



October 31, 2018

BY ELECTRONIC SUBMISSION

Ronald W. Smith
Corporate Secretary
MSRB
1300 I Street NW, Suite 1000
Washington, DC 20005

Re: Regulatory Notice 2018-22 Request for Comment on Draft Interpretive Guidance on Pennying and Draft Amendments to Exiting Guidance on Best Execution

Dear Mr. Smith,

The following comments are submitted in response to 2018-22. Founded in 1980, Amuni Financial, Inc. (AMUNI) is a full-service broker-dealer specializing in the sale of individual fixed-income securities. AMUNI appreciates the fact that the MSRB is exploring the effects that pennyning (last-looks) has on the market and whether or not existing MSRB rules are outdated.

AMUNI is active in the fixed-income secondary market, and our business is affected by last-looks on a daily basis across all of the major ATSS. In our experience, the practice of utilizing last-looks is prevalent in the market and is most likely to occur en masse when the market experiences periods of low volatility and light supply. When abused, this practice undeniably discourages public quotations as well as limits the amount of traders that are willing to aggressively bid the bid-wanted of firms that embrace "last-look" trading policies.

AMUNI does not believe that the MSRB should create a new rule to prohibit pennyning. In our opinion, it would be more effective to police this issue by enforcing existing MSRB rules while focusing on the most egregious cases of abuse. It is our belief that differentiating between the practices of pennyning in institutional and/or retail order flow is unnecessary and counterproductive due to the negative consequences of doing so in each instance. Also, a "safe harbor" provision giving parameters for pennyning is unworkable due to the vast differences in the business models of municipal market participants. It would be more practical for the MSRB to make clear to all market participants that the practice of last-looks is a last resort used in extreme circumstances and by issuing guidance to dealers on best practices.

Regarding the MSRB's question surrounding "bidding in competition," our traders currently treat every bid-wanted as "in comp" so the designation appears lost on our trading desk and has become a moot point. This has occurred over time and is directly related to the frequency and prevalence of last-looks in the bid-wanted auctions. Traders will gravitate to those platforms and dealers with the best hit-rates and execution regardless of whether or not a bid-wanted is "in-comp."

AMUNI believes that an intent based standard would be impossible to prove because when a bid-wanted is submitted by a firm, there will always be a chance that the bonds will trade depending on market movement and the corresponding bid received. Regarding putting out bid-wanted for price discovery, I would argue that



every bid-wanted could be construed as being placed for price discovery. Isn't price discovery the point of a bid-wanted? You are trying to find the counterparty willing to pay the most for the bond in question. I'm not sure how it could be proven otherwise.

Thank you for the opportunity to comment on this practice. It is our belief that anything limiting competition in the municipal market is detrimental to our customers. There will always be a reason for internalizing, but we believe the MSRB should continue to investigate and give guidance on this practice. By reviewing data collected from the ATSS, as well as the brokers' brokers, the MSRB should be able to give the market guidance on what constitutes a legitimate business reason for this practice.

Sincerely yours,

A handwritten signature in blue ink that reads "M. Petagna".

Mike Petagna

President

Amuni Financial, Inc.

November 13, 2018

Submitted Electronically

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street NW
Washington, DC 20005

RE: Request for Comment on Draft Interpretive Guidance on Pennying and Draft Amendments to Existing Guidance on Best Execution

Dear Mr. Smith:

On behalf of the Bond Dealers of America (“BDA”), I am pleased to submit this letter in response to the MSRB’s Notice 2018-22 (the “Notice”): Request for Comment on Draft Interpretive Guidance on Pennying and Draft Amendments to Existing Guidance on Best Execution. The BDA is the only DC-based group representing the interests of securities dealers and banks exclusively focused on the U.S. fixed income markets. We welcome this opportunity to present our comments.

General Comments

To begin, members of the BDA want to acknowledge that they are familiar with the somewhat common practice of “pennying” as generally defined in the Notice but believe that a narrowing of the definition would benefit the marketplace should the MSRB seek to provide interpretive guidance in this regard. Our members believe that the MSRB is erroneously conflating numerous practices in the municipal securities market under the rubric of “pennying,” and should limit their focus to a singular problematic practice of “pennying” as defined by our members below.

The BDA advises the MSRB to be cautious when considering comments from certain market participants who assert that the “highest bid” on a bid wanted situation should *always* prevail in the sale of municipal securities. There are legitimate reasons regarding why this may not be the most appropriate course of action. For example, dealers often purchase municipal securities following a bid wanted auction because the dealer believes the bids do not accurately reflect a fair price for those municipal securities. For this and other reasons, the BDA believes that it is critical that any MSRB guidance concerning “pennying” narrowly address the specific abusive practice and not attempt in this effort to address the concern of low trade fulfillment rate or overall market liquidity.

Specific Questions regarding “Pennyning”

- *What is “Pennyning”?*

The BDA believes that “pennyning” is the practice and pattern of a dealer to engage in a systematic business strategy to use bids wanteds for price discovery with the intent to purchase the municipal securities at a nominally higher price over the cover bids. We believe that the combination of the bid data and the MSRB trade data clearly identifies which dealers are engaged in this abusive practice as some dealers engage in “pennyning” on a daily basis. Thus, the *intention* of the dealer is inherent to the definition of “pennyning” and it is this practice that is concerning for the market place.

- *Is “pennyning” Common?*

The BDA membership does encounter the practice of “pennyning” (as we define above) frequently and agrees that this practice is troublesome. The BDA supports the efforts of the MSRB to clarify that the practice (as we define it above) is a violation of MSRB Rule G-17.

- *Does “pennyning” impair liquidity in the municipal securities market?*

Although the BDA does not have any empirical data to prove this point, we do believe that “pennyning” may impact the confidence of bidding dealers overall and their willingness to participate in bid wanted auctions. As such, the practice of “pennyning” potentially contributes to low execution or fulfillment rates and thus compromises a successful auction. Most importantly, dealers who engage in “pennyning” frequently impair their ability to fulfill their own customer bid wanted requests as electronic trading platforms often times disclose a dealer’s trade fulfillment rate. Increasingly, the market can identify which dealers consistently engage in “pennyning” and avoid auctions initiated by those dealers. Accordingly, the BDA believes that “pennyning” probably does impact liquidity in the municipal securities market.

- *Does the proposed interpretative guidance appropriately address “pennyning”?*

The BDA supports the MSRB’s efforts in adopting an interpretative release that would address the practice of “pennyning” as we have defined. However, the BDA believes that the proposed interpretative release focuses too much on the use of bids wanted for price discovery purposes and not enough regarding the identified business strategy and practice of a dealer that participates in “pennyning.” Considering the requirements of MSRB Rule G-18, the BDA believes that it could be unclear for market participants if the focus remains on price discovery alone. As discuss above, the bid data and MSRB trade data clearly reveal who may be engaged in this practice and thus any interpretative guidance should be clearly focused on the *systematic* nature of the dealer behavior as an element of “pennyning.”

- *The BDA strongly believes the MSRB should not adopt a rule to prohibit “pennyning”.*

The BDA believes that a release of interpretative guidance under Rule G-17 would be the best vehicle to address this practice. As alluded throughout the Notice, the MSRB is going to be challenged to accurately define “pennyning” in any rulemaking effort. An interpretative guidance

affords the MSRB the ability to identify “pennying” under the fair dealing principles of Rule G-17 and will be thus easier to capture the more qualitative and intent-based elements of “pennying.” The BDA recommends that the MSRB avoids creating a concrete definition of “pennying” as the fact pattern is usually clear when it actually occurs.

- *Should the MSRB provide a safe harbor or some other guidance concerning blind bids by dealers?*

The BDA believes that a safe harbor for dealers bidding in auctions could be helpful if the MSRB makes clear that such safe harbor is not the only option to avoid violating Rule G-17. Many dealers purchase municipal securities following an auction for which they did not participate for altogether legitimate reasons. Often times it is the customer itself that refuses to sell its security at the high bid price resulting from an auction and thus the dealer’s purchase of the security at a nominally higher price is done to accommodate their customer. Therefore, the BDA cautions the MSRB not to discourage these legitimate practices even if they may impact overall trade fulfillment rates. The BDA further recommends the MSRB be clear in guidance that dealers who participate in their own bid auctions and then purchase the security at a nominally higher bid, is not necessarily engaging in “pennying”.

- *What is the appropriate balance between complying with best execution requirements and avoiding “pennying”?*

The BDA believes that the difference between compliance with Rule G-18 and “pennying” comes down to the business approach a dealer takes with respect to the purchase of municipal securities from its customers. Where a dealer routinely uses a bids wanted process to determine in good faith that it is obtaining a favorable price for customers, that is the heart of compliance with Rule G-18. Where a dealer, however, routinely uses a bid wanted process with the *intention* to purchase all of the municipal securities of its customers, or for certain kinds or categories of municipal securities of its customers, the BDA believes that the bids wanted process may merely be a manner by which a dealer can comply with Rule G-18 while still being able to engage in a systematic business strategy of “pennying”. This latter practice the BDA believes is not a legitimate means by which a dealer complies with Rule G-18.

In regard to the second set of questions in the Notice (starting on page 8), the BDA agrees that posting bids wanted on multiple trading platforms is not a necessary component of compliance with MSRB Rule G-18. However, the BDA does believe that there are good and legitimate reasons for a dealer to post bids wanted on multiple trading platforms. Where a dealer may have concerns regarding what kinds of bids it may receive on any given trading platform, a dealer may want more visibility for the bids wanted. Often times, though, the BDA believes that dealers post bids wanted on multiple trading platforms out of a regulatory concern (G-18). Accordingly, the BDA believes that it is important for the MSRB to be very clear that a dealer does not need to post bids wanted on multiple platforms.

* * *

If you or your staff has any questions or need additional information, please do not hesitate contact me directly at 202.204.7901 or mnicholas@bdamerica.org. We look forward to your response.

Sincerely,

A handwritten signature in blue ink that reads "M. Nicholas". The signature is fluid and cursive, with the first name "M." and the last name "Nicholas" clearly legible.

Michael Nicholas
Chief Executive Officer
Bond Dealers of America

Comment on Notice 2018-22

from ROBERT VENTRICE, EMMET & CO.

on Friday, September 14, 2018

Comment:

EMMET & CO HAS EXPERIENCED THIS SITUATION WITH PENNYING. DEALER'S PUTTING OUT BIDS WANTED FOR CUSTOMERS ON PLATFORMS, THEN USING OUR BID TO BUY INTERNALLY. SOMETIMES CHEAPER THAN OUR BID OR PENNY'S HIGHER THAN OUR BID. ANOTHER SITUATION WHERE THIS EXISTS: DEALER'S PUTTING CUSTOMER BONDS OUT FOR THE BID WITH A BROKER AS IN COMP. (THEY RESERVED THE RIGHT TO BID THEMSELVES). PROBLEM IS, THEY DO NOT GIVE THEIR FIRM'S BID TO THE BROKER BEFORE VIEWING HIGH BID FROM BROKER. ANOTHER SITUATION WE HAVE SEEN IS, BIDDING BIDS WANTED AT A HIGHER PRICE AND SEEING THE MSRB TRADE PRINT MUCH CHEAPER. EXAMPLE, WE BID A BOND AT \$103, WE NOTICE A CUSTOMER BUY AT \$101 AND WE DID "NOT" BUY THE BOND. THIS DISCOURAGES US FROM BIDDING NEXT TIME WITH THIS DEALER, IN TURN HURTS THE RETAIL CUSTOMER. THANK YOU.



Hartfield, Titus & Donnelly, LLC.

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Jersey City, NJ 07310
(201) 217-8115

www.HTDonline.com

November 13, 2018

Submitted Electronically via MSRB Portal to:

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board

Dear Mr. Smith,

Hartfield, Titus & Donnelly, LLC (“HTD” or the “Firm”) appreciates the opportunity to respond to MSRB Notice 2018-22, wherein comments were requested concerning draft interpretive guidance related to “pennying” and other existing guidance for best execution obligations; specifically, the practice of posting bid-wanted on multiple platforms to achieve compliance with best execution requirements. HTD is a Municipal Securities Broker’s Broker (MSBB) and, as such, believes that its central role in the municipal bid-wanted marketplace provides the Firm, and other MSBBs, with perspective that should be taken into consideration with the commentary of other market participants who are participating in the MSRB’s request for comments.

Pennying

“Pennying” is defined in Notice 2018-22 as when “the dealer, after reviewing bid information received [from an MSBB conducting a bid-wanted for the dealer], either matches the high bid received in response to the bid-wanted or purchases the bonds at a price that is nominally higher than the high bid.” The MSRB also included “last-look” as another name for “pennying”, however, HTD feels that this is in error being that “last look” is more commonly understood to mean when a MSBB suggests to a bid-wanted bidding participant to revise their bid based on information that is only known to the broker and the selling dealer. This practice is prohibited under MSRB Rule G-43.

As a general matter, HTD would not characterize “pennying” as a prevalent activity. Instances when the dealer that is submitting the bid-wanted is “in competition” with the bid-wanted¹ and is ultimately the high bid for the bonds are not unusual, but are not prevalent either. As the market participant conducting the bid-wanted, an MSBB is uniquely positioned to observe and manage instances where perceived abuses of the bid-wanted process may have occurred. This is not to say that MSBBs should assume a regulatory enforcement roll in this process, but rather, should continue to conduct and manage bid-wanted in a manner that is compliant with MSRB Rule G-43.

Additionally, to the extent that a dealer is using a MSBB to conduct a bid-wanted purely for price discovery, HTD suggests that the MSRB should reiterate its guidance from Rule G-43 which

¹ A practice where the selling dealer is also soliciting bids internally.

prohibits the use of MSBBs solely for price discovery purposes and provide any carve-out guidance where applicable if necessary.

Best Execution

HTD's observation as a MSBB is that there has been a significant increase in the number of bid-wanted that are posted with multiple MSBBs and platforms since the inception of MSRB Rule G-18 ("Best Execution"). It is apparent that there is a misunderstanding among market participants of what constitutes best-execution obligations under Rule G-18. This misunderstanding is causing participants to post what are essentially duplicate bid-wanted solely for the purpose of meeting a misunderstood compliance obligation. The unintended consequence of this misunderstanding is that these duplicate bid-wanted often do not trade (e.g. many bidders do not take these bid-wanted items seriously, or "bidder fatigue") and a false sense of market volume is created.

HTD feels that this can easily be addressed by the MSRB by providing clear guidance to the marketplace that in a bid-wanted auction, every bid is, in fact, a "market" for the purposes of MSRB Rule G-18 and that it is not necessary to put bid-wanted out with multiple MSBBs to satisfy compliance obligations under this rule.

In addition to what is provided herein, HTD is including as an attachment to this letter its responses to the questions provided in MSRB Notice 2018-22 to provide additional context to the Firm's responses concerning these topics.

Sincerely,



Edward J. Smith
Chief Compliance Officer
Hartfield, Titus & Donnelly, LLC



Christopher C. Ferreri
Chief Operating Officer
Hartfield, Titus & Donnelly, LLC

encl.

Request for Comment

The MSRB seeks comment on draft interpretive guidance on pennyning. In considering the draft interpretive guidance, the MSRB invites commenters to consider the following questions. The MSRB particularly welcomes statistical, empirical and other data from commenters that may support their views and/or support or refute the views or assumptions or issues raised in this request for comment.

1. Is pennyning prevalent or uncommon in the municipal securities market?
 - a. As Municipal Securities Broker's Brokers, we wouldn't characterize the activity as prevalent. There are cases when the dealer submitting the bid wanted does bid the bonds and becomes high bid, but anecdotally, we don't think this is widespread.

2. Would bidding dealers bid more often or more aggressively if they were confident that widespread pennyning did not occur in the municipal market or if they were confident that pennyning would not occur in a bid-wanted?
 - a. We collect tens of thousands of Bids in our normal course of business. Many of these bids are received electronically from automated feeds. We have seen a large increase in the number of bids we receive, however we don't believe that the greater quantity produces materially better liquidity. Our brokers communicate with their customers on a regular basis, many time during the day seeking competitive bids for the Bid Wanted we receive. From our perspective, traders bid more aggressively for bonds that they see greater value in. We wouldn't interpret the activity we see as suffering from any pennyning influence.

3. Does the draft interpretive guidance raise any new questions or sufficiently answer the question of what is pennyning? Is more guidance necessary to answer this question? If so, what type of guidance would be valuable?
 - a. It is our view that this activity needs to be monitored by the particular venue and if there is a pattern of behavior which we believe would negatively impact the market, say an increase in the prevalence of pennyning, then we would address that issue with the firm directly. It is our job to operate fair and liquid markets and we have done so for more than 50 years. We would not make decisions to favor any particular customer at the expense of being fair to the broader market.

4. Does the draft interpretive guidance represent the appropriate approach to addressing pennyning in the municipal securities market?
 - a. In our view, yes. We welcome the guidance provided by the MSRB as it is perfectly aligned with our mission; to operate fair, liquid markets. The guidance provides us with a balance of regulatory support for our markets and the flexibility in our approach to evolve.

5. As an alternative to adopting the draft interpretive guidance, should the MSRB instead pursue rulemaking to prohibit pennyng? Why or why not? Are there other alternatives that may achieve the same or greater benefits sought by the MSRB at lower cost or burden?
 - a. It is our view that rulemaking will be less effective than regulatory guidance. We would anticipate much discussion around a clear definition of pennyng which in turn would provide opportunities for participants to find workarounds to specific definitions. Guidance enables market operators to deal with this issue from both a business view and regulatory view.

6. If the dealer bids in competition (the dealer submits a bid as part of the bid-wanted process) and on a blind basis (without knowledge of the other bid prices), should any guidance or rule make clear that pennyng has not occurred in those situations, even if the dealer's best such bid is the same as or only modestly better than the next best bid?
 - a. If a dealer were to submit a bid for the same issues that they are posting a bid wanted for, clearly there could be no assumption of pennyng. This would certainly alleviate any concern, however there are likely many instances where the timing of the bid wanted submission and the submitting dealer's interest in bidding are not simultaneous. Demanding this from the submitting dealer would likely limit better pricing.

7. What are the pros and cons of a dealer using a bid-wanted as opposed to a bid-wanted in competition? Why would a dealer with interest in a bond not distribute a bid-wanted in competition as opposed to distributing a bid-wanted and then purchasing the bond for its account following the end of the bid-collection period?
 - a. There is a wide variety of technical capabilities among the dealer community. Some are highly automated and distribute thousands of bids and bid wanteds on a daily basis. Requiring that the submitting dealer could only bid upon the submission of the bid wanted would likely limit bidding activity. Many, many firms are not fully automated and the process simply is more time-consuming and manual. Again, forcing a dealer to only submit bid wanteds in competition would likely limit their activity.

8. The draft interpretive guidance provides that, depending on the facts and circumstances, the use of bid-wanted (whether distributed via an ATS or broker's broker) solely for price discovery purposes would be an unfair practice within the meaning of Rule G-17, and that the repeated practice of pennyng would be indicative of having the sole purpose of price discovery.
 - a. Is it appropriate to apply an intent-based standard to determine whether pennyng has occurred?
 - i. We think this would be difficult to manage and an imperfect measure of actual intent. In addition, placing the monitoring and enforcement of this standard on

- the market operator, be it a Broker's Broker or ATS may be harmful to the competitive nature of the various market operators.
- b. Is it more appropriate to pursue a bright-line standard?
 - i. In our view, guidance on this issue is preferred to bright-line standards which over time may be subject to change or workarounds.
 - c. Are there instances in which the use of a bid-wanted solely for price discovery should not be deemed an unfair practice within the meaning of Rule G-17?
 - i. We don't believe bid wanteds should be used solely for price discovery.
9. Should the MSRB define what volume or frequency of pennyng would constitute a "repeated practice"? Is guidance necessary on whether a dealer has engaged in a "repeated practice" of pennyng?
 - a. It is our view that the market operators should monitor the bid wanted process and determine if a particular dealer's activity is detrimental to the operation of the market.
10. Given that Rule G-18, on best execution, is an order-handling rule designed to encourage competition, if widespread pennyng discourages dealers from bidding or bidding aggressively, should the MSRB interpret a repeated practice of pennyng as impairing a dealer's ability to meet its best-execution obligations? For example, if a dealer's policies and procedures permit it to engage in a repeated practice of pennyng, should those policies and procedures be viewed as inconsistent with the dealer's best-execution obligations?
 - a. I think we leave this alone as it's a dealer question.
11. Is the process for retail bid-wanted significantly different than the process for institutional bid-wanted (e.g., longer firm times—the length of time for which the bidder must honor the bid provided, use of bid-wanted versus bid-wanted in competition, use of last looks)? Is it significantly different even for similar-size positions? If so, are there reasonable grounds for the difference in process or should they be more alike?
 - a. I would pass on this as well as our business is not retail.
12. Should there be a "safe harbor" under the Rule G-17 interpretation for internalization with a substantial price improvement over the best bid in a bid-wanted? If so, is there an amount that should presumptively be deemed "substantial" price improvement?
 - a. It is our view that the market operators monitor for this behavior based on regulatory guidance rather than firm amounts.

Request for Comment

The MSRB seeks comment on the draft amendments to the implementation guidance on best execution. In considering the draft amendments, the MSRB invites commenters to consider the following questions. The MSRB particularly welcomes statistical, empirical and other data from commenters that may support their views and/or support or refute the views or assumptions or issues raised in this request for comment.

1. Is the practice of posting the same bid-wanted simultaneously on multiple trading platforms prevalent in the municipal securities market?
 - a. We believe it is.

2. Does the posting of the same bid-wanted simultaneously on multiple trading platforms provide dealers with greater access to liquidity?
 - a. To the contrary, we believe that it generates a false view of liquidity.

3. Are there reasons for a dealer to post the same bid-wanted simultaneously on multiple trading platforms other than for the purpose of complying with Rule G-18?
 - a. It is our view that posting to an ATS or a Broker's Broker is posting to multiple participants and should constitute adequate distribution to comply with Rule G-18.

4. Does the posting of the same bid-wanted simultaneously on multiple trading platforms impact dealers' willingness to respond to bid-wanted, and do dealers alter their bidding strategies when responding to bid-wanted that are posted simultaneously on multiple trading platforms?
 - a. We do have anecdotal evidence that this process frustrates dealers' willingness to respond.

5. Does the practice of posting the same bid-wanted simultaneously on multiple trading platforms otherwise have an effect on market liquidity? If the foregoing effects are observed, should the MSRB take any action, such as engaging in rulemaking, to prevent any perceived or observed market harms?
 - a. It is our view that the MSRB's recent guidance on posting to an ATS or Broker's Broker provides adequate distribution. We don't think any further action is required.

6. Does the practice of posting simultaneously on multiple trading platforms occur on the offering side of the market? If so, please comment on its prevalence and impact in response to the above questions as it relates to that side of the market.

- a. We believe that it does, and is being done to satisfy an incorrect interpretation of the Best Execution.
-
- 7. Would the draft amendments, if adopted, create direct, indirect or inadvertent costs or burdens? Is there data or other evidence, including studies or research, that support commenters' cost or burden estimates?
 - a. As market operators we feel it would create a burden on us and unnecessarily increase our regulatory costs.

October 26, 2018

Submitted Electronically

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street, NW, Suite 1000
Washington, D.C. 20005

Re: MSRB Notice 2018-22: Request for Comment on Draft Interpretative Guidance on Pennying

Dear Mr. Smith:

Headlands Tech Global Markets, LLC (“HTGM”) appreciates the opportunity to comment on the Municipal Securities Rulemaking Board’s (“MSRB”) above-referenced notice proposing the draft interpretative guidance on the practice of pennyning, often referred to as last-look (the “Proposal”). We applaud the MSRB’s Proposal as an appropriate first step to curb this prevalent and anti-competitive practice in the municipal bond market. However, even more needs to be done to prohibit abuse of last-look. The MSRB should propose a rule against the use of last-look, except in very limited circumstances.

HTGM is a quantitative trading company that is a Securities and Exchange Commission registered, Financial Industry Regulatory Authority member broker-dealer.¹ HTGM launched its municipal bond trading business in March 2014 and uses proprietary models to price bonds electronically. Over its four plus years in business, HTGM has frequently encountered the practice of last-look, wherein the dealer observes the prices submitted to a completed auction and decides to purchase the bonds from the customer, usually at a price at least equal to or slightly better than the winning bid. HTGM can state with confidence that the practice is prevalent and widespread in the municipal bond market.

HTGM uses information from a variety of sources, including MSRB trade prints and color report data provided by trading venues, to attempt to piece together what happens in a bid-wanted auction when HTGM determines it submitted the winning bid price. For example, over a recent two-week period on one of the largest alternative trading system (“ATS”) platforms, HTGM estimates it received an execution on only 35 percent of the unique auctions in which it submitted the winning bid.² For another 30 percent of those auctions won by HTGM, it appears no trade took place (i.e. there was no trade reported to MSRB). HTGM estimates that the remaining 35 percent of auctions were affected by some version of last-look.

¹ HTGM is a widely-recognized participant in the municipal bond market, executing approximately 1,300 plus trades per day with over 400 counterparties, responding to more than 13,000 bid-wanted auctions per day, and ranking as a top participant on all major municipal bond ATS platforms. This volume makes HTGM a significant liquidity provider and one of the country’s largest dealers in the municipal bond secondary market. HTGM also transacts directly with institutional counterparties and provides direct prices to certain municipal securities dealers.

² As dealers can initiate a bid-wanted auction for the same bond(s) on multiple ATS platforms, HTGM only included auctions that were on a single ATS platform in its analysis.

Specifically, in nearly 18 percent of unique auctions in which HTGM submitted the winning bid, HTGM was *not* the transacting counterparty. Instead, HTGM can only assume the dealer initiating the auction internalized the order as the transaction occurred at an *equivalent or better* price than HTGM's submitted, winning bid (i.e., last-look in practice). Incredibly, in approximately another 17 percent of auctions won by HTGM, not only was HTGM *not* the transacting counterparty, but the transaction occurred at a *worse* price than HTGM's winning price (i.e., last-look in practice).³ This type of behavior happened consistently across all ATS platforms throughout 2018. On one ATS platform alone, HTGM estimates its winning bid has been last-looked or traded through over 4,600 times so far this year.

Importantly, dealers are choosing to use this practice despite the competitiveness of the bid-wanted auction process. On average, HTGM sees at least seven bidders per auction. With such participation, there is no justifiable need for last-look. And the auctions would likely have even more participation if last-look were not being abused by dealers.

The MSRB is correct in the Proposal that last-look harms competitiveness by deterring aggressive pricing and participation by dealers in the bid-wanted process who know the submitting dealer may step in front of their winning bid. Last-look creates a disincentive to "put your best foot forward" or even bid at all. Indeed, other markets have already learned important lessons about the abuse of similar behavior, such as the equities markets in the 1990s and, more recently, the FX markets.⁴

Furthermore, the MSRB has previously expressed concern about last-look in the context of broker's brokers trading in municipal bonds in a December 22, 2012 Notice to Dealers. The MSRB stated therein that the use of last-look by broker's brokers solely for price discovery purposes and not with a bona fide intent to trade harms the bid-wanted and offering processes by reducing bidders, thereby reducing the likelihood that the high bid in a bid-wanted will represent the fair market value of the securities. Despite the 2012 Notice to Dealers, the abuse of last-look in the municipal market did not, as admitted by the MSRB in the Proposal at issue, stop. The practice is still being abused almost six years later.

There have been important strides in the competitiveness and transparency of the municipal bond market, thanks in large part to the enactment of responsible rules. Although the Proposal should assist in furthering these efforts, the only way to ensure the use of last-look does not continue to be abused, is for the MSRB to go a step further than issuing guidance and propose a rule against the use of last-look except in limited circumstances. Requiring a submitting dealer to place its own prices in the competitive auction for bid-wanted with all other participants would put all liquidity providers on equal footing and encourage more frequent and aggressive pricing by auction participants, thereby improving pricing quality for customers. Additionally, it is difficult to comprehend how this requirement would place an unreasonable burden on the submitting dealer.

Accordingly, more concrete expectations and requirements should be established in a proposed rule than those provided for in the Proposal. A rule will give regulators specific guidelines and exceptions to

³ This occurs when a broker-dealer obtains prices for a customer via the bid-wanted auction, but then internalizes the order by purchasing the bond from its customer for its own account at a lower price than the winning bid in the auction. The price differential may result from the submitting broker-dealer including a "desk credit" – essentially a markdown – in the price at which it purchases the bond from its customer.

⁴ See Barboza, David. "30 Firms to Pay \$900 Million in Investor Suit." *NY Times*, 25 Dec. 1997, <https://www.nytimes.com/1997/12/25/business/30-firms-to-pay-900-million-in-investor-suit.html>. Accessed 26 Oct. 2018. See also Teague, Solomon. "Last-look Guidance Felt as Market Prepares for FX Code Deadline." *Euromoney*, 08 Mar. 2018, <https://www.euromoney.com/article/b177kg8nx48plm/last-look-guidance-felt-as-market-prepares-for-fx-code-deadline>. Accessed 26 Oct. 2018.

review and enforce to eliminate any abusive use of this practice. The rule should set the clear expectation that the use of last-look should not be part of the dealer's every day normal business practices but, instead, should occur only in the rare situation when a dealer does not receive a reasonable response to a request for bid-wanted and/or needs to use the practice to conform with best execution responsibilities. The rule should require dealers that want to use last-look in such exceptional circumstances to have clearly written policies and procedures in place as to when it may be used. This gives dealers flexibility to carry out their duties and responsibilities but makes it clear that abuse of the process will not be tolerated. Such rule-making is the only way to guarantee continued progress in the competitiveness and transparency of the municipal bond market.

Thank you for this opportunity to provide our comments. We welcome any questions from the MSRB regarding this important issue.

Sincerely,

A handwritten signature in blue ink that reads "Matthew F. Andresen". The signature is fluid and cursive, with a long horizontal stroke at the end.

Matthew F. Andresen
CEO

Regional Brokers, Inc. (RBI) appreciates the opportunity to respond to Notice 2018-22 issued by the Municipal Securities Rulemaking Board (MSRB) in which the MSRB is requesting comment on draft interpretation guidance related to “pennying” and draft amendments on existing guidance on best execution relating to the posting of bid-wanted on multiple trading platforms. RBI is a Municipal Securities Broker’s Broker (MSBB).

1. Pennying

“Pennying”, as referred to in this request, is the practice by a firm of stepping slightly though the high bid provided by an MSBB in order to keep the bonds “in house”. RBI does not believe that the practice is prevalent, and understands that its counterparties have legitimate reasons for bidding, and keeping, bonds internally (for example, ensuring that their customers receive prices that reflect Best Execution for their bonds).

RBI would suggest that any guidance furnished by the MSRB in this regard should continue to remind firms that they may engage in this practice only when legitimate reasons apply. Firms should look not only to the mandate of Rule G-17, Fair Dealing, but also to previous guidance from Rule G-43, which forbids the “use of broker’s brokers solely for price discovery purposes”.

One other comment that RBI would make regarding this request notice is that the term “last look” be removed from any association with guidance related to pennyning. “Last looks” are already prohibited on the part of MSBBs by MSRB Rule G-43, and while the MSRB has attempted to use the term differently in this case, RBI believes that the inclusion of the term could cause confusion, having already been prohibited elsewhere in the MSRB rules.

2. Best Execution

Historically, any dealer who quoted a bid or asked side for a bond was said to be making a “market” on that bond. When RBI, as an MSBB, places an item out for the bid, it considers each bid to be a market for the bond.

Since the inception of MSRB Rule G-18, “Best Execution”, RBI has seen an increase in the number of items put out for the bid with multiple MSBBs. Firms engaging in this practice have explained to RBI that the Rule, as strictly read, (and despite early guidance from the MSRB) implies that they should do this in order to demonstrate best execution.

MSRB Rule G-18 (a) states that, using certain factors, “a dealer must use reasonable diligence to ascertain the best market for the subject security and buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions”. One of the factors in determining whether a dealer has used reasonable diligence is listed in part (a) (3) of the Rule, “the number of markets checked”.

“Market”, under Supplementary Material .04, is defined as “a variety of different venues, including but not limited to broker’s brokers, alternative trading systems or platforms...”

The inclusion of broker’s brokers and platforms as “venues” therefore implies that if dealers choose to make use of “markets checked” in order to achieve best execution, they should put the bonds out with multiple broker’s brokers.

RBI would request that in any future guidance, the MSRB define each bid received by an MSBB as a “market”, thereby correcting what RBI believes to be the misunderstanding that items should be placed with multiple MSBBs and ATS’s in order to evidence best execution.

Guidance of this sort by the MSRB would be the simplest way to alleviate the issues, real or not, that have arisen around “depth of market”, “bidder fatigue”, and “actual market volume”.

Joseph A. Hemphill III
CEO
Regional Brokers, Inc.

H. Deane Armstrong
CCO
Regional Brokers, Inc.



November 13, 2018

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board

Dear Mr. Smith,

RW Smith & Associates, LLC (“RWS” or the “Firm”) appreciates the opportunity to respond to MSRB Notice 2018-22, wherein comments were requested concerning draft interpretive guidance related to “pennying” and other existing guidance for best execution obligations; specifically, the practice of posting bid-wanted on multiple platforms to achieve compliance with best execution requirements. RWS is a Municipal Securities Broker’s Broker (MSBB) and, as such, believes that its central role in the municipal bid-wanted marketplace provides the Firm, and other MSBBs, with perspective that should be taken into consideration with the commentary of other market participants who are participating in the MSRB’s request for comments.

Pennying

“Pennying” is defined in Notice 2018-22 as when “the dealer, after reviewing bid information received [from an MSBB conducting a bid-wanted for the dealer], either matches the high bid received in response to the bid-wanted or purchases the bonds at a price that is nominally higher than the high bid.” The MSRB also included “last-look” as another name for “pennying”, however, RWS feels that this is in error being that “last look” is more commonly understood to mean when a MSBB gives an opportunity to a bid-wanted bidding participant to revise their bid based on information that is only known to the broker and the selling dealer. This practice is prohibited under MSRB Rule G-43.

As a general matter, RWS would not characterize “pennying” as a prevalent activity. Instances when the dealer that is submitting the bid-wanted is “in competition” with the bid-wanted¹ and is ultimately the high bid for the bonds are not unusual, but are not prevalent either. As the market participant conducting the bid-wanted, an MSBB is uniquely positioned to observe and manage instances where perceived abuses of the bid-wanted process may have occurred. This is not to say that MSBBs should assume a regulatory enforcement roll in this process, but rather, should continue to conduct and manage bid-wanted in a manner that is compliant with MSRB Rule G-43.

Additionally, to the extent that a dealer is using a MSBB to conduct a bid-wanted purely for price discovery, RWS suggests that the MSRB should reiterate its guidance from Rule G-43 which prohibits the use of MSBBs solely for price discovery purposes and provide any carve-out guidance where applicable if necessary.

¹ A practice where the selling dealer is also soliciting bids internally.
RW Smith & Associates, LLC

Best Execution

RWS's observation as a MSBB is that there has been a significant increase in the number of bid-wanted items that are posted with multiple MSBBs and platforms since the inception of MSRB Rule G-18 ("Best Execution"). It is apparent that there is a misunderstanding among market participants of what constitutes best-execution obligations under Rule G-18. This misunderstanding is causing participants to post what are essentially duplicate bid-wanted items solely for the purpose of meeting a misunderstood compliance obligation. The unintended consequence of this misunderstanding is that these duplicate bid-wanted items often do not trade (e.g. many bidders do not take these bid-wanted items seriously, or "bidder fatigue") and a false sense of market volume is created.

RWS feels that this can easily be addressed by the MSRB by providing clear guidance to the marketplace that in a bid-wanted auction, every bid is, in fact, a "market" for the purposes of MSRB Rule G-18 and that it is not necessary to put bid-wanted items out with multiple MSBBs to satisfy compliance obligations under this rule.

In addition to what is provided herein, RWS is including as an attachment to this letter its responses to the questions provided in MSRB Notice 2018-22 to provide additional context to the Firm's responses concerning these topics.

Sincerely,

Denien Rasmussen
Co-Chief Compliance Officer
Chief Operating Officer



Request for Comment

The MSRB seeks comment on draft interpretive guidance on pennyning. In considering the draft interpretive guidance, the MSRB invites commenters to consider the following questions. The MSRB particularly welcomes statistical, empirical and other data from commenters that may support their views and/or support or refute the views or assumptions or issues raised in this request for comment.

1. Is pennyning prevalent or uncommon in the municipal securities market?
 - a. As Municipal Securities Broker's Brokers, we wouldn't characterize the activity as prevalent. There are cases when the dealer submitting the bid wanted does bid the bonds and becomes high bid, but anecdotally, we don't think this is widespread.
2. Would bidding dealers bid more often or more aggressively if they were confident that widespread pennyning did not occur in the municipal market or if they were confident that pennyning would not occur in a bid-wanted?
 - a. We collect tens of thousands of Bids in our normal course of business. Many of these bids are received electronically from automated feeds. We have seen a large increase in the number of bids we receive, however we don't believe that the greater quantity produces materially better liquidity. Our brokers communicate with their customers on a regular basis, many times during the day seeking competitive bids for the Bid Wantedes we receive. From our perspective, traders bid more aggressively for bonds that they see greater value in. We wouldn't interpret the activity we see as suffering from any pennyning influence.
3. Does the draft interpretive guidance raise any new questions or sufficiently answer the question of what is pennyning? Is more guidance necessary to answer this question? If so, what type of guidance would be valuable?
 - a. It is our view that this activity needs to be monitored by the particular venue and if there is a pattern of behavior which we believe would negatively impact the market, say an increase in the prevalence of pennyning, then we would address that issue with the firm directly. It is our job to operate fair and liquid markets and we have done so for more than 33 years. We would not make decisions to favor any particular customer at the expense of being fair to the broader market.
4. Does the draft interpretive guidance represent the appropriate approach to addressing pennyning in the municipal securities market?
 - a. In our view, yes. We welcome the guidance provided by the MSRB as it is perfectly aligned with our mission; to operate fair, liquid markets. The guidance provides us with a balance of regulatory support for our markets and the flexibility in our approach to evolve.

5. As an alternative to adopting the draft interpretive guidance, should the MSRB instead pursue rulemaking to prohibit pennyng? Why or why not? Are there other alternatives that may achieve the same or greater benefits sought by the MSRB at lower cost or burden?
 - a. It is our view that rulemaking will be less effective than regulatory guidance. We would anticipate much discussion around a clear definition of pennyng which in turn would provide opportunities for participants to find workarounds to specific definitions. Guidance enables market operators to deal with this issue from both a business view and regulatory view.

6. If the dealer bids in competition (the dealer submits a bid as part of the bid-wanted process) and on a blind basis (without knowledge of the other bid prices), should any guidance or rule make clear that pennyng has not occurred in those situations, even if the dealer's best such bid is the same as or only modestly better than the next best bid?
 - a. If a dealer were to submit a bid for the same issues that they are posting a bid wanted for, clearly there could be no assumption of pennyng. This would certainly alleviate any concerns, however there are likely many instances where the timing of the bid wanted submission and the submitting dealer's interest in bidding are not simultaneous. Demanding this from the submitting dealer would likely limit better pricing.

7. What are the pros and cons of a dealer using a bid-wanted as opposed to a bid-wanted in competition? Why would a dealer with interest in a bond not distribute a bid-wanted in competition as opposed to distributing a bid-wanted and then purchasing the bond for its account following the end of the bid-collection period?
 - a. There is a wide variety of technical capabilities among the dealer community. Some are highly automated and distribute thousands of bids and bid wanteds on a daily basis. Requiring that the submitting dealer could only bid upon the submission of the bid wanted would likely limit bidding activity. Many firms are not fully automated and the process simply is more time-consuming and manual. Again, forcing a dealer to only submit bid wanteds in competition would likely limit their activity.

8. The draft interpretive guidance provides that, depending on the facts and circumstances, the use of bid-wanted (whether distributed via an ATS or broker's broker) solely for price discovery purposes would be an unfair practice within the meaning of Rule G-17, and that the repeated practice of pennyng would be indicative of having the sole purpose of price discovery.
 - a. Is it appropriate to apply an intent-based standard to determine whether pennyng has occurred?
 - i. We think this would be difficult to manage and an imperfect measure of actual intent. In addition, placing the monitoring and enforcement of this standard on the market operator, be it a Broker's Broker or ATS may be harmful to the competitive nature of the various market operators.
 - b. Is it more appropriate to pursue a bright-line standard?
 - i. In our view, guidance on this issue is preferred to bright-line standards which over time may be subject to change or workarounds.
 - c. Are there instances in which the use of a bid-wanted solely for price discovery should not be deemed an unfair practice within the meaning of Rule G-17?
 - i. We don't believe bid wanteds should be used solely for price discovery.

9. Should the MSRB define what volume or frequency of pennyng would constitute a "repeated practice"? Is guidance necessary on whether a dealer has engaged in a "repeated practice" of pennyng?

- a. It is our view that the market operators should monitor the bid wanted process and determine if a particular dealer's activity is detrimental to the operation of the market.
10. Given that Rule G-18, on best execution, is an order-handling rule designed to encourage competition, if widespread pennyng discourages dealers from bidding or bidding aggressively, should the MSRB interpret a repeated practice of pennyng as impairing a dealer's ability to meet its best-execution obligations? For example, if a dealer's policies and procedures permit it to engage in a repeated practice of pennyng, should those policies and procedures be viewed as inconsistent with the dealer's best-execution obligations?
 - a. This is better answered by a dealer.
11. Is the process for retail bid-wanted significantly different than the process for institutional bid-wanted (e.g., longer firm times—the length of time for which the bidder must honor the bid provided, use of bid-wanted versus bid-wanted in competition, use of last looks)? Is it significantly different even for similar-size positions? If so, are there reasonable grounds for the difference in process or should they be more alike?
 - a. Probably better answered by a dealer.
12. Should there be a "safe harbor" under the Rule G-17 interpretation for internalization with a substantial price improvement over the best bid in a bid-wanted? If so, is there an amount that should presumptively be deemed "substantial" price improvement?
 - a. It is our view that the market operators monitor for this behavior based on regulatory guidance rather than firm amounts.



Request for Comment

The MSRB seeks comment on the draft amendments to the implementation guidance on best execution. In considering the draft amendments, the MSRB invites commenters to consider the following questions. The MSRB particularly welcomes statistical, empirical and other data from commenters that may support their views and/or support or refute the views or assumptions or issues raised in this request for comment.

1. Is the practice of posting the same bid-wanted simultaneously on multiple trading platforms prevalent in the municipal securities market?
 - a. We believe it is.

2. Does the posting of the same bid-wanted simultaneously on multiple trading platforms provide dealers with greater access to liquidity?
 - a. To the contrary, we believe that it generates a false view of liquidity.

3. Are there reasons for a dealer to post the same bid-wanted simultaneously on multiple trading platforms other than for the purpose of complying with Rule G-18?
 - a. It is our view that posting to an ATS or a Broker's Broker is posting to multiple participants and should constitute adequate distribution to comply with Rule G-18.

4. Does the posting of the same bid-wanted simultaneously on multiple trading platforms impact dealers' willingness to respond to bid wanteds, and do dealers alter their bidding strategies when responding to bid-wanted that are posted simultaneously on multiple trading platforms?
 - a. We do have anecdotal evidence that this process frustrates dealers' willingness to respond.

5. Does the practice of posting the same bid-wanted simultaneously on multiple trading platforms otherwise have an effect on market liquidity? If the foregoing effects are observed, should the MSRB take any action, such as engaging in rulemaking, to prevent any perceived or observed market harms?
 - a. It is our view that the MSRB's recent guidance on posting to an ATS or Broker's Broker provides adequate distribution. We don't think any further action is required.

6. Does the practice of posting simultaneously on multiple trading platforms occur on the offering side of the market? If so, please comment on its prevalence and impact in response to the above questions as it relates to that side of the market.
 - a. We believe that it does, and is being done to satisfy an incorrect interpretation of the Best Execution.

7. Would the draft amendments, if adopted, create direct, indirect or inadvertent costs or burdens? Is there data or other evidence, including studies or research, that support commenters' cost or burden estimates?
 - a. As market operators we feel it would create a burden on us and unnecessarily increase our regulatory costs.



November 13, 2018

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street NW
Suite 1000
Washington, DC 20005

Re: MSRB Notice 2018-22: Request for Comment on Draft Interpretive Guidance on Pennying and Draft Amendments to Existing Guidance on Best Execution

Dear Mr. Smith:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ appreciates this opportunity to respond to Notice 2018-22 (the “Notice”)² issued by the Municipal Securities Rulemaking Board (the “MSRB”) in which the MSRB is requesting comment on draft interpretive guidance related to “pennying” and draft amendments to existing guidance on best execution relating to the posting of bid-wanted on multiple trading platforms. On balance, SIFMA appreciates the principles-based approach that the MSRB has taken, however, our members feel additional clarity is necessary.

I. Pennying Interpretive Guidance

a. Definitions

i. Pennying and “Last Look”

In the Notice, the MSRB states that pennying may have harmful effects on the

¹ SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry’s nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. 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 <http://www.sifma.org>.

² MSRB Notice 2018-15 (July 19, 2018).

municipal securities market based upon concerns from “several dealers.” Our members believe this is not a pervasive practice. “Pennyning” may mean different things to different market participants. SIFMA and its members believe that “pennyning” should be defined as the persistent or pattern of internalization of orders for which the dealer internalized at prices that are only nominally better than the cover bids.

SIFMA and its members want to begin this interaction with the MSRB by making clear that a fulsome conversation on this issue cannot be had without clear definitions of pennyning, internalizing, and “last look.”³ In particular, we feel that the draft guidance does not sufficiently answer the question of what is pennyning, and to some extent appears to synonymize “pennyning,” internalization and “last look”. Additional clear guidance on these points would be helpful. Again, SIFMA and its members believe pennyning should be defined as the persistent or pattern of internalization of orders by the dealer, at bid prices that are only nominally better than the cover bids. The determination of what is “nominal” should be based on the facts and circumstances of the credit and the order. Again, it is critical to note that pennyning, internalizing, and last-look are not all the same thing, and clear delineations should be made among these three terms.

ii. Internalization

Internalizing is not in and of itself a problem with respect to liquidity in the municipal securities market. SIFMA and its members are pleased that the MSRB recognizes that not all forms of internalization have negative effects on the market and some may be beneficial to the market. SIFMA and its members agree that internalizing to improve upon the best bid in a bid-wanted, due to the best bid received not resulting in a fair and reasonable price to the customer, is beneficial. SIFMA and its members also agree with the MSRB that when a dealer itself provides the best bid in a blind competition, there is no perceived or actual harm to the market as the winning bidder won pursuant to the terms of the auction.

iii. Nominal Price Improvement

In our view, “nominal” should be defined and determined by a facts and circumstances analysis. Each firm should be able to develop policies, procedures and supervisory procedures that set reasonable parameters for what is a nominal price improvement. SIFMA and its members note that the supplementary material to MSRB Rule G-18, on best execution, sets forth the requirement for periodic review of a firm’s policies and procedures, including the quality of executions of its customer’s

³ The term “last look” has negative connotations in certain contexts, most notably in municipal securities bid rigging cases nearly a decade ago. SIFMA would like to clarify there are different uses of “last look” other than in the context of MSRB G-43 and the prohibition against broker’s brokers giving preferential information to bidders in bid-wanted. Using the term “last look” interchangeably in the MSRB’s guidance would be confusing, particularly without a clear definition, as utilizing a “last look” is not in and of itself problematic so long as it does not result in pennyning as defined herein.

transactions. Through this process required pursuant to MSRB Rule G-18, dealers have a mechanism for reviewing customer executions to which they could add a review for pennyng. We encourage the MSRB consider this mechanism as an efficient potential solution to the concerns stated in the Notice.

b. Price Discovery

As noted above, we believe that pennyng should be defined as the persistent or pattern of internalization of orders by the dealer at prices that are only nominally better than the cover bids. We agree that the use of bid-wanted solely for price discovery purposes by a dealer without any intention to trade if a favorable bid is received may be a violation of a dealer's fair-dealing obligations under MSRB Rule G-17. In the 2013 SIFMA MSRB Rule G-43 Best Practices,⁴ SIFMA highlighted to market participants that the MSRB warned selling dealers that they should not use the bid-wanted process solely for price discovery.

However, there are instances in which the use of a bid-wanted solely for price discovery should not be deemed an unfair practice within the meaning of Rule G-17. For example, a client may not wish to decide whether to place an order until they know the bonds can be sold at a reasonable price. If the client wants to put an item out to bid to try to sell the item if such item can be sold at a reasonable price, the dealer may instigate a bid-wanted to gauge potential liquidity for the customer. Dealers are concerned about any guidance that may create the unintended consequence of limiting the ability of the dealer to service the client's needs or regulatory obligations without the request creating regulatory issues.

c. Changing Market

SIFMA and its members note that the number of bid-wanted responses has been trending higher, in part due to technology and algorithmic trading,⁵ and the proposed guidance may not necessarily have the desired effect. Dealers bid on items fully understanding that they will only buy a very small percentage of items. Some firms feel that a dealer who has posted a bid-wanted improving the bid for the purpose of

⁴ SIFMA Municipal Division MSRB Rule G-43 Best Practices (December 2013), available at: https://www.sifma.org/wp-content/uploads/2017/08/Municipal_MSRB-Rule-G43-SIFMA-Best-Practices.pdf.

⁵ See MSRB Analysis of Municipal Securities Pre-Trade Data from Alternative Trading Systems (October 2018), found at: <http://msrb.org/~media/Files/Resources/Analysis-of-Municipal-Securities-Pre-Trade-Data.ashx?la=en> (“Furthermore, a new breed of market participants—proprietary trading firms that rely upon automated algorithms to trade their own capital—have increasingly occupied a significant space in the municipal securities market. While proprietary trading firms are often registered as broker-dealers, they are not a traditional broker-dealer (or an investment adviser, for that matter), since they only trade their principal accounts without acting as an agent, a dealer or an investment manager for their customers. Proprietary trading firms are naturally heavy users of ATS platforms, as they are drawn to the anonymity and speedy auto-execution features of ATSS to interact with other market participants.”)

internalization does not in any way impact the bidding dealer's decisions on how to bid and when to bid items on the alternative trading system. Price improvement of any kind is widely accepted in other financial markets and used as a measure of performance.

d. Need for Additional Study

Pennyning, as we have defined such term above, is abusive. However, there is only anecdotal evidence that pennyning harms liquidity in the municipal market. Although SIFMA and its members acknowledge the MSRB's concern regarding "bidder fatigue," it is unclear if bidding dealers would bid more often or more aggressively if internalization did not occur. Prior to the finalization of any proposed interpretive notice on pennyning, we believe there should be studies showing the practice hinders liquidity.

II. Best Execution Amendments

SIFMA appreciates the draft amendment to the implementation guidance on best execution. This guidance takes a step in the right direction to clarify the guidance. However, the change may not go far enough. SIFMA and its members suggest changing the "may" to a "does" in the first edit on page 11. This change would make it clear that such multiple postings are not necessary. Also, in the second insertion on page 11, the second use of "may" should be removed to make clear that each dealer constitutes a "market", as that term is broadly defined in paragraph .04 of the Supplementary Material.

Since the original guidance was released, it has become common practice by some dealers in the municipal securities industry to post the same bid-wanted simultaneously on multiple trading platforms. Posting of the same bid-wanted simultaneously on multiple trading platforms provides dealers with marginal, if any, increased access to liquidity. Other than a marginal increase in liquidity, or potentially increased connectivity, posting the same bid-wanted simultaneously on multiple trading platforms largely occurs for MRSB Rule G-18 compliance. The posting of the same bid-wanted simultaneously on multiple trading platforms may impact a dealers' willingness to respond to bid-wanted. Dealers do sometimes alter their bidding strategies when responding to bid-wanted that are posted simultaneously on multiple trading platforms. Depending on the size of the dealer firm and the sophistication of their technology, some firms may have an aggregator, and send the same bid to all trading platforms at once, whereas other firms pick one channel through which to respond. Some firms will not respond. The practice of posting the same bid-wanted simultaneously on multiple trading platforms may have a negative impact on the market, depending on the size of the trade,⁶ by giving market participants a false impression that there are more positions out for bid than there really are, and therefore a false perception of liquidity. However, it is clear

⁶ The impact of this practice is apparent for large trades; the effects of this practice on odd lot trades is insignificant.

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
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that a dealer posting bonds they own or posting a bid-wanted on multiple platforms is not a rule violation.

The offering side of the market is very different than the bid-wanted side of the market. With respect to offerings, the process is much more controlled event though some of the same “noise” exists.

With respect to the draft amendments, we don’t have enough information to determine if any inadvertent costs or burdens would be created, but we don’t believe there would be any such costs or burdens.

IV. Conclusion

SIFMA and its members appreciate this opportunity to comment on the draft interpretive guidance and draft amendments. We would be pleased to discuss any of these comments in greater detail, or to provide any other assistance that would be helpful. If you have any questions, please do not hesitate to contact the undersigned at (212) 313-1130.

Sincerely yours,

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

cc: ***Municipal Securities Rulemaking Board***
Lynnette Kelly, President and Chief Executive Officer
Michael Post, General Counsel
Lanny Schwartz, Chief Regulatory Officer
John Bagley, Chief Market Structure Officer
Leila Barbour, Market Leadership Manager
Saliha Olgun, Associate General Counsel
Carl Tugberk, Assistant General Counsel

Appendix
MSRB Questions on Draft Interpretive Guidance on Pennyning

1. Is pennyning prevalent or uncommon in the municipal securities market?

A: We do not believe that pennyning, as we have defined it, is a pervasive practice.

2. Would bidding dealers bid more often or more aggressively if they were confident that widespread pennyning did not occur in the municipal market or if they were confident that pennyning would not occur in a bid-wanted?

A: There is no clear evidence, and opinions vary.

3. Does the draft interpretive guidance raise any new questions or sufficiently answer the question of what is pennyning? Is more guidance necessary to answer this question? If so, what type of guidance would be valuable?

A: No, we do not believe that the draft interpretive guidance sufficiently addresses the issues, and that further study would be valuable.

4. Does the draft interpretive guidance represent the appropriate approach to addressing pennyning in the municipal securities market?

A: No. Our suggestions are set forth in our attached letter.

5. As an alternative to adopting the draft interpretive guidance, should the MSRB instead pursue rulemaking to prohibit pennyning? Why or why not? Are there other alternatives that may achieve the same or greater benefits sought by the MSRB at lower cost or burden?

A: No, as stated above, we believe the definition of pennyning needs to be clarified and additional study would be helpful.

6. If the dealer bids in competition (the dealer submits a bid as part of the bid-wanted process) and on a blind basis (without knowledge of the other bid prices), should any guidance or rule make clear that pennyning has not occurred in those situations, even if the dealer's best such bid is the same as or only modestly better than the next best bid?

A: Of course. Bids received as part of the bid wanted process, by any dealer, are clearly not pennyning. SIFMA and its members feel that dealer bids in competition and on a blind basis clearly do not constitute pennyning, and any

guidance or rule should make it clear that pennyning has not occurred in those situations. Also, our members feel reviewing the bids received is necessary to check compliance with the fair pricing rule.

7. What are the pros and cons of a dealer using a bid-wanted as opposed to a bid-wanted in competition? Why would a dealer with interest in a bond not distribute a bid-wanted in competition as opposed to distributing a bid-wanted and then purchasing the bond for its account following the end of the bid-collection period?

A: There is no difference.

8. The draft interpretive guidance provides that, depending on the facts and circumstances, the use of bid-wanted (whether distributed via an ATS or broker's broker) solely for price discovery purposes would be an unfair practice within the meaning of Rule G-17, and that the repeated practice of pennyning would be indicative of having the sole purpose of price discovery.

- a. Is it appropriate to apply an intent-based standard to determine whether pennyning has occurred?

A: We believe that our definition of pennyning addresses the MSRB's concerns.

- b. Is it more appropriate to pursue a bright-line standard?

A: No.

- c. Are there instances in which the use of a bid-wanted solely for price discovery should not be deemed an unfair practice within the meaning of Rule G-17?

A: A dealer doesn't know if a customer will sell until the bids come back. The dealer should not be put in a position of having to refuse to put an item out to bid for a client unless the client will definitely sell at any price.

9. Should the MSRB define what volume or frequency of pennyning would constitute a "repeated practice"? Is guidance necessary on whether a dealer has engaged in a "repeated practice" of pennyning?

A: No, a bright line test is not warranted. We have made some suggestions on this issue in our letter.

10. Given that Rule G-18, on best execution, is an order-handling rule designed to encourage competition, if widespread pennyng discourages dealers from bidding or bidding aggressively, should the MSRB interpret a repeated practice of pennyng as impairing a dealer's ability to meet its best-execution obligations? For example, if a dealer's policies and procedures permit it to engage in a repeated practice of pennyng, should those policies and procedures be viewed as inconsistent with the dealer's best-execution obligations?

A: No. As long as SIFMA's definition of pennyng is used, feel that MSRB Rule G-17 is sufficient. Also, the MSRB should not define what volume or frequency of internalization at a nominal amount over the cover bid would constitute a persistent or "repeated practice," rather it should permit dealers to set appropriate policies and procedures based on facts and circumstances.

11. Is the process for retail bid-wanted significantly different than the process for institutional bid-wanted (e.g., longer firm times—the length of time for which the bidder must honor the bid provided, use of bid-wanted versus bid-wanted in competition, use of last looks)? Is it significantly different even for similar-size positions? If so, are there reasonable grounds for the difference in process or should they be more alike?

A: Yes, and there are reasonable grounds for these differences. The process for retail bid-wanted is longer than the process for institutional bid-wanted. The grounds for the difference in processing time is that the markets are different, as is the coverage. It simply is a different and slower market, due in part to the larger number of investors and financial advisors that cover them. Also, by their nature, it may be more difficult to reach a retail client that is not always available, as opposed to an institutional investor. Finally, it is important to note that there is a higher standard of care due to retail investors, so additional time to ensure due care is warranted.

12. Should there be a "safe harbor" under the Rule G-17 interpretation for internalization with a substantial price improvement over the best bid in a bid-wanted? If so, is there an amount that should presumptively be deemed "substantial" price improvement?

A: Yes, SIFMA is in favor of the development of a "safe harbor" under the Rule G-17 interpretation, as long as it is based on a principles-based approach. Internalization with a greater than nominal price improvement over the best bid in a bid-wanted does not meet our definition of pennyng. We do believe that the interpretive notice should be clear that such internalization is permitted, as it is beneficial and not harmful to the market. SIFMA believes there should be no bright line test that demarks where nominal price

improvement ends. Further, there is no set amount that should presumptively be deemed “nominal” or “greater than nominal” price⁷ improvement. Market conditions, current interest rates, the price of the security and the term of the securities are some variables that make setting such a presumptive amount challenging. Again, SIFMA and its members feel that the determination of what is a nominal amount for the purposes of ascertaining whether a broker dealer is pennyng, should be determined by the facts and circumstances.

13. Is there any data that sheds light on the prevalence or impact of pennyng on the market?

A: None that we are aware of.

14. Would the draft interpretive guidance, if adopted, create direct, indirect or inadvertent costs or burdens? Is there data or other evidence, including studies or research, that support commenters’ cost or burden estimates?

A. We are not aware of other evidence of cost or burden estimates.

⁷ We note that we focus on the term “nominal.” In our view, there is a range of prices between nominal price improvement and potentially substantial price improvement.

November 14, 2018

Submitted Electronically

Ronald W. Smith
Corporate Secretary
MSRB
1300 I Street NW
Washington, D.C. 20005

Re: Request for Comment on Draft Interpretive Guidance on Pennyning and Draft Amendments to Existing Guidance on Best Execution

Dear Mr. Smith:

TMC Bonds ("TMC") is pleased to present its comments, with respect to "Interpretive Guidance on Pennyning and Draft Amendments to Existing Guidance on Best Execution."¹ TMC Bonds is a registered Alternative Trading System ("ATS"), that was recently acquired by the Intercontinental Exchange that has been conducting Bids Wanted ("BW") auctions for the past 18 years on behalf of its users in municipal securities as well as other asset classes on an anonymous basis. TMC runs approximately 4,500 daily municipal BW auctions.

The Municipal Markets Would Benefit from Additional Clarity on Pennyning

The proliferation and use of multiple venues to run BWs has introduced valuable competition into the marketplace, but has also led to a lack of transparency in auction methodology and a diminished ability to detect market practices.

Our TMC user feedback regarding concerns of "last-looks" or "pennyning" supports the idea that greater transparency and control of the TMC auction process, including guidance around pennyning practices, would promote fair and competitive markets.

To help frame the magnitude of potential "last looks" or "pennyning", TMC conducted a study of its municipal BW auctions for the month of January 2018. TMC had for the bid approximately 96,000 items of which 22% traded. Of the executed BWs, only 524 (.5%) had prices entered by the requestor after the Bid-by time, indicating that requestors utilizing the application were not systematically viewing auction results before entering their bids, as Firm-Time BW bids are not viewable until after the collection period. TMC believes that post collection period bids should be allowed for various administrative reasons, but not allowed for non-competitive market purposes.

However, as there is no requirement for a requestor to enter a bid in the auction, the auction results could have been used by requestor to trade away from the platform. To assess the magnitude of this,

¹ <http://msrb.org/~media/Files/Regulatory-Notices/RFCs/2018-22.ashx??n=1>

possibility, TMC examined the MSRB price feed for matched trades that occurred after the item was for the bid where there was a single dealer buy reported from the customer. Approximately 5.2% of the auctions that did not trade on TMC had a subsequent purchase from the customer with no corresponding dealer trade as reported by the MSRB. Because the requestor's bids were not known, there was no transparency as to how or when the requestors' bids were determined.

Additionally, a number of RFQ's TMC has for the bid traded away from the platform. A number of these trades were reported as dealer to dealer trades giving the appearance of a trade lost to a competitor, but in actuality these are really not trade aways, but "stock" trades as certain dealers settle transactions via intra-company transfers which results in an extra dealer trade report to the MSRB. This type of delivery unintentionally masks the universe of potential "penneyed" transactions as the "away from market" indicator is seldom observed by the market. An in-competition bid would help instill the integrity of the auction process as firms would know the full stack of bids.

There has been some discussion by industry participants that if a last-look price improvement was sufficient, then "penning" did not occur. TMC believes the use of the term "penning" fosters this belief and should be sufficiently defined as to discourage systematic use of auction results to improve a dealer's own bid for non-competitive use. For context, TMC examined the variance of the reported trade price to the BW auction's high bid as a barometer of possible penning. 47% of the time, the improved price to the customer was less than \$1.00/bond better than TMC's high bid. Again, while there are reasonable scenarios where this would be acceptable, these types of occurrences leave a bad taste with liquidity providers. Furthermore, systematic price improvement of prices by a greater amount can also affect the integrity of the auction process. A requirement for in-comp bids would help eliminate the potential conflict and provide the market with greater confidence of fair dealing.

Approximately 19% of the items TMC had for the bid traded away from TMC to other dealers. This highlights the fact that many of TMC's BW's are being placed on multiple venues including broker's brokers. The use of multiple vendors may foster a sense of market uncertainty as there is not a centralized auction book. Differences in fee schedule and whether the price maker or taker results in different rankings of bid stacks between vendors. For example, some vendor's bill monthly versus time of trade and/or may charge the bidder versus the seller. As multiple auction venues may be involved, it's difficult for both a dealer and auction agent to ascertain a comprehensive view of the results.

Best Execution is Negatively Impacted by Posting BWs on Multiple Trading Platforms

As both the growth in electronic trading and the requirements of Best Execution (G-18), have encouraged market participants to utilize efficient means for exposing Request for Quotes (RFQs) to the market, ATSS have played a significant role in helping firms receive competitive pricing for their clients. The proliferation of items available for the bid has also opened the door for new types of players to enter the market, such as "Algos", who stand ready to commit their capital as market makers. On a typical day, TMC will manage 4,500 BW items and receive approximately 5.38 bids per item, a combination of both trader and machine algo bidding. It is not unusual to have a double digit number of bids on more liquid names.

As both the process by which most firms solicit RFQs has changed and the number of markets checked have increased, there are a number of consequences that have constrained the optimal functioning of the

market and impaired the ability to efficiently process the volume of RFQs. First, dealers are now placing RFQ's out on multiple trading venues whereas historically there was only one auction agent. This evolution has, in turn, resulted in a proliferation of BW's as most dealers' feel compelled to gain as much exposure for the client RFQ as possible in order to comply with MSRB Rule G-18. For market makers, this practice of posting on multiple venues both ties up capital and creates unnecessary market noise as the manual (i.e. non-algorithmic) bidders attempt to sift through thousands of duplicate BW items, unsure if the BW was a duplicate or a unique item. While the MSRB has pointed out in past guidance letters such "Implementation Guidance on the MSRB-G18, on Best Execution" dated November 15, 2015, "there may be facts and circumstances under which it may be sufficient for a dealer to check only one such market and satisfy the best-execution obligation", the language is sufficiently vague which encourages dealers to cover their obligation via multiple postings.

Mandating the in-comp bid Would Improve Market Efficiency

Furthermore, the posting of an RFQ on multiple venues, and the corresponding loss of the auction agent knowing the RFQ seeker's bid, have fostered a sense of unfair dealing as other bidders do not feel they are competing on a level playing field. This loss of process by the auction agent results in participants either not bidding or placing a weaker bid than they otherwise would. In the voice-brokerage methodology, a broker would not release the bid to the dealer until the requesting dealer provided its bid. This protocol ensured that all participants were treated fairly and enabled the broker to properly monitor the bidding. TMC supports the MSRB mandating the in-comp bid and believes it would improve market efficiency on a number of fronts. First, market participants would know that all bidders would be subject to the same auction terms, which would foster a more competitive marketplace. Second, the in-comp bid would help regulators monitor auctions whereby patterns of systematic abuse for either pricing purposes (or "pennying") could be more readily identified. TMC believes that firms should have the ability to "last-look" as there are numerous examples where it is necessary. For example, the customer requests price improvement. Third, by having the in-comp bid, auction agents would have the ability to notify participants if their capital is being committed as firms who are not high bid, could be released from the BW auction during the firm time. This adjusted BW auction process would encourage the deployment of non-committed capital to other RFQs.

In mandating the in-comp bid, the MSRB would encourage a more competitive auction process. As questioned in the MSRB's Request for Comment, the MSRB would not have to mandate in-comp BW's with close second bids ("cover") that "pennying" did not occur as the existing G-43 guidelines require brokers to run a fair process and not allow late bids. An alternative to this interpretation would be for auctions with around-times where the RFQ requestor is able to see bids during the collection period. Under an around-time BW, the bid stack would be consistently viewable by the dealer and thus potentially influence its bid. Under a firm-time BW, a dealer checking multiple venues would essentially be collecting multiple bids just like a broker's broker, but with the discretion to use the stack. The MSRB may consider that, for the "around-time" auctions, the requestor would need to submit its bid with the initial request. Furthermore, it seems nonsensical that, according to G-43(c)(i)(F) a broker's broker must make a decision to notify the bidder/seller of the quality of a quote only versus predetermined parameters, but a dealer functioning in the same capacity when collecting from multiple venues, may use the auction data to change its own price, but is not under the same obligation of using pre-determined parameters. Harmonization between these ideas may improve the integrity of the process.

Lastly, the use of requestor scorecards (conversion ratios) to assist bidders in ascertaining the likelihood of a particular item trading has resulted in mixed outcomes. While the metric helps bidders decide how to prioritize their time when deciding which items to bid, it may result in less than favorable outcomes for requestors with below average scores. As bidders are more likely to focus on bonds that are expected to trade, a firm with a low ratio will not necessarily see the same number or quality of bids, ceteris paribus, as a highly rated participant. This results in a bifurcated market where orders are exposed to the same marketplace, but treated differently. Whereas the requestor with low conversion ratio might receive a reasonable price, the retail customer may have not have gotten the best price. If a firm has artificially low conversion ratios due to their tendency to trade internally, then providing the in-comp bid to the auction agent will raise the firm's standing and thereby benefit its clients.

TMC greatly appreciates the MSRB proactively soliciting comments in this area and welcomes the opportunity for any further discussion.

Thomas S. Vales
Chief Executive Officer
TMC Bonds LLC
New York, NY