

MEMO# 27913

February 26, 2014

MSRB Proposes New Best Execution Rule; Member Call Scheduled for Wednesday, March 5

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TO: MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 3-14 RE: MSRB PROPOSES NEW BEST EXECUTION RULE; MEMBER CALL SCHEDULED FOR WEDNESDAY, MARCH 5

The MSRB has requested public comment on a proposal to establish for the first time explicit requirements for municipal securities dealers to seek the most favorable price possible when executing transactions for retail investors. [1] The proposed rule is modeled after FINRA's best-execution rule for equity and non-municipal fixed income securities, but tailored to the municipal securities market. Comments on the proposal are due on or before March 21, 2014.

We have scheduled a brief member call to discuss the proposal on Wednesday, March 5 at 3:00 pm Eastern time. If you would like to participate on the call, please contact Jennifer Odom at jodom@ici.org or 202-325-5833.

In August 2013, the MSRB published a concept proposal on best execution requesting comment on whether a new MSRB rule should apply best-execution concepts to the municipal securities market. [2] The concept proposal specifically asked whether a best-execution requirement would effectively buttress existing MSRB fair-pricing obligations. After considering the comments submitted in response to the concept proposal, the MSRB has determined to propose a best-execution rule that is generally harmonized with FINRA Rule 5310 but tailored to the characteristics of the municipal securities market. The MSRB also has determined to propose an exception from the best-execution rule for all transactions with sophisticated municipal market professionals (SMMPs). The Release explains that while the objective of proposed Rule G-18 would be to provide a customer with a price that is as favorable as possible under prevailing market conditions, the best-execution requirement generally would target the process by which dealers handle orders and execute transactions, and would complement and buttress the MSRB's existing fair-pricing rules.

Proposed Rule G-18 would require that, like FINRA Rule 5310, dealers use reasonable

diligence in seeking to obtain for their customer transactions the most favorable terms available under prevailing market conditions. Under Rule proposed G-18, dealers are required to use reasonable diligence in informing themselves of the most favorable terms available, among the variety of markets in which a securities transaction could be executed, and then execute the transaction in the best market to provide the most favorable price possible to the customers. Proposed Rule G-18 includes particular rule language and supplementary material designed to tailor best-execution obligations to the characteristics of the municipal securities market and to provide guidance on how best-execution concepts apply to municipal securities transactions. This tailoring includes accommodations for situations involving less availability of quotations and relevant pricing information, the role of broker's brokers in providing liquidity, the role of dealers' inventories in providing liquidity, the variance in the nature of dealers' municipal securities business, and the lack of standardized and publicly reported statistical data regarding the quality of executions of municipal securities transactions.

In conjunction with the proposal, the MSRB is seeking comment on an exception (proposed changes to Rule G-48) from the new best-execution rule for transactions with SMMPs. According to the MSRB, this proposed exception follows a similar approach to fair-pricing obligations under existing MSRB rules, on the grounds that imposing additional execution requirements on dealers in transactions with such well-informed and sophisticated investors may not be necessary.

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endnotes

[1] Request for Comment on Draft Best-Execution Rules, Including Exception for Transactions with Sophisticated Municipal Market Professionals, MSRB Notice 2014-02 (February 19, 2014) ("Release"), available at <http://www.msrb.org/~media/Files/Regulatory-Notices/RFCs/2014-02.ashx?n=1>.

[2] Request for Comment on Whether to Require Dealers to Adopt a "Best Execution" Standard for Municipal Securities Transactions, MSRB Notice 2013-16 (August 6, 2013), available at <http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2013/2013-16.aspx>.

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