BDA Bond Dealers of America

1909 K Street NW • Suite 510
Washington, DC 20006
202.204.7900
www.bdamerica.org

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Submitted Electronically

Office of Exemption Determinations
Employee Benefits Security Administration (EBSA)
Attention: D-11933
U.S. Department of Labor
200 Constitution Avenue NW
Suite 400
Washington, DC 20210

RE: Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemption (RIN 1210-AB82)

Ladies and Gentlemen:

On behalf of the Bond Dealers of America ("BDA"), I am pleased to submit this letter in response to the Department of Labor's (DOL) Request for Information ("RFI") (RIN 1210-AB82). BDA is the only Washington, DC based trade association representing middle-market and regional broker-dealers active in the U.S. fixed income markets.

The Department of Labor and the Securities and Exchange Commission should work together to formulate an improved best interest standard of care.

The Department of Labor (DOL) and the Securities and Exchange Commission (SEC) have an opportunity to craft a best interest standard of care applicable to retirement and non-retirement accounts that does not treat commissions in a brokerage account as prohibited compensation, does not prohibit principal transactions, and relies on the clear disclosure of material conflicts of interest. BDA recommends that the DOL and SEC evaluate how current Financial Industry Regulatory Authority (FINRA) and Municipal Securities Rulemaking Board (MSRB) rules effectively mitigate conflicts of interest and protect investors, while also preserving client access to investments that meet the unique investment and risk profiles of each individual investor. A more uniform best interest standard of care will reduce investor confusion related to differing standards of care for investors, especially for those investors that hold retirement and non-retirement accounts.

In particular, BDA would like to emphasize the following rules that protect investors and mitigate conflicts of interest related to principal transactions. These rules, and the currently applicable "impartial conduct standards," provide strong investor protections as the DOL and SEC continue to evaluate standards of care generally. The following rules also provide dealers with flexibility to develop policies and procedures to carry out their compliance responsibilities.

- **FINRA 2010 on Commercial Honor and Principles of Trade**, which requires broker-dealer to observe high standards of commercial honor and just and equitable principles of trade in the course of their business interactions.
- **FINRA 2111 on the Suitability** of an investment in a recommended transaction or investment strategy, including the decision to hold a security. This rule requires the broker-dealer representative to have a reasonable basis that the transaction or strategy is suitable for the investor given the investor investment profile.
- **FINRA 2121 and MSRB G-30 on Fair Prices and Commissions** requires broker-dealers to buy and sell securities to customers at fair prices and for no more than a fair commission. This rule applies to principal and agency transactions and is in place to ensure investors do not suffer from excessive mark ups or mark downs or fees related to their transactions.
- **FINRA 5310 and MSRB G-18 on Best Execution** is an order handling rule that requires, amongst other things, that dealers have a rigorous and documented process in place to ensure investor transactions take place after a diligent examination of the market for the subject security. This rule also applies to principal transactions and requires a dealer to have policies and procedures in place to ensure that when a dealer transacts in a security held in inventory, the price the investor is offered benefits from the dealer using reasonable diligence in an examination of the market for the subject security.
- **Effective May 2018, FINRA 2232 and MSRB G-15 (Retail Confirmation Rules)** will require broker-dealers to disclose on certain retail investor trade confirmations markups and markdowns for principal transactions. This rule will create a compensation disclosure for retail investors.

The rule and exemptions unnecessarily prohibit access to the benefits of a dealer's inventory.

BDA members are active participants in all fixed-income securities markets, including the taxable and tax-free municipal securities markets. As the BDA has stated in previous comment letters, the prohibition on recommending both tax-free and taxable municipal securities out of inventory is an unnecessary restriction. This restriction should be eliminated.

The BDA has consistently raised the issue of the municipal securities principal transaction prohibition as a restriction that does not benefit investors. The municipal securities market is a regional marketplace where dealers in certain regions provide liquidity to the issuances that regional investors demand. By prohibiting principal transactions, retirement investors will lose access to regional expertise into both taxable and tax-exempt municipal bonds. The dealers that service retirement investors that demand municipal bonds will have to source those bonds from other dealers and will have to transact on an agency basis in a marketplace where many bonds trade relatively infrequently. This could result in inferior prices to retirement investors relative to the price the dealer who held the bonds on its balance sheet could have offered. In the BDA's view this prohibition on access to dealer municipal inventory will not benefit retirement investors. It should be eliminated.

The rule and the exemptions may result in situations when investors cannot have their securities immediately bid by dealers.

The problem with retirement investors being prohibited from being offered many bonds, including municipal bonds, out of inventory is compounded by how the rule limits access to bid-side dealer liquidity for retirement investors. The general rule and the Best Interest Contract Exemption represent a total prohibition on principal transactions, including a dealer engaging in a principal transaction in which the dealer bids and purchases a security from a retirement investor. Therefore, retirement investors that want to access dealer-supplied liquidity will be required to opt-in to the Principal Transaction Exemption, including the contractual requirements, in order for the dealer to provide liquidity on the bid-side to a retirement investor looking to sell bonds. For retirement investors, especially retirement investors seeking to sell bonds quickly and for fair market value, this requirement is an unnecessary restriction.

The term "sufficiently liquid" should be removed from the principal trading exemption.

BDA notes that there are many observable, market-based measures used to assess the quality of a security, including liquidity. As stated above, selling securities to an investor that are suitable for the investor's risk tolerance should continue to be permissible. Furthermore, retirement investors typically build a portfolio of bonds to align the maturities of their bonds with expected life events, such as retirement.

For example, a 45-year-old retirement investor that expects to retire at 65 may ask a financial advisor for recommendations of several bonds that mature in 20 years. This matches the maturity date of the bond, the date when the investor receives the return of their full invested principal and final interest payment, with the date when the investor wants that investment principal back during retirement.

While liquidity is an important factor, it should not be a determinative factor for a retirement investment, because buy and hold retirement investors are more concerned with the return of principal and interest and less concerned with liquidity and market conditions that would only impact the value of their investment in a situation where they would need to quickly turn the security into cash. Therefore, BDA recommends that the Department remove the "sufficiently liquid" definition from any future principal trading exemption and, as stated above, rely on existing broker-dealer rules that focus on suitability.

BDA urges the Department to remove the anti-arbitration clause from the Best Interest Contract Exemption.

As stated above, the BDA believes that the Department should create a best interest standard of care that relies on existing rules and the impartial conduct standards. This standard or care should not bar arbitration in favor of class litigation. BDA members are concerned that the class action lawsuits associated with this rule will be a highly burdensome legal issue for market participants unless the Best Interest Contract Exemption is amended. Given the Department's recently stated legal position that it will not defend the anti-arbitration clause of the Best Interest Contract Exemption and the fact that the contract is a significant compliance, client communication, and legal burden that will become applicable in January, BDA believes there is an urgent need to remove this clause from the scope of the rules.

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In conclusion, BDA urges the Department to delay the applicability dates of the exemptions as it continues to engage with the SEC on a harmonized best interest standard of care. This is a tremendous opportunity to deliver a standard of care that is clear for retirement and non-retirement investors, does not limit choice, and allows broker-dealers to continue to provide investors the benefits of the principal trading under the strong protections of an improved best interest standard of care and existing and future FINRA and MSRB rules.

Thank you for the opportunity to provide comments.

Sincerely,

Mike Nicholas

Chief Executive Officer