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## **MSRB Releases Long-Awaited Best Ex Guidance.**

WASHINGTON - The Municipal Securities Rulemaking Board released its much-anticipated best execution guidance for dealers on Friday, providing answers to frequently asked questions about the rule as well as the exemption for sophisticated municipal market professionals.

MSRB Rule G-18 on best execution requires dealers, whether acting as agents or principals, to use "reasonable diligence" to determine the best market for a security and to then buy or sell the security in that market so the price for the customer "is as favorable as possible under prevailing market conditions." The best execution standard does not necessarily mean a dealer must find the best price.

Dealers are exempted from the rule if their customer is considered an SMMP under both Rules D-15, which defines an SMMP, and Rule G-48 on transactions with SMMPs. The rule also does not apply to trades between dealers. But it covers customer trades that are cleared through another dealer.

The MSRB first filed G-18 with the Securities and Exchange Commission in August 2014 and received SEC approval later that year on Dec. 8. The rule was supposed to have been effective on Dec. 7 of this year, but dealers had questions about implementing it so the MSRB agreed to delay the effective date until after it issued the guidance. The effective date for the rule is now March 21, 2016. The MSRB has tried to ensure its rule and guidance align with the Financial Industry Regulatory Authority's rule on best execution for dealers trading corporate debt.

In its rule, the MSRB provides dealers with a non-exhaustive list of factors to take into account when using reasonable diligence to ascertain the best price for a muni, including: the character of the market for the security; the size and type of transaction; the number of markets checked; the information reviewed to determine the current market for the subject security or similar securities; the accessibility of quotations, and; the terms and conditions of the customer's inquiry or order.

The guidance tries to answer dealers' questions about such issues as: what constitutes reasonable diligence; how they should document their compliance; how to meet best-ex requirements in extreme market conditions, and; how brokers' brokers or alternative trading systems can be used to show reasonable diligence in determining the best market.

"The MSRB is issuing this guidance to facilitate dealers' compliance with their new obligations and ensure that retail investors consistently receive the benefit of fair handling of their orders to buy or sell municipal securities," said MSRB executive director Lynnette Kelly.

But the MSRB makes clear that it is somewhat limited in the guidance it can give on the rule. Rule G-18 is meant to be flexible to fit the diverse nature of different dealers' businesses, the board said, so determining whether a dealer exercised reasonable diligence "necessarily involves a 'facts and circumstances' analysis, and the actions that in one instance may meet a dealer's best-execution obligation may not satisfy that obligation under another set of circumstances."

The guidance urges dealers to develop written policies and procedures that both fit their specific

business models and ensure documentation of their compliance. Even though the rule is meant to allow a broad range of policies and procedures, the MSRB recommends that dealers consider reviewing and including the existing practices of their trading operations, existing best practices within the municipal securities market, and existing best practices in the corporate debt securities market with respect to FINRA's best execution rule.

The MSRB suggests dealers pay attention to three requirements in the rule when documenting compliance. They should: have written policies and procedures for compliance; document periodic reviews of their written policies and procedures and the results of those reviews, and; consider documenting their adherence to the policies and procedures.

In the event of extreme market conditions, the MSRB said it expects dealers to have evaluated their procedures for such situations to make sure they: still treat customer orders fairly, consistently and reasonably; disclose to customers any differences in normal order-handling procedures, and; only implement different procedures designed to respond to extreme market conditions when warranted by market conditions.

The MSRB said there is no set number of either markets or dealers a dealer should check to meet its diligence requirement. A dealer should generally check more than one market or expose customer orders to multiple offerings or bids and show the external offerings or bids to retail customers, it said.

The rule also does not require dealers to use broker's brokers or ATS' as part of their diligence. The guidance said the rule is not designed to favor a particular type of venue over another and that the "expansive interpretation" of the term "best market" is meant to allow dealers to tailor their compliance with their specific areas of business. However, the guidance notes that electronic systems are becoming more available and dealers should periodically consider whether ATSs would provide benefits for their customer transactions.

Additionally, the guidance said using only one broker's broker pricing for a security or one ATS will not categorically qualify as reasonable diligence, but a dealer's policies and procedures can establish the facts and circumstances under which a dealer could be allowed to do so.

The self-regulator also received questions about what qualifies as a similar security under the rule. While not providing an exhaustive list, the MSRB said dealers could look at the issuer, source of repayment, credit rating, coupon, maturity, or a variety of other factors to determine similarity.

Leslie Norwood, associate general counsel and co-head of municipal securities for the Securities Industry and Financial Markets Association, said SIFMA welcomes the guidance but still needs to review it carefully with its members. She added that SIFMA will review the guidance with an eye toward differences between the MSRB's and FINRA's, as well as any implications for the market or any implementation challenges.

Jessica Giroux, general counsel and managing director of federal regulatory policy with Bond Dealers of America, said BDA also appreciates the MSRB's effort and work with FINRA and will be talking to its members about the changes.

"As always, the BDA continues to focus on the transparency and efficiency of the municipal securities market and we know the MSRB is implementing this (and other) rules for the same purposes," she said.

THE BOND BUYER

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