sifma
Invested in America

March 2, 2017

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: SR-MSRB-2017-01: Notice of Filing of a Proposed Rule Change To Add New MSRB Rule G–49, on Transactions Below the Minimum Denomination of an Issue, to the Rules of the MSRB, and To Rescind Paragraph (f), on Minimum Denominations, From MSRB Rule G–15

Dear Mr. Fields:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates this opportunity to respond to the Municipal Securities Rulemaking Board's (the "MSRB's") proposed addition of new MSRB Rule G-49 on transactions below the minimum denomination of an issue, as filed with the Securities and Exchange Commission (the "SEC").[2] As stated in our prior letters to the MSRB[3] on the amendments at issue in the Filing, SIFMA and its members support the original intent of the rule which has been stated by the MSRB as seeking to protect investors that own municipal securities in amounts below the

[1] SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over $2.5 trillion for businesses and municipalities in the U.S., serving clients with over $20 trillion in assets and managing more than $67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. 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] 82 Fed. Reg. 10123 (Feb. 9, 2017) (the "Filing").

[3] *See* letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA, to Ronald W. Smith, Corporate Secretary, MSRB, dated May 25, 2016 (regarding MSRB Notice 2016-13 (April 7, 2016) (the "Original Notice")) (the "First SIFMA Letter") and letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA, to Ronald W. Smith, Corporate Secretary, MSRB, dated October 18, 2016 (regarding MSRB Notice 2016-23 (September 27, 2016) (the "Second Notice")) (the "Second SIFMA Letter", and together with the First SIFMA Letter, the "Prior SIFMA Letters").

minimum denomination. However, SIFMA is disappointed in the recent amendments to the draft rule and feels strongly that the amendments to the draft rule do not serve their stated purpose. To the contrary, SIFMA members feel the amendments as drafted negatively impact investors. In this letter, we will explain and illustrate our concern with the proposed rule, and suggest alternative language.

I. Suitability and Liquidity Related to Below-Minimum Denomination Positions

The MSRB's goals can be effectively achieved by making consideration of liquidity, as a result of a below-minimum denomination position, part of the Rule G-19 analysis. The MSRB appears to presume that below-minimum denomination positions are not suitable for any investors. On the contrary, below-minimum denomination positions may be suitable for investors that find the price attractive for the relative risk, and are not concerned about the potential lack of liquidity in the position. Assuming consideration of the liquidity of a below-minimum denomination position is handled in Rule G-19, there would be no need for Rule G-49 other than with respect to confirmation disclosure, a matter that would be best addressed in Rule G-15.

II. Causes of Below-Minimum Denomination Positions

As stated in the Prior SIFMA Letters, there are many scenarios that could cause a customer's position to fall below the minimum denomination. A below-minimum denomination position may be created by a number of events including, corporate actions (optional redemptions (e.g., pro rata redemptions), sinking fund payments, etc.), allocations by investment advisors, the division of an estate as a result of a death or divorce, and by court order.[4] These are some of the reasons positions exist below the minimum denomination, and the investor should not be penalized for the creation of a below-minimum denomination position that is out of their control. SIFMA is concerned about the liquidity impact of the proposal, because, when the liquidity of below-minimum denomination positions is hampered, the end investor is the one penalized.

III. Interdealer Limitation Should Be Removed

SIFMA and its members feel strongly that Rule G-49(c), which limits interdealer transactions, should be deleted. Again, the purpose of the rule is to prohibit dealers from effecting transactions with ***customers*** in amounts below the

[4] Securities Exchange Act Release No. 45174, Notice of Filing of Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Minimum Denominations (December 19, 2001), 66 FR 67342 (December 28, 2001), at fn 3.

minimum denomination – with certain exceptions without creating an additional number of below-minimum denomination positions. With that in mind, Rule G-49(c), which limits interdealer transactions, is unwarranted, harms liquidity and is inconsistent with the original customer protection purpose of the rule. Dealers should be permitted to trade below-minimum denomination positions and sell such a position to another dealer who would then be able to, in accordance with the exemption, sell such position to a customer to add to a customer's existing below-minimum denomination position. In light of today's automated trading environment, we strongly prefer not to produce the liquidation statements, as it hinders transfers of these positions on alternative trading systems and through interdealer brokers. The benefits of the elimination of the liquidation statement, however, are completely outweighed by the negative impacts of limiting interdealer transactions. If it would help remove some of the MSRB's concerns, SIFMA and its members would prefer the elimination of G-49(c), even if the consequence was liquidation statements would need to be produced.

IV. Timing of Sales

The exception in Rule G-49 (b)(ii)(B) and interdealer limitation in Rule G-49(c) create timing concerns. Under Rule G-49 (b)(ii)(B), a dealer is permitted to break up a below-minimum denomination block to sell to a customer that already has a below-minimum denomination block. The dealer may then sell any remaining portion of the below minimum denomination position to one or more customers that already have a position in the issue. But what if the dealer doesn't have any other customers at the time that are interested and valid purchasers of such below-minimum denomination positions? If the dealer doesn't sell the remaining position to one or more customers at the time of the sale to the first customer, and the dealer then is prohibited from selling the bonds the remainder to another dealer pursuant to Rule G-49(c), then the dealer is stuck with the orphan remainder until and unless they find another customer to whom to sell the remainder. SIFMA members feel that this prohibition unnecessarily hampers liquidity in these below-minimum denomination positions.

V. It Should be Clarified that A Dealer's Ability to Sell Securities Under the Exemption Is Not Different Based on the Source of Bonds

SIFMA and its members feel strongly that the exceptions in new Rule G-49 (b)(ii) should apply regardless of whether the dealer acquired the bonds from a customer or in an inter-dealer transaction. The current draft of the rule is unclear and can be interpreted different ways. It concerns us that one potential reading of the rule prohibits breaking up the below-minimum denomination position if the position is acquired from a customer, but permits breaking up the position if

acquired from a dealer. It stands to reason that Rule G-49(b)(ii)(A) and (B) should apply irrespective of the source of the bonds.

SIFMA reiterates that if the MSRB's intent is to limit this exception to positions acquired from dealers, the MSRB is effectively limiting liquidity for customers that have below-minimum denomination positions. SIFMA and its members see no reason why there should be a prohibition on dealers selling the below-minimum denomination position to more than one customer if the position is acquired from a customer. We believe that Rule G-49(b)(ii)(A) and (B) should both be available to dealers, regardless of whether the bonds were purchased from a customer or a dealer. Again, the source of the bonds should not matter in this instance, as that fact has no impact on whether additional below-minimum denomination pieces are being created. SIFMA and its members feel the rule would be more clear if Rule G-49(b)(ii)(B) was applied without regard to the source of the securities.

If it is not the MSRB's intent to distinguish between securities acquired from a customer and those acquired from a dealer, the language below might provide some clarification. SIFMA and its members propose the following two alternatives to clarify Rule G-49(b)(ii) as follows: I

> Alternative 1: (ii) The prohibition in section (a) of this rule shall not apply to the sale of securities to a customer in an amount below the minimum denomination, provided ~~that the below-minimum denomination position being sold is the same amount as the below-minimum denomination position~~ that the dealer acquired the below-minimum denomination position from a customer in a transaction where such customer fully liquidated its position in the security, as described in section (b)(i) of this rule and the amount being sold under paragraph (A) or, in the aggregate, under paragraph (B), of this subsection is the same amount as the below-minimum denomination position acquired by the dealer; or, the below minimum denomination position being sold was acquired by the dealer in an inter-dealer transaction and the amount being sold under paragraph (A) or, in the aggregate, under paragraph (B), of this subsection is the same amount as the below-minimum denomination position that the dealer acquired in the inter-dealer transaction.
>
> In effecting ~~such~~ a sale to a customer pursuant to this subsection (ii) in an amount below the minimum denomination, the dealer may:
>
> > (A) Sell the entire below-minimum denomination position to one customer; or

> (B) Sell the entire, or a portion of, the below-minimum denomination position to one or more customers that have a position in the issue and any remainder to a maximum of one customer that does not have a position in the issue, even if the transaction(s) do not result in a customer increasing its position to an amount at or above the minimum denomination.

or

> Alternative 2: (ii) The prohibition in section (a) of this rule shall not apply to the sale of securities to a customer in an amount below the minimum denomination, provided that the below-minimum denomination position being sold was ~~is the same amount as the below-minimum denomination position that the dealer~~ acquired by the dealer either from a customer in a transaction where such customer fully liquidated its position in the security, as described in section (b)(i) of this rule~~;~~ or~~,the below-minimum denomination position being sold was acquired by the dealer~~ in an inter-dealer transaction, and in either of the above cases the amount being sold under paragraph (A) or, in the aggregate, under paragraph (B), of this subsection is the same amount as the below-minimum denomination position that the dealer so acquired ~~in the inter-dealer transaction~~.
>
> In effecting such a sale to a customer in an amount below the minimum denomination, the dealer may:
>
> (A) Sell the entire below-minimum denomination position to one customer; or
>
> (B) Sell the entire, or a portion of, the below-minimum denomination position to one or more customers that have a position in the issue and any remainder to a maximum of one customer that does not have a position in the issue, even if the transaction(s) do not result in a customer increasing its position to an amount at or above the minimum denomination.

In response to the Prior SIFMA Letters, the second additional dealer sale exception in the prior draft Rule G-49(b)(iii) was removed, however, Rule G-49 (b)(ii) was not amended. The language that was removed read as follows:

> (iii) The prohibition in section (a) of this rule shall not apply to a sale of securities to a customer in an amount below the minimum denomination if the customer already has a position in the issue below the minimum denomination and the sale will result in the

> customer having a position at or above the minimum denomination. The dealer may then sell any remaining portion of the below-minimum denomination position to one or more customers that already have a position in the issue.

We ask that this language from Rule G-49(b)(iii) in the Second Notice be restored if Rule G-49 (b)(ii) remains unchanged.

VI. Examples

SIFMA's comments to the MSRB in the Prior SIFMA Letters were largely dismissed as potentially creating additional below minimum denomination positions. The examples below illustrate concretely that the clarifications SIFMA seeks would potentially reduce the number of positions that are below the minimum denominations.

> Example 1. Firm A's Customer 1 owns $75,000 of a bond with a $100,000 minimum denomination. Firm A can sell all of the $75,000 to another dealer. There is one position that is below the minimum denomination.
>
> Example 2. Another customer of Firm A, Customer 2, has $50,000 and wants another $50,000. It is unclear under the proposed rule whether Firm A can break up the $75,000 it acquired from Customer 1 in Example 1 to sell Customer 2 $50,000. There is language that suggests that Firm A cannot execute this transaction under the new rule, so there remain two positions below the minimum denomination: Customer 1's $75,000 position and Customer 2's $50,000 position. We feel the rule should be clarified to make clear that Firm A is permitted to execute this transaction, as it would reduce the number of below minimum denomination positions to one, as Customer 1's position at Firm A would be $25,000 and Customer's 2 position would then be at the minimum denomination of $100,000.

Example 3. Firm A acquires $50,000 from Firm B. Firm A can sell $50,000 to its customer that wants $50,000 or sell the $50,000 it acquired from Firm B to another dealer.

Example 4. Firm A acquires $50,000 from Firm B. There is one below minimum denomination position. Firm A can sell $25,000 to a customer who already owns some of the security. If no other Firm A customers want the remaining $25,000, under one potential reading of the rule, Firm A is stuck with that orphan position and there is still one position below the minimum denomination. Under another potential reading of the draft rule, Firm A would be able to sell the remaining $25,000 to another one of its customers. It cannot be sold to another dealer, even if that other dealer is looking for the $25,000 to get one of its customers up to the minimum. If Firm A were permitted to sell the position to another dealer, then there could be zero below minimum denomination positions.

Example 5. Customer 1 purchases a $200,000 position in a security that has a $100,000 minimum denomination, and a $100,000 increment thereafter. Due to a corporate action or some other reason, Customer 1 now has a $145,000 position in the security. Customer 2 of Firm A will buy a $100,000 position, but then Firm A will be stuck with a $45,000 orphan position and there will still only be one non-conforming position if the draft rule is interpreted most restrictively. It cannot be sold to another dealer, even if that other dealer is looking for the $45,000 position to get one of its customers up to the minimum, add to their position, or looking for a good deal. If Firm A were permitted to sell the position to another dealer, then there could be zero below minimum denomination positions. If Firm A is not permitted to sell the position to another dealer, Firm A is unlikely to accommodate Customer 1 in order to avoid being stuck with an orphan position.

VII. Access to Accurate Information

SIFMA reiterates its concerns that the accuracy and validity of minimum denomination data available continues to be a significant compliance issue. Many information service providers have blank or incorrect information in the minimum denomination field. Additionally, some private placement memorandum ("PPM")

documents are not on the MSRB's Electronic Municipal Market Access ("EMMA") website, so there is no way for the dealer to check for the minimum denomination information on that particular transaction. To remedy this issue, we renew our request for MSRB Rule G-32 be amended to require the filing of minimum denomination information on EMMA on all transactions.

Again, expecting traders to look up minimum denomination information in an Official Statement or PPM prior to making a trade is not efficient or realistic. Underwriting dealers are already required to send to the Depository Trust and Clearing Corporation ("DTCC") minimum denomination and increment information though the New Issue Information Dissemination System ("NIIDS") by mandate of Rule G-34. However, information service providers are not necessarily picking up this information from NIIDS. We strongly encourage the MSRB to take the minimum denomination information that underwriters already provide via the DTCC's NIIDS feed and display the information on EMMA, denoting that the field indicates authorized minimum denominations as of the time of issuance. If a security is not NIIDS eligible, then the dealer should be able to send the information directly to the MSRB for transparency purposes on EMMA. These modest improvements to EMMA to increase the transparency of minimum denomination information would greatly assist investors and regulated dealers alike, in furtherance of the MSRB's stated mission.

VIII. Additional Request for Clarity

SIFMA's members would appreciate clarity in the MSRB Rules for the following example:

> Example 6. Customer 1 has 2 accounts with Firm A in a security that has a $5,000 minimum denomination. Customer 1 initially purchases two $5,000 positions, one for each account. Due to a corporate action or some other reason, one account now has $3,000 and the other account now has $2,000 of the security. Can Customer 1 liquidate $3,000, as it is the entire position in one account? SIFMA feels strongly that there is no ability to easily aggregate across accounts, and that this transaction should be permitted. Does it change the answer if the accounts have different beneficiaries (such as each of the customer's children) or other characteristics? How is "entire position" defined under Rule G-49?

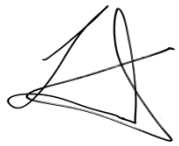
> Example 7. Dealer A owns $200,000 of a municipal security with minimum denomination of $100,000 and $50,000 increments. Customer 1 wants to purchase $150,000, and Customer 2, who currently owns $150,000 of the bonds, is willing to buy the remaining $50,000. Under G-15 as currently constructed and under proposed G-49, there are concerns that Dealer A would not be able to sell the $50,000 to Customer 2 since the $50,000 did not originate from a transaction where Dealer A purchased from a customer in a full liquidation. However, if Rule G-49 was clarified to clearly permit this transaction, there would be no adverse liquidity impact to either Customer 1 or Customer 2 since both would own above minimum positions as a result. In fact, Customer 1 is harmed because Dealer A would likely not be willing to sell to Customer 1 since it may not be able to sell the remaining piece to Customer 2. In this situation, the rule is operating to the disadvantage of the customer.

IX. Conclusion

Again, as stated in the Prior SIFMA Letters, SIFMA supports the intent of the original rule, which was stated as seeking to protect ***investors*** that own municipal securities in amounts below the minimum denomination. However, some of the proposed changes lack clarity, and could result in less liquidity for customers while creating additional and unnecessary challenges for dealers. We continue to have serious concerns that the new language does not appropriately balance the interests of issuers, customers, dealers and the market as a whole. We have suggested alternative language that we feel would both support the stated purpose of the rule and clarify the rule to ease some of the regulatory risk. 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 [redacted].

Sincerely yours,



Leslie M. Norwood
Managing Director and
Associate General Counsel

cc: ***Municipal Securities Rulemaking Board***
Lynnette Kelly, Executive Director
Robert Fippinger, Chief Legal Officer
Michael Post, General Counsel – Regulatory Affairs
Sharon Zackula, Associate General Counsel
Barbara Vouté, Director – Market Practices