Comment on MSRB NOTICE 2013-16 (August 6, 2013)

WHETHER TO REQUIRE DEALERS TO ADOPT A "BEST EXECUTION" STANDARD FOR MUNICIPAL SECURITIES TRANSACTIONS

Thank you for providing this opportunity to convey thoughts about best execution and transparency. Throughout our response we have directly addressed the questions you have raised while concurrently keeping in mind two important goals: 1) design procedures that ensure the best possible prices for buyers; and 2) be certain that well intended procedures do not ultimately have unexpected consequences that are damaging to investors, particularly in the areas of price and liquidity.

1) Would implementation of a best execution requirement help ensure investors receive fair and reasonable prices?

Yes, we believe a best execution requirement would accomplish this; however it is important to take into consideration the type of market, size of order and the liquidity of a particular security. In volatile market environments the value of a particular bond might be significantly different from dealer to dealer. If a dealer is unsure of where a specific credit might trade, the dealer may decline bidding on the item, thereby reducing liquidity and exacerbating wide swings in prices.

2) Are there certain segments of the municipal market or categories of municipal securities for which a best execution requirement would not be appropriate, e.g. transactions in new issues or transactions in variable rate demand obligations?

It would be appropriate to apply 'best execution' to new issue trading because there is a defined period of time in which all buyers would receive the original new issue price (post-sale). This would ensure fair pricing. We have responded to the remainder of the questions but believe it would be very difficult to apply the requirement in the secondary market.

3) Should a best execution requirement apply to all transactions with customers in municipal securities, or should transactions with certain customers, such as sophisticated municipal market professionals (SMMPs) as defined in the interpretation to Rule G-17, on fair dealing, be exempt?

A best execution requirement should *not* apply to dealer to dealer trades. Inter-dealer trades are executed based on current market conditions, inventory positions, and desk limits. It would be beneficial to show the highest bidder, number of bidders, as well as one or two cover bids. Under the new restated SMMP notice (MSRB notice 2012-27) they would not be exempt as it pertains to both recommended and non-recommended transactions.

4) Would implementing a best execution requirement support compliance by dealers with their fair-pricing obligations to customers? If so, how would the existing requirements for fair pricing be helped by the application of a best execution requirement?

It is critical that an industry standard for best execution be developed to give some form of regulatory guidance as to what is considered 'fair and reasonable'. There should be a defined set of guidelines to follow, as well as an outlet, such as an industry contact firms can approach to make inquiries and obtain clarity on what is and isn't permissible in times of market volatility.

5) Do dealers currently follow a 'best execution' plan in connection with the purchase or sale of municipal securities?

Yes, we, have adopted a firm policy that would ensure fair pricing for customers. Trade information is offered on EMMA for all investors to see, and our trading desks maintain documentation of bid wanteds and bid wanted history.

6) Would disclosure that a firm does not utilize a best execution standard be a reasonable alternative to a best execution requirement?

It would be beneficial to disclose a standard on every trade if we are using 'fair and reasonable' pricing.

7) Should there be a minimum number of quotations that must be received in order to support the prevailing market price established by a dealer?

No, this would not be appropriate because some cusips do not trade frequently. Trying to obtain multiple quotes could negatively impact the investor that is in need of liquidity, especially in times of market volatility. It is our experience that in these volatile times a limited number of bids may be available. This does not mean that the bid available is not fair and reasonable, only that it is the only bid available at that time.

The amendment to Rule G-23 implemented on May 27, 2011 that prohibits a broker, dealer, or municipal securities dealer ("dealer") that serves as financial advisor to an issuer for a particular issue sold on either a negotiated or competitive bid basis from switching roles and underwriting the same issue has had the effect of eliminating bids from the market place. We are absolutely convinced that allowing the financial advisor to act in the capacity of underwriter in competitive deals would increase the number of bids and add needed liquidity.

The negative impact of prohibiting financial advisors from bidding on their own competitive issues was strongly illustrated during the market sell off this summer. Liquidity dried up and we saw many instances where only one competitive bid was received for a local issuer. If we, or other financial advisors bringing competitive issues to market, had been allowed to bid, there would have been at least two bids, thereby producing better liquidity and transparency. Issuers were hurt by G-23.

8) If a best execution standard is adopted, how often should the MSRB require that dealers conduct a review of their practices relating to best execution? What factors would be relevant to a determination whether this review should be more or less frequent?

NASD Notice to Members 01-22 "Best Execution" states that at a minimum, firms should conduct reviews on a quarterly basis, but should consider whether more frequent reviews are needed depending on various market conditions that may arise. Using this guideline would have all product areas addressed in the same manner.

9) Should procedures address circumstances under which dealers might seek quotations from:

- **-one or more alternative trading systems?**
- **-one or more broker's brokers?**
- **- one or more affiliates of the dealer's firm?**
- **-the dealer firm's clearing firm?**
- **-dealer firms that participated in the underwriting of the subject municipal securities?**

No, individual dealers should develop procedures on bid wanteds to ensure their customers get the best price. It is not practical to reach out to so many outlets, as some larger firms will not bid items shown on the street.

10) How could a dealer be expected to ensure best execution when selling a municipal security to an investor from the dealer's inventory?

Monitoring EMMA is a useful way to ensure best execution if a security is frequently traded. However, it is important to understand that traders can only work with the information that is available at the time of the trade. For less-frequently traded bonds, we perform our own due diligence to determine where the price should be set. This includes credit analysis, locating a comparable bond, as well as taking into consideration the size of the trade.

11) In the municipal securities market, is it a common practice for customers to direct dealers to solicit bid wanteds from particular dealers, alternative trading systems, or through broker's brokers? If not, should dealers be required to provide these alternatives to customers?

No, because customers are free to choose whichever dealer they wish to use to obtain a bid. It is not common, but if this is requested by a customer, we will accommodate it, and use our best judgment to determine which platform would be most suitable. Currently, there are three or four platforms that are used throughout the marketplace.

12) Do customers inquire as to the methods that dealers employ to determine the prevailing market price for municipal securities?

We do not receive requests directly from customers but occasionally the Financial Consultant may inquire on their behalf.

13) What are the most significant challenges, if any, currently experienced with interpretation and execution of best execution duties for fixed income securities under FINRA Rule 5310?

Limited trading makes it difficult to obtain multiple dealer quotes. Fixed-income securities trade with less frequency and less volume than their equity counterparts. If best execution is required, fewer dealers may make a market for a particular fixed-income security. Given our firm's history and its large number of retail trades, we find there can be a disparity between the retail and the round lot trade details. Documenting 'best execution' for odd lots would be a challenge.

14) Are there alternative methods that the MSRB should consider to provide more transparency to the process dealers employ when determining the prevailing market price for municipal securities in the secondary market that may be more effective for investors and/or less costly or burdensome to dealers? Would a best execution or similar requirement have any negative effect on the protection of investors and the public interest, or on the fair an efficient operation of the municipal market? If so, please describe in detail.

A consolidated platform should be developed (and possibly published on EMMA) to show all bids and covers received on a specific bond on a specific day. Broker's brokers and alternative platforms should be required to provide this to further improve transparency to all participants.

15) What tools do dealers employ to document and preserve diligence undertaken to substantiate the basis of the prevailing market price? What other tools might be needed if a best execution or similar requirement were adopted by the MSRB?

On customer sells, traders review trade price history in EMMA of the issuer's cusip being sold, and make a fair and reasonable bid based upon size, prevailing market conditions, and any current material events that may be relevant to the bond being bid. All this is documented and attached to the trade order ticket. All trade desk offerings reflected on the inventory screens will display any material information that is relevant to the issue being offered, which the FC is to communicate to any customer who may purchase that issue. The FC verifies that these disclosers are made by completing and signing off on a Municipal Bond checklist. A daily internal price variance report is reviewed to determine if any of the current offerings are out of range from the previous 5 day high, low and average price range. A daily executed trade report that displays the trades from the day before and their price differential from the last trade of the day is also reviewed. Any trades that show a price variance of more than 3 points are researched, and reasons for variance are documented, and if deemed necessary, a price correction will occur.

16) If your firm conducts a post-trade internal review of pricing, does it audit all trades, a sampling of trades and what frequency is employed for such review, e.g. daily, weekly, month or on a quarterly basis?

Equity trades are reviewed daily and monthly. This is accomplished by the service of an outside vendor that provides detailed analysis of all trade executions. Fixed Income and Municipals have a sampling of trades reviewed daily to determine if any outlier trades have occurred. This must be done on a manual basis, and at this time, there is no capability to electronically capture all the needed trading data to perform an in-depth analysis. There also is a quarterly manual audit done to review for any possible execution concerns.

17) If your firm conducts a post-trade internal review, how often does it adjust pricing?

During the manual daily trade review, if a trade is flagged as an outlier, the appropriate desk is asked for the supporting documentation for the trade in question. If it is then determined that a price adjustment is necessary, the price correction is processed and the appropriate data that was used to justify the correction is added to the record of the trade.

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