size blocks and transactions thinly-traded issues*. Retail Dealers already expend significant resources on post-trade operational and compliance systems, including best-execution review systems, in order to ensure fair treatment of customers and compliance with existing rules.

We believe that the imposition of pre-trade written notice/acknowledgement requirements will inordinately increase the cost of these trading activities. We can state unequivocally that additional resources will need to be developed to deal with the tracking of these notices, the documentation of the determination of what action to take in response to a fair price notice from an MSBB, and the supervision of that decision-making process. All of these issues are more fully discussed directly below.

MSBB Fair Price Determination and Notification Process

The requirement in Rule G-43(a)(iv) of the Proposed Rule that MSBBs review the results of each bid-wanted to determine whether the resulting price is fair and reasonable is the most problematic substantive provision in the Proposed Rule, because the process is designed to occur pre-trade, and because we believe

⁵ See Rule G-43(a)(iv) and (d)(i)(H).

that we are better situated to review the results of the bid-wanted process for this purpose. When a Retail Dealer receives the high bid from an MSBB on a bid wanted, it reviews that bid price as *one piece of information* in deciding whether to execute that sale at that price. As the MSRB states in the Notice, the Retail Dealers generally make substantial investments in their municipal securities departments in the areas of trading and analysis, and that therefore Retail Dealers can analyze the prices resulting from bid-wanted.

We also note that while the MSRB is likely correct that the vast majority of Market transactions will not be subject to this provision of the Proposed Rule, we are concerned that many transactions in the less liquid sectors of the Market may be. For example, we are concerned that adding a pre-trade bid-wanted price review will substantially impact the trading of retail size orders and transactions in thinly traded securities, as these types of transactions are the most likely to result in a high bid for which MSBBs will have difficulty in making a fair price determination. This is the case because retail size orders are subject to significant trade-price variations on a day to day basis, as bidders interested in these size orders regularly move in and out of the market, and the absence of one or two bidders from one day to the next could have significant impact on the high bid. In addition, thinly-traded issues do not, by their nature, provide meaningful recent transaction executions against which to judge the result of a bid-wanted. We believe that requiring MSBBs to analyze the high bids in these bid-wanted will result in a substantial number of these transactions being subject to the analysis, notification and written acknowledgement requirements of the Proposed Rule, further impeding liquidity in these parts of the Market.

We also are concerned that, if the Proposed Rule is adopted, Retail Dealers will be subject to second-guessing on every executed transaction in connection with which they were notified by the MSBB that it could not make a fair price determination. Given that Retail Dealers will be required to defend these transactions to regulators (or plaintiffs' attorneys) operating with the benefit of hindsight, we believe that the amount of diligence required to analyze the price of these transactions, document the results of that diligence, and subject those determinations to appropriate supervisory review would greatly outweigh the financial benefit to the Retail Dealer of effecting the transaction, further impeding liquidity for retail size orders and thinly-traded issues.

The likely practical result of this state of affairs would seem to be that Retail Dealers would be forced to make a determination along the lines of the following: either the MSBB's determination was clearly erroneous, in which case the Retail Dealer will consider executing the trade (but may not do so in all cases, based upon a risk assessment), or the trade with the client will not be executed. We also note that this situation would not necessarily be cured by putting the securities out to a different MSBB or trading system (assuming that such a

process was feasible for single retail orders), because the price resulting from that secondary process would *still* need to be analyzed in light of the first price received to determine whether it differed sufficiently from the result of the first bid-wanted to defend the decision to execute the transaction with the customer.

Based on the foregoing, we believe that requiring the MSBB (acting in a traditional broker capacity) to judge the fairness of a specific bid received for every bid-wanted, and in certain cases initiate a process with the Retail Dealer prior to the execution of a transaction, which the Retail Dealer would need to then analyze and respond to in writing to complete the process, also prior to the execution of the transaction, is likely to result in fewer of these transactions being executed. And for the reasons set forth above, we believe that this unintended consequence is most likely to impact retail transactions and transactions in thinly-traded securities, which are already among the less liquid parts of the Market.

We also request that the MSRB consider whether the reduction of liquidity in retail orders and thinly-traded securities could have implications beyond the Market. For example, if thinly-traded securities become even harder to trade, would issuers of securities likely to be thinly traded be required to disclose in future offerings how difficult it may be to liquidate a security purchased in the offering? Could similar disclosure become generally required for retail investors purchasing in offerings? If so, what likely impact could the increased illiquidity of these types of positions have on issuers' ability to raise money in the future?

Specific Restrictions on Bid-Wanted

Rule G-43(c) both requires and prohibits certain activities in connection with the conduct of a bid-wanted. We note that, most importantly, this section does not reflect that the Retail Dealer has any ability to direct or restrict the conduct of a bid-wanted in a manner consistent with the Proposed Rule. In order for an MSBB to efficiently serve its Retail Dealer clients, it must be able to conduct the bid-wanted *as directed by the Retail Dealer*. Retail Dealers are in the best position to determine whether specific restrictions on a bid-wanted will have the likely effect of improving the process.

Retail Dealers believe that it is imperative that all bidders in a bid-wanted be treated fairly, and in a consistent manner. However, we believe that the proposed restrictions prohibit communications that are necessary for efficient bid-wanted. For example, Rule G-43(c)(iv) effectively prohibits the MSBB running a bid-wanted from letting bidders know whether they are likely to be used in a bid-wanted. If a bidder knows he is unlikely to be used in a bid-wanted, he can deploy that capital to a different bid-wanted. If not, that capital will necessarily be out of the market until that transaction is concluded. Providing this type of information allows bidders to effectively deploy their capital during the trading

day, to the benefit of the market. We also note that this provision could also be construed to prohibit MSBBs from providing information to potential sellers or bidders about the general nature of the market as they perceive it on a given day (“Market Color”). We believe that such Market Color is important to the efficient operation of the Market. We request that the MSRB specifically consider the effect that this rule provision could have on liquidity in the market.

In addition, Rule G-43(c)(vi) prohibits MSBBs from contacting bidders *even in cases where the MSBB believes that the bid is clearly erroneous* unless the MSBB (i) receives permission from the Retail Dealer selling the bonds, or (ii) notifies its clients in advance that such contacts may be made, and all other bidders are also given the opportunity to adjust their bids. We ask that this provision be reviewed, as we believe it may lead to an increase in transactions based on clearly erroneous bids, as well as unintentionally lead to bidder behavior that would be to the detriment of the seller. Lastly, Rule G-43(c)(vii) prohibits an MSBB from adjusting a bid without the bidder’s written acknowledgement, so that a bidder’s oral instructions are insufficient. We are concerned that if adjusting or correcting bids is subject to a written instruction requirement, bidders may be inclined to simply withdraw their bids rather than remaining in a bid-wanted for which they have submitted an erroneous bid and following procedures to adjust their bids.

Request for Comment Regarding Electronic Trading Systems and MSBBs with Customers

We agree with the position set forth in the SIFMA MSBB Letter that the MSRB’s request for comment regarding more permissive rules for electronic trading systems is anti-competitive. As the primary customers of MSBBs (and other Market trade-execution counterparties), Retail Dealers need multiple venues through which to seek to execute securities transactions. Rules that favor one trading venue over another present the risk that the non-favored venues will become less robust, therefore limiting the options available to the Retail Dealers in the future. For these reasons we believe that there should be no distinctions made in the application of the Proposed Rule, should one be adopted, to any entity that meets the definition of MSBB without regard to the ownership of that entity, or whether that entity is a traditional MSBB, an electronic trading system, or a hybrid of the two.

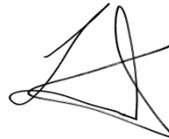
We also agree with the MSRB’s statement that prohibiting MSBBs from having customers might be viewed as anti-competitive, and we do not believe that such a prohibition is warranted. We do believe, however, that MSBBs that have customers should be subject to the same minimum net capital requirements as a municipal securities dealer that has customers (but does not carry customer accounts).

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We wish to thank the MSRB and its staff for their work in developing the Proposed Rule and for this opportunity to comment on it. We would be pleased to discuss any of these comments in greater detail, or to provide any other assistance that would help facilitate your review of the Proposed Rule. If you have any questions, please do not hesitate to contact the undersigned at (212) 313-1130.

Respectfully,

A handwritten signature in black ink, appearing to be 'L. Norwood', written over a faint, light-colored signature line.

Leslie M. Norwood
Managing Director and
Associate General Counsel