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Page 1 of * 639

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2015 - * 03
Amendment No. (req. for Amendments *)

Filing by Municipal Securities Rulemaking Board

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * ☑ Amendment * ☐ Withdrawal ☐

Section 19(b)(2) * ☑ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

- 19b-4(f)(1)
- 19b-4(f)(2)
- 19b-4(f)(3)
- 19b-4(f)(4)
- 19b-4(f)(5)
- 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document

Exhibit 3 Sent As Paper Document

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Proposed Rule Change Consisting of Proposed New Rule G-42, on Duties of Non-Solicitor Municipal Advisors, and Proposed Amendments to Rule G-8, on Books and Records to be Made by Brokers, Dealers, Municipal Securities Dealers, and Municipal Advisors

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Michael Last Name * Post

Title * General Counsel - Regulatory Affairs

E-mail * mpost@msrb.org

Telephone * (703) 797-6600 Fax (703) 797-6700

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

Municipal Securities Rulemaking Board
has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 04/24/2015

By Ronald W. Smith

(Name *)

(Title *)

Corporate Secretary

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Persona Not Validated - 1422382132618,

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information *

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

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Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act" or "Exchange Act"),[1] and Rule 19b-4 thereunder,[2] the Municipal Securities Rulemaking Board (the "MSRB" or "Board") is filing with the Securities and Exchange Commission (the "SEC" or "Commission") a proposed rule change consisting of proposed new Rule G-42, on duties of non-solicitor municipal advisors ("Proposed Rule G-42" or "proposed rule") and proposed amendments to Rule G-8, on books and records to be made by brokers, dealers, municipal securities dealers, and municipal advisors (collectively, the "proposed rule change"). The MSRB requests that the proposed rule change be approved with an implementation date six months after the Commission approval date for all changes.

(a) The text of the proposed rule change is attached as Exhibit 5. Text proposed to be added is underlined, and text proposed to be deleted is enclosed in brackets.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved by the Board at its meeting on September 17, 2014. Questions concerning this filing may be directed to Michael L. Post, General Counsel - Regulatory Affairs, Sharon Zackula, Associate General Counsel, or Benjamin A. Tecmire, Counsel, at (703) 797-6600.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Following the financial crisis of 2008, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").[3] The Dodd-Frank Act establishes a new federal regulatory regime requiring municipal advisors to register with the SEC, deeming them to owe a fiduciary duty to their municipal entity clients and granting the MSRB rulemaking authority over them. The MSRB, in the exercise of that authority, is currently developing a comprehensive regulatory framework for municipal advisors. A significant element of that regulatory framework is Proposed Rule G-42, which would establish core standards of conduct for municipal advisors that engage in

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 Pub. Law No. 111-203, 124 Stat. 1376 (2010).

municipal advisory activities, other than municipal advisory solicitation activities (hereinafter, "municipal advisors").[4] Proposed Rule G-42 is accompanied by associated proposed amendments to Rule G-8.

Proposed Rule G-42

Proposed Rule G-42 would establish the core standards of conduct and duties of municipal advisors when engaging in municipal advisory activities. The proposed rule draws on aspects of existing law and regulation under other relevant regulatory regimes, including those applicable to brokers, dealers and municipal securities dealers under MSRB rules and the Exchange Act, investment advisers under the Investment Advisers Act of 1940[5] ("Investment Advisers Act") and commodity trading advisors under the Commodity Exchange Act ("CEA").[6]

In summary, the core provisions of Proposed Rule G-42 would:

- Establish certain standards of conduct consistent with the fiduciary duty owed by a municipal advisor to its municipal entity clients, which includes, without limitation, a duty of care and of loyalty;

- Establish the standard of care owed by a municipal advisor to its obligated person clients;

- Require the full and fair disclosure, in writing, of all material conflicts of interest and legal or disciplinary events that are material to a client's evaluation of a municipal advisor;

- Require the documentation of the municipal advisory relationship, specifying certain aspects of the relationship that must be included in the documentation;

- Require that recommendations made by a municipal advisor are suitable for its clients, or determine the suitability of recommendations made by third parties when appropriate; and

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4 See Registration of Municipal Advisors, Rel. No. 34-70462 (Sept. 20, 2013), 78 FR 67467, at 67519, note 679 (Nov. 12, 2013) ("SEC Final Rule") (recognizing that the regulation of municipal advisors includes the "application of standards of conduct . . . that may be required by the Commission or the MSRB, and other requirements unique to municipal advisors that may be imposed by the MSRB"). The proposed rule change would not apply to municipal advisors when engaging in the solicitation of a municipal entity or obligated person within the meaning of Exchange Act Section 15B(e)(9) (15 U.S.C. 78o-4(e)(9)).

5 15 U.S.C. 80b-1 et seq.

6 7 U.S.C. 1 et seq.

- Specifically prohibit a municipal advisor from engaging in certain activities, including, in summary:

    - receiving excessive compensation;
    - delivering inaccurate invoices for fees or expenses;
    - making false or misleading representations about the municipal advisor's resources, capacity or knowledge;
    - participating in certain fee-splitting arrangements with underwriters;
    - participating in any undisclosed fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client of the municipal advisor;
    - making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities, with limited exceptions; and
    - entering into certain principal transactions with the municipal advisor's municipal entity clients.

In addition, the proposed rule change would define key terms used in Proposed Rule G-42 and provide supplementary material. The supplementary material would provide additional guidance on the core concepts in the proposed rule, such as the duty of care, the duty of loyalty, suitability of recommendations and "Know Your Client" obligations; provide context for issues such as the scope of an engagement, conflicts of interest disclosures, excessive compensation and the impact of client action that is independent of or contrary to the advice of a municipal advisor, and the applicability of the proposed rule change to 529 college savings plans ("529 plans") and other municipal entities; provide guidance regarding the definition of "engage in a principal transaction;" the continued applicability of state and other laws regarding fiduciary and other duties owed by municipal advisors; and, finally, include information regarding requirements that must be met for a municipal advisor to be relieved of certain provisions of Proposed Rule G-42 in instances when it inadvertently engages in municipal advisory activities.

Standards of Conduct

Section (a) of Proposed Rule G-42 would establish the core standards of conduct and duties applicable to municipal advisors. The approach toward the core standards and duties in Proposed Rule G-42 flows from the distinctions drawn in the Dodd-Frank Act between a municipal advisor's duties owed to clients that are municipal entities and those duties owed to clients that are obligated persons. The Dodd-Frank Act specifically deems a municipal advisor to owe a fiduciary duty to its municipal entity clients.[7] In contrast,

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[7] See Section 15B(c)(1) of the Exchange Act, 15 U.S.C. 78o-4(c)(1) which provides:

> A municipal advisor and any person associated with such municipal advisor shall be deemed to have a fiduciary duty to any

the Dodd-Frank Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients.[8]

Subsection (a)(i) of Proposed Rule G-42 would provide that each municipal advisor in the conduct of its municipal advisory activities for an obligated person client is subject to a duty of care. Subsection (a)(ii) would provide that each municipal advisor in the conduct of its municipal advisory activities for a municipal entity client is subject to a fiduciary duty, which includes, without limitation, a duty of loyalty and a duty of care. The standards contained in these subsections would not supersede any more restrictive provisions of state or other laws applicable to the activities of municipal advisors.

Proposed supplementary material would provide guidance on the duty of care and the duty of loyalty. Generally, in lieu of providing detailed requirements, the duties would be described in terms that would empower the client to, in large part, determine the scope of services and control the engagement with the municipal advisor (with the municipal advisor's agreement).

Paragraph .01 of the Supplementary Material would describe the duty of care to require, without limitation, a municipal advisor to: (1) exercise due care in performing its municipal advisory activities; (2) possess the degree of knowledge and expertise needed to provide the municipal entity or obligated person client with informed advice; (3) make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client; and (4) undertake a reasonable investigation to determine that the municipal advisor is not basing any recommendation on materially inaccurate or incomplete information. The duty of care that would be established in section (a) of Proposed Rule G-42, would also require the municipal advisor to have a reasonable basis for: any advice provided to or on behalf of a client;[9] any representations made in a certificate that it signs that will be reasonably foreseeably relied upon by the client, any other party involved in the municipal securities transaction or municipal financial product, or investors in the municipal entity client's securities or securities secured by payments from an obligated

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> municipal entity for whom such municipal advisor acts as a municipal advisor, and no municipal advisor may engage in any act, practice, or course of business which is not consistent with a municipal advisor's fiduciary duty or that is in contravention of any rule of the Board.

[8] See SEC Final Rule, 78 FR at 67475, note 100.

[9] The duty of care, which is applicable to all municipal advisory activities, would apply to the provision of comments following the review of any document and the provision of language for use in any document -- including an official statement -- to the extent that conduct constituted municipal advisory activity. Furthermore, such conduct would be required to comport with the fiduciary duty owed in the case of a municipal entity client.

person client; and, any information provided to the client or other parties involved in the municipal securities transaction in connection with the preparation of an official statement for any issue of municipal securities as to which the advisor is advising.

Paragraph .02 of the Supplementary Material would describe the duty of loyalty to require, without limitation, a municipal advisor, when engaging in municipal advisory activities for a municipal entity, to deal honestly and with the utmost good faith with the client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. Paragraph .02 would also provide that the duty of loyalty would preclude a municipal advisor from engaging in municipal advisory activities with a municipal entity client if it cannot manage or mitigate its conflicts of interest in a manner that will permit it to act in the municipal entity's best interests.

Paragraph .03 of the Supplementary Material would specify that a municipal advisor is not required to disengage from a municipal advisory relationship if a municipal entity client or an obligated person client elects a course of action that is independent of or contrary to advice provided by the municipal advisor.

Paragraph .04 of the Supplementary Material would specify that a municipal advisor could limit the scope of the municipal advisory activities to be performed to certain specified activities or services if requested or expressly consented to by the client, but could not alter the standards of conduct or impose limitations on any of the duties prescribed by Proposed Rule G-42. Paragraph .04 would provide that, if a municipal advisor engages in a course of conduct that is inconsistent with the mutually agreed limitations to the scope of the engagement, it may result in negating the effectiveness of the limitations.

Paragraph .07 of the Supplementary Material would state, as a general matter, that, municipal advisors may be subject to fiduciary or other duties under state or other laws and nothing in Proposed Rule G-42 would supersede any more restrictive provision of state or other laws applicable to municipal advisory activities.

Disclosure of Conflicts of Interest and Other Information

Section (b) of Proposed Rule G-42 would require a municipal advisor to fully and fairly disclose to its client in writing all material conflicts of interest, and to do so prior to or upon engaging in municipal advisory activities. The provision would set forth a non-exhaustive list of scenarios under which a material conflict of interest would arise or be deemed to exist and that would require a municipal advisor to provide written disclosures to its client.

Paragraph (b)(i)(A) would require a municipal advisor to disclose any actual or potential conflicts of interest of which the municipal advisor becomes aware after reasonable inquiry that could reasonably be anticipated to impair the municipal advisor's ability to provide advice to or on behalf of the client in accordance with the applicable standards of conduct (i.e., a duty of care or a fiduciary duty). Paragraphs (b)(i)(B)

through (F) would provide more specific scenarios that give rise to conflicts of interest that would be deemed to be material and require proper disclosure to a municipal advisor's client. Under the proposed rule change, a material conflict of interest would always include: any affiliate of the municipal advisor that provides any advice, service or product to or on behalf of the client that is directly related to the municipal advisory activities to be performed by the disclosing municipal advisor; any payments made by the municipal advisor, directly or indirectly, to obtain or retain an engagement to perform municipal advisory activities for the client; any payments received by the municipal advisor from a third party to enlist the municipal advisor's recommendations to the client of its services, any municipal securities transaction or any municipal financial product; any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client; and any conflicts of interest arising from compensation for municipal advisory activities to be performed that is contingent on the size or closing of any transaction as to which the municipal advisor is providing advice. Paragraph (b)(i)(G) would require municipal advisors to disclose any other engagements or relationships of the municipal advisor that could reasonably be anticipated to impair its ability to provide advice to or on behalf of its client in accordance with the applicable standards of conduct established by section (a) of the proposed rule.

Under subsection (b)(i), if a municipal advisor were to conclude, based on the exercise of reasonable diligence, that it had no known material conflicts of interest, the municipal advisor would be required to provide a written statement to the client to that effect.

Subsection (b)(ii) would require disclosure of any legal or disciplinary event that would be material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel. To facilitate the use of existing records, a municipal advisor would be permitted to fulfill this disclosure obligation by identifying the specific type of event and specifically referring the client to the relevant portions of the municipal advisor's most recent SEC Forms MA or MA-I[10] filed with the Commission, if the municipal advisor provides detailed information specifying where the client could access such forms electronically. The requirement to specifically refer to the relevant portions of the forms would not be satisfied by a broad reference to the section of the forms containing such disclosures. Similarly, the specific-information requirement for access to the forms would not be satisfied by a general reference to the SEC's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR"). A municipal advisor could alternatively meet this latter requirement, for example, by publishing its most recent forms on its own website and then providing the client with the direct web link or internet address.

Paragraph .05 of the Supplementary Material would provide that the required conflicts of interest disclosures must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict and must include an explanation of how the municipal advisor addresses or intends to manage or mitigate

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[10] See 17 CFR 249.1300 (SEC Form MA); 17 CFR 249.1310 (SEC Form MA-I).

each conflict.[11] Coupled with its duty to disclose material conflicts of interest, a municipal advisor's obligation to explain how it addresses or intends to manage or mitigate its material conflicts of interest was included in the proposed rule to reflect the Board's intent to eliminate, or at least to expose and reduce the occurrence of, material conflicts of interest that might incline a municipal adviser to provide advice or a recommendation which was not disinterested.[12] If not properly managed or mitigated, material conflicts of interest could lead to a failure to protect a municipal advisor's client's interest, thereby causing a breach of the duty of care and/or loyalty that would be established by proposed section (a).

Paragraph .06 of the Supplementary Material would provide that a municipal advisor that inadvertently engages in municipal advisory activities but does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship[13] would not be required to comply with sections (b) and (c) of Proposed Rule G-42 (relating to disclosure of conflicts of interest and documentation of the relationship), if the municipal advisor takes the prescribed actions listed under paragraph .06 promptly after it discovers its provision of inadvertent advice. The municipal advisor would be required to provide to the client a dated document that would include: a disclaimer stating that the municipal advisor did not intend to provide advice and that, effective immediately, the municipal advisor has ceased engaging in municipal advisory activities with respect to that client in regard to all transactions and municipal financial products as to which advice was inadvertently provided; a notification that the client should be aware that the municipal advisor has not provided the disclosure of material conflicts of interest and other information required under section (b); an identification of all of the advice that was inadvertently provided, based on a reasonable investigation; and

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11 This requirement is analogous to the requirement of Form ADV (17 CFR 279.1) under the Investment Advisers Act (15 U.S.C. 80b-1 et seq.) that obligates an investment adviser to describe how it addresses certain conflicts of interest with its clients. See, e.g., Form ADV, Part 2, Item 5.E.1 of Part 2A (requiring an investment adviser to describe how it will address conflicts of interest that arise in regards to fees and compensation it receives, including the investment adviser's procedures for disclosing the conflicts of interest with its client). See also, Form ADV, Part 2A Items 6, 10, 11, 14 and 17.

12 See, e.g., SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191-92 (1963).

13 Under subsection (f)(vi) of Proposed Rule G-42, a municipal advisory relationship would be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person, and would be deemed to have ended on the earlier of (i) the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship required in section (c) of Proposed Rule G-42 or (ii) the date on which the municipal advisor withdraws from the municipal advisory relationship.

a request that the municipal entity or obligated person acknowledge receipt of the document. The municipal advisor also would be required to conduct a review of its supervisory and compliance policies and procedures to ensure that they are reasonably designed to prevent inadvertently providing advice to municipal entities and obligated persons. The final sentence of paragraph .06 of the Supplementary Material would also clarify that the satisfaction of the requirements of paragraph .06 would have no effect on the applicability of any provisions of Proposed Rule G-42 other than sections (b) and (c), or any other legal requirements applicable to municipal advisory activities. Such other legal requirements, would include, but would not be limited to, other MSRB rules (including Rule G-23), Financial Industry Regulatory Authority ("FINRA") rules or federal or state laws that apply to municipal advisory activities.[14]

Documentation of the Municipal Advisory Relationship

Section (c) of Proposed Rule G-42 would require each municipal advisor to evidence each of its municipal advisory relationships by a writing, or writings created and delivered to the municipal entity or obligated person client prior to, upon or promptly after the establishment of the municipal advisory relationship. The documentation would be required to be dated and include, at a minimum:[15]

- the form and basis of direct or indirect compensation, if any, for the municipal advisory activities to be performed, as provided in proposed subsection (c)(i);

- the information required to be disclosed in proposed section (b), including the disclosures of conflicts of interest, as provided in proposed subsection (c)(ii);

- a description of the specific type of information regarding legal and disciplinary events requested by the Commission on SEC Form MA and SEC Form MA-I, as provided in proposed subsection (c)(iii), and detailed information specifying where the client may electronically access the

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[14] Rule G-23, on activities of financial advisors, generally provides that a dealer that has a financial advisory relationship (as defined by Rule G-23(b)) with respect to the issuance of municipal securities is precluded from acquiring all or any portion of such issue, directly or indirectly, from the issuer as principal, either alone or as a participant in a syndicate or other similar account formed for that purpose. A dealer is also, under Rule G-23, precluded from arranging the placement of an issue with respect to which it has a financial advisory relationship.

[15] While no acknowledgement from the client of its receipt of the documentation would be required, a municipal advisor must, as part of the duty of care it owes its client, reasonably believe that the documentation was received by its client.

municipal advisor's most recent Form MA and each most recent Form MA-I filed with the Commission;[16]

- the date of the last material change to the legal or disciplinary event disclosures on any SEC Forms MA or MA-I filed with the Commission by the municipal advisor, as provided in proposed subsection (c)(iv);

- the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement, as provided in proposed subsection (c)(v);

- the date, triggering event, or means for the termination of the municipal advisory relationship, or, if none, a statement that there is none, as provided in proposed subsection (c)(vi); and

- any terms relating to withdrawal from the municipal advisory relationship, as provided in proposed subsection (c)(vii).

Proposed Rule G-42(c) also would require municipal advisors to promptly amend or supplement the writing(s) during the term of the municipal advisory relationship as necessary to reflect any material changes or additions in the required information. For example, if the basis of compensation or scope of services materially changed during the term of the relationship, the municipal advisor would be required to amend or supplement the writing(s) and promptly deliver the amended writing(s) or supplement to the client. The same would be true in the case of material conflicts of interest discovered after the relationship documentation was last provided to the client. The amendment and supplementation requirement in proposed section (c) would apply to any material changes and additions that are discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor. Any amendments or supplementation also would be subject to the requirements of the proposed rule change that would apply as if it were the first relationship documentation provided to the client.

Proposed Rule G-42(c) is modeled in part on Rule G-23, which requires a broker, dealer or municipal securities dealer ("dealer") that enters into a financial advisory relationship with an issuer to evidence that relationship in writing prior to, upon or promptly after the inception of that relationship. Like Rule G-23, proposed section (c)

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[16] Compliance with this requirement could be achieved in the same manner, and (so long as done upon or prior to engaging in municipal advisory activities for the client) concurrently with providing to the client the information required under proposed subsection (b)(ii). However, the description of the events contained in Forms MA or MA-I must be sufficiently specific to allow a municipal entity or obligated person client to understand the nature of any disclosed legal or disciplinary event. In addition, the municipal advisor must provide detailed information specifying where the client could access such forms electronically. See supra note 10 and accompanying text.

would not require that the writing(s) evidencing the relationship be a bilateral agreement or contract. For example, if state law provided for the procurement of municipal advisory services in a manner that did not require a writing sufficient to establish a bilateral agreement, a municipal advisor could send its client a writing, such as a letter that references the procurement document and contains the terms and disclosures required by proposed Rule G-42(b) and (c) to evidence its municipal advisory relationship with its municipal entity or obligated person client.

Recommendations and Review of Recommendations of Other Parties

Section (d) of Proposed Rule G-42 would provide that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product unless the municipal advisor has determined, based on the information obtained through the reasonable diligence of the municipal advisor, whether the transaction or product is suitable for the client.[17] Proposed section (d) also contemplates that a municipal advisor may be requested by the client to review and determine the suitability of a recommendation made by a third party to the client. If a client were to request this type of review, and such review were within the scope of the engagement, the municipal advisor's determination regarding the suitability of the third-party's recommendation regarding a municipal securities transaction or municipal financial product would be subject to the same reasonable diligence standard -- requiring the municipal advisor to obtain relevant information through the exercise of reasonable diligence.

As to both types of review, the municipal advisor would be required under proposed section (d) to inform its municipal entity or obligated person client of its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the advisor reasonably believes the recommended transaction or product is, or is not, suitable for the client; and whether the municipal advisor has

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[17] Some securities market participants are required to make only recommendations that are "consistent with" their customer's best interests. (See FINRA Notice 12-25, Suitability (May 2012)). As provided in proposed section (a) and paragraph .02 of the Supplementary Material to Proposed Rule G-42, a municipal advisor to a municipal entity client owes the client a fiduciary duty that includes a duty of loyalty in addition to the duty of care, which requires the municipal advisor to deal honestly and with the utmost good faith with the municipal entity client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. A municipal advisor's recommendations of municipal securities transactions and municipal financial products to a municipal entity client, as is the case with all municipal advisory activities performed for a municipal entity client, must comport with the municipal advisor's fiduciary duty and particularly its duty of loyalty. The MSRB considers the duty of loyalty described in Proposed Rule G-42 to be even more rigorous than a standard requiring consistency with a client's best interests.

investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives. The proposed rule does not include requirements regarding how such information must be communicated by the municipal advisor to the client, and a municipal advisor would be permitted to choose the appropriate method by which to communicate the information to its client so long as it comports with the duty of care owed.

Section (d), like other provisions of Proposed Rule G-42, would reflect the basic principle that the client controls the scope of the engagement with its municipal advisor (with the agreement of the municipal advisor). For example, a municipal advisor's engagement may be limited in scope because the municipal advisor's client already reached a decision regarding a particular municipal securities transaction or municipal financial product, or engaged another professional to undertake certain duties in connection with a municipal securities transaction or municipal financial product. Paragraph .04 of the Supplementary Material would provide that a municipal advisor and its client could limit the scope of the municipal advisory relationship to certain specified activities or services. A municipal advisor, however, would not be permitted to alter the standards of conduct or duties imposed by the proposed rule with respect to that limited scope.

The proposed rule change would adopt, and apply to municipal advisors, the existing MSRB interpretive guidance regarding the general principles currently applicable to dealers for determining whether a particular communication constitutes a recommendation of a securities transaction.[18] Consistent with the approach in the case of dealers, a municipal advisor's communication to its client that could reasonably be viewed as a "call to action" to engage in a municipal securities transaction or enter into a municipal financial product would be considered a recommendation and obligate the municipal advisor to conduct a suitability analysis of its recommendation. Depending on all of the facts and circumstances, communications by a municipal advisor to a client that concern minor or ancillary matters that relate to, but are not recommendations of, a municipal securities transaction or municipal financial product might constitute advice (and therefore trigger many other provisions of the proposed rule) but would not trigger the suitability obligation set forth in proposed section (d).

Paragraph .08 of the Supplementary Material would provide guidance related to a municipal advisor's suitability obligations. Under this provision, a municipal advisor's determination of whether a municipal securities transaction or municipal financial product is suitable for its client must be based on numerous factors, as applicable to the particular type of client, including, but not limited to: the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and

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[18] See MSRB Rule G-19. See also MSRB Notice 2002-30 (Sept. 25, 2002) Notice Regarding Application of Rule G-19, on Suitability of Recommendations and Transactions, to Online Communications.

complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued are reasonably expected to be outstanding, and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after the municipal advisor has conducted a reasonable inquiry.

In connection with a municipal advisor's obligation to determine the suitability of a municipal securities transaction or a municipal financial product for a client, which should take into account its knowledge of the client, paragraph .09 of the Supplementary Material would require a municipal advisor to know its client. The obligation to know the client would require a municipal advisor to use reasonable diligence to know and retain essential facts concerning the client and the authority of each person acting on behalf of the client, and is similar to requirements in other regulatory regimes.[19] The facts "essential" to knowing one's client would include those required to effectively service the municipal advisory relationship with the client; act in accordance with any special directions from the client; understand the authority of each person acting on behalf of the client; and comply with applicable laws, rules and regulations.

As a practical matter, it is understood that a client could at times elect a course of action either independent of or contrary to the advice of its municipal advisor. Paragraph .03 of the Supplementary Material would provide that the municipal advisor would not be required to disengage from the municipal advisory relationship on that basis.

Specified Prohibitions

Subsection (e)(i) of Proposed Rule G-42 would prohibit discrete conduct or activities that would conflict, or would be highly likely to conflict, with the core standards of conduct – the duty of loyalty and the duty of care – applicable to municipal advisors under Proposed Rule G-42 and the Exchange Act.

Paragraph (e)(i)(A) would prohibit a municipal advisor from receiving compensation from its client that is excessive in relation to the municipal advisory activities actually performed for the client. Paragraph .10 of the Supplementary Material

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[19] Similar requirements apply to brokers and dealers under FINRA Rule 2090 (Know Your Customer) and swap dealers under Commodity Futures Trading Commission ("CFTC") Rule 402(b) (General Provisions: Know Your Counterparty), 17 CFR 23.402(b), found in CFTC Rules, Ch. I, Pt. 23, Subpt. H (Business Conduct Standards for Swap Dealers and Major Swap Participants Dealing with Counterparties, including Special Entities) (17 CFR 23.400 et. seq.). Notably, the CFTC's rule applies to dealings with special entity clients, defined to include states, state agencies, cities, counties, municipalities, other political subdivisions of a State, or any instrumentality, department, or a corporation of or established by a State or political subdivision of a State. See CFTC Rule 401(c) (defining "special entity") (17 CFR 23.401(c)).

would provide additional guidance on how compensation would be determined to be excessive. Included in paragraph .10 are several factors that would be considered when evaluating the reasonableness of a municipal advisor's compensation relative to the nature of the municipal advisory activities performed, including, but not limited to: the municipal advisor's expertise, the complexity of the municipal securities transaction or municipal financial product, whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product, the length of time spent on the engagement and whether the municipal advisor is paying any other relevant costs related to the municipal securities transaction or municipal financial product.

Paragraph (e)(i)(B) would prohibit municipal advisors from delivering an invoice for fees or expenses for municipal advisory activities that does not accurately reflect the activities actually performed or the personnel that actually performed those activities. This provision would not prohibit a municipal advisor from including a discount for the services it actually performed, if accurately disclosed.

Paragraph (e)(i)(C) would prohibit a municipal advisor from making any representation or submitting any information that the municipal advisor knows or should know is either materially false or materially misleading due to the omission of a material fact, about its capacity, resources or knowledge in response to requests for proposals or in oral presentations to a client or prospective client for the purpose of obtaining or retaining an engagement to perform municipal advisory activities. Note that, additionally, the MSRB's existing fundamental fair practice rule, Rule G-17, precludes municipal advisors, in the conduct of their municipal advisory activities, from engaging in any deceptive, dishonest or unfair practice with any person.

Paragraph (e)(i)(D) would prohibit municipal advisors from making or participating in two types of fee-splitting arrangements: (1) any fee-splitting arrangement with an underwriter on any municipal securities transaction as to which the municipal advisor has provided or is providing advice; and (2) any undisclosed fee-splitting arrangement with providers of investments or services to a municipal entity or obligated person client of the municipal advisor.

Paragraph (e)(i)(E) would, generally, prohibit a municipal advisor from making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities. However, the provision contains three exceptions. The prohibition would not apply to: (1) payments to an affiliate of the municipal advisor for a direct or indirect communication with a municipal entity or obligated person on behalf of the municipal advisor where such communication is made for the purpose of obtaining or retaining an engagement to perform municipal advisory activities; (2) reasonable fees paid to another municipal advisor registered as such with the Commission and MSRB for making such a communication as described in subparagraph (e)(i)(E)(1); and (3) payments that are permissible "normal business dealings" as described in MSRB Rule G-20. The proposed rule change, however, would not prescribe parameters that would effectively limit a client's ability to decide the source of funds for the payment of fees for services rendered by the municipal advisor.

Principal Transactions

Subsection (e)(ii) of Proposed Rule G-42 would prohibit a municipal advisor to a municipal entity, and any affiliate of such municipal advisor, from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice. The ban on principal transactions would apply only with respect to clients that are municipal entities. The ban would not apply to principal transactions between a municipal advisor (or an affiliate of the municipal advisor) and the municipal advisor's obligated person clients. Although such transactions would not be prohibited, importantly, all municipal advisors, including those engaging in municipal advisory activities for obligated person clients, are currently subject to the MSRB's fundamental fair-practice rule, Rule G-17.

Paragraph .07 of the Supplementary Material would provide an exception to the ban on principal transactions in subsection (e)(ii) in order to avoid a possible conflict with existing MSRB Rule G-23, on activities of financial advisors. Specifically, the ban in subsection (e)(ii) would not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities on the basis that the municipal advisor provided advice as to the issuance, because such a transaction is the type of transaction that is addressed, and, in certain circumstances, prohibited by Rule G-23. The purpose of this provision would be to avoid a potential conflict in MSRB rules and provide, until such time as the MSRB may further review and potentially amend Rule G-23, that the specific prohibition against principal transactions contained in subsection (e)(ii) would not prohibit such underwriting transactions, as they are already addressed and prohibited in certain circumstances by Rule G-23.

For purposes of the prohibition in proposed subsection (e)(ii), subsection (f)(i) would define the term "engaging in a principal transaction" to mean "when acting as a principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client." This definition draws on the statutory language regarding principal transactions in the Investment Advisers Act.[20] Among other things, the definition was designed to exclude transactions thought to be potentially covered by some commenters, such as the taking of a cash deposit or the payment by a client solely for professional services. Further, paragraph .11 of the Supplementary Material would clarify that the term "other similar financial products," as used in subsection (f)(i), would include a bank loan but only if it is in an aggregate principal amount of $1,000,000 or more and is economically equivalent to the purchase of one or more municipal securities. Bank loans would be included under the specified circumstances because, as a matter of market practice, they serve as a financing

[20] See 15 U.S.C. 80b-6(3).

alternative to the issuance of municipal securities and pose a comparable, acute potential for self-dealing and other breaches of the fiduciary duty owed by a municipal advisor to a municipal entity client.

Definitions

Section (f) of Proposed Rule G-42 would provide definitions of the terms "engaging in a principal transaction," "affiliate of the municipal advisor,"[21] "municipal advisory relationship,"[22] and "official statement."[23] Further, for several terms in Proposed Rule G-42 that have been previously defined by federal statute or SEC rules, proposed section (f) would, for purposes of Proposed Rule G-42, adopt the same meanings. These terms would include "advice;"[24] "municipal advisor;"[25] "municipal advisory activities;"[26] "municipal entity;"[27] and "obligated person."[28]

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21 "Affiliate of the municipal advisor" would mean "any person directly or indirectly controlling, controlled by, or under common control with such municipal advisor." See Proposed Rule G-42(f)(iii).

22 Proposed Rule G-42(f)(vi) provides that a "municipal advisory relationship" would

> be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person. The municipal advisory relationship shall be deemed to have ended on the date which is the earlier of (i) the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship required in section (c) of this rule or (ii) the date on which the municipal advisor withdraws from the municipal advisory relationship.

23 "Official statement" would have the same meaning as in MSRB Rule G-32(d)(vii). See Proposed Rule G-42(f)(ix).

24 "Advice" would have the same meaning as in Section 15B(e)(4)(A)(i) of the Exchange Act (15 U.S.C. 78o-4(e)(4)(A)(i)); SEC Rule 15Ba1-1(d)(1)(ii) (17 CFR 240.15Ba1-1(d)(1)(ii)); and other rules and regulations thereunder. See Proposed Rule G-42(f)(ii).

25 "Municipal advisor" would

> have the same meaning as in Section 15B(e)(4) of the Act, 17 CFR 240.15Ba1-1(d)(1)-(4) and other rules and regulations thereunder; provided that it shall exclude a person that is otherwise a municipal advisor solely based on activities within the meaning of Section 15B(e)(4)(A)(ii) of the Act and rules and regulations thereunder or

Applicability of Proposed Rule G-42 to 529 College Savings Plans and Other Municipal Fund Securities

The regulation of municipal advisors, as the SEC has recognized,[29] is relevant to municipal fund securities.[30] Paragraph .12 of the Supplementary Material emphasizes the proposed rule's application to municipal advisors whose municipal advisory clients are sponsors or trustees of municipal fund securities.

Proposed Amendments to Rule G-8

The proposed amendments to Rule G-8 would require each municipal advisor to make and keep any document created by the municipal advisor that was material to its review of a recommendation by another party or that memorialize its basis for any conclusions as to suitability.

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any solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Act and rules and regulations thereunder.

See Proposed Rule G-42(f)(iv).

26 "Municipal advisory activities" would mean those activities that would cause a person to be a municipal advisor as defined in subsection (f)(iv) (definition of "municipal advisor") of Proposed Rule G-42. See Proposed Rule G-42(f)(v).

27 "Municipal entity" would "have the same meaning as in Section 15B(e)(8) of the Act, 17 CFR 240.15Ba1-1(g) and other rules and regulations thereunder." See Proposed Rule G-42(f)(vii).

28 "Obligated person" would "have the same meaning as in Section 15B(e)(10) of the Act, 17 CFR 240.15Ba1-1(k) and other rules and regulations thereunder." See Proposed Rule G-42(f)(viii).

29 See SEC Final Rule, 78 FR at 67472-3.

30 "Municipal fund security" is defined in MSRB Rule D-12 to mean "a municipal security issued by an issuer that, but for the application of Section 2(b) of the Investment Company Act of 1940, would constitute an investment company within the meaning of Section 3 of the Investment Company Act of 1940." The term refers to, among other things, interests in governmentally sponsored 529 college savings plans and local government investment pools.

(b) Statutory Basis

Section 15B(b)(2) of the Exchange Act[31] provides that:

> The Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

Section 15B(b)(2)(C) of the Exchange Act[32] provides that the MSRB's rules shall:

> be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

Section 15B(b)(2)(L)(i) of the Exchange Act[33] requires, with respect to municipal advisors, the Board to adopt rules to prescribe means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients.

The MSRB believes that, the proposed rule change is consistent with Sections 15B(b)(2),[34] 15B(b)(2)(C)[35] and 15B(b)(2)(L)(i)[36] of the Exchange Act because it will enhance the protections afforded to municipal bond issuers and investors by providing

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31 15 U.S.C. 78o-4(b)(2).

32 15 U.S.C. 78o-4(b)(2)(C).

33 15 U.S.C. 78o-4(b)(2)(L)(i).

34 15 U.S.C. 78o-4(b)(2).

35 15 U.S.C. 78o-4(b)(2)(C).

36 15 U.S.C. 78o-4(b)(2)(L)(i).

guidance to municipal advisors that is designed to promote compliance with the standards of conduct, requirements and intent of the Dodd-Frank Act.

In this regard, neither the Dodd-Frank Act nor the recently-adopted SEC Final Rule prescribe the duties and obligations of municipal advisors beyond a general statement that municipal advisors shall be deemed to have a fiduciary duty to any municipal entity for whom the municipal advisor acts as a municipal advisor. Adoption of Proposed Rule G-42 will fulfill the need for regulatory guidance with respect to the standards of conduct and duties of municipal advisors and the prevention of breaches of a municipal advisor's fiduciary duty to its municipal entity clients. Proposed Rule G-42 also will establish standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for obligated persons and provide guidance to these municipal advisors as to what conduct would satisfy these duties and obligations.

The MSRB believes that by articulating specific standards of conduct and duties for municipal advisors, Proposed Rule G-42 will assist municipal advisors in complying with the statutorily-imposed requirements of the Dodd-Frank Act, and help prevent failures to meet those requirements. The proposed rule change will aid municipal entities and obligated persons that choose to engage municipal advisors in connection with their issuances of municipal securities as well as transactions in municipal financial products by promoting higher ethical and professional standards of such municipal advisors. The MSRB also believes that articulating standards of conduct and duties of municipal advisors will enhance the ability of the MSRB and other regulators to oversee the conduct of municipal advisors, as contemplated by the Dodd-Frank Act.

The MSRB believes the proposed rule change will enhance municipal entity and obligated person protections by ensuring that these entities have access to sufficient information to make meaningful choices, based on the merits of the municipal advisor, when considering engaging a municipal advisor by requiring municipal advisors to provide detailed disclosures of material conflicts of interest and certain other information prior to or upon the establishment of the municipal advisory relationship. As a result, municipal advisor clients will be able to evaluate municipal advisors on this objective set of information. These protections will also be enhanced as a result of the proposed rule change's guidance for municipal advisors that could assist advisors in complying with, or help prevent breaches of, their fiduciary duty and duty of care, as well as other applicable obligations such as the duty of fair dealing (which is owed under MSRB Rule G-17 by all municipal advisors to all persons). To the extent that this guidance, provided in the supplementary material in the proposed rule change, would increase the likelihood of compliance by municipal advisors, municipal entities and obligated persons will benefit. Investors in municipal bond offerings will also benefit from the proposed rule change to the extent that a municipal entity or obligated person issuing bonds that uses a municipal advisor is more likely to receive services that reflect a higher ethical and professional standard than otherwise would be the case.

The proposed rule change would also, to some extent, prescribe means for municipal advisors to help prevent breaches of these duties, which would include, among

others: requirements for the information that must be included in the documentation of the municipal advisory relationship; specified activities (such as certain principal transactions) that would be explicitly prohibited; and disclosure requirements that must accompany a municipal advisor's recommendation regarding a municipal security or a municipal financial product.

Section 15B(b)(2)(L)(iv) of the Exchange Act[37] requires that rules adopted by the Board:

> not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2)(L)(iv) of the Exchange Act[38] because the proposed rule change would impose on all municipal advisors, including small municipal advisors, only the necessary and appropriate regulatory burdens needed to promote compliance with the proposed rule change. To accomplish this, Proposed Rule G-42 would use both a principles and prescriptive-based approach to establish the core standards of conduct in order to, among other things, accommodate the diversity of the municipal advisor population, including small municipal advisors and sole proprietorships, and to provide uniform protections to its clients, investors and the public.

The MSRB recognizes that municipal advisors would incur costs to meet the standards of conduct and duties contained in the proposed rule changes. These costs also could include additional compliance and recordkeeping costs. To ensure compliance with the disclosure obligations of the proposed rule change, municipal advisors could incur costs by seeking advice from legal and compliance professionals when preparing disclosures to clients. However, the MSRB believes that some of these costs are accounted for in the SEC Final Rule which requires disclosure of at least some similar information, such as the disclosure of disciplinary events. Proposed Rule G-42 could also impose additional costs on municipal advisors by requiring the disclosure of additional information directly to clients, some of which must already be submitted to the SEC on SEC Forms MA[39] and MA-I.[40] The MSRB has considered these costs and that there could be some instances of duplicative disclosure, but believes that the overlap in disclosure requirements between the SEC and MSRB will be minimal and that the disclosure requirements of the proposed rule are important elements of Proposed Rule G-

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37 15 U.S.C. 78o-4(b)(2)(L)(iv).

38 15 U.S.C. 78o-4(b)(2)(L)(iv).

39 17 CFR 249.1300.

40 17 CFR 249.1310.

42 that protect municipal advisor clients and foster transparency in the municipal advisory marketplace.

As to the potential costs associated with additional recordkeeping requirements, the SEC recognized in its economic analysis[41] of its recordkeeping requirements that municipal advisors should already be maintaining books and records as part of their day-to-day operations. In addition, municipal advisors who are also registered as broker-dealers or investment advisers are currently subject to the recordkeeping requirements of those regulatory frameworks. Against this back-drop, the MSRB believes that the costs associated with the few additional recordkeeping requirements associated with Proposed Rule G-42 will not be significant.

The MSRB believes that any increase in municipal advisory fees attributable to the additional costs of the proposed rule change will be minimal and that at least the element of fixed costs per municipal advisory firm will be spread across the number of advisory engagements for each firm. The MSRB recognizes, however, that for smaller municipal advisors with fewer clients, the cost of compliance with the proposed rule change's standards of conduct and duties could represent a greater percentage of annual revenues, and, thus, such advisors could be more likely to pass those costs along to their advisory clients.

The MSRB also recognizes that, as a result of these costs, some municipal advisors could decide to exit the market, curtail their activities, consolidate with other firms, or pass the costs on to municipal entities and obligated persons in the form of higher fees. The MSRB believes, however, that by articulating the core standard of conduct and duties and obligations of municipal advisors and by prescribing means that would prevent breaches of these duties, the proposed rule change will reduce possible confusion and uncertainty about what is required in order to comply with relevant provisions of the Dodd-Frank Act. Therefore, the proposed rule change likely will reduce certain costs of compliance that might have otherwise been incurred by allowing municipal advisors to more quickly and accurately determine compliance requirements.

The MSRB also believes that the proposed rule change is consistent with Section 15B(b)(2)(G) of the Exchange Act,[42] which provides that the MSRB's rules shall:

> prescribe records to be made and kept by municipal securities brokers, municipal securities dealers, and municipal advisors and the periods for which such records shall be preserved.

The proposed rule change would require, under the proposed amendments to Rule G-8, that a municipal advisor make and keep records of any document created by the municipal advisor that was material to its review of a recommendation by another party

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41 See SEC Final Rule, 78 FR at 67619.

42 15 U.S.C. 78o-4(b)(2)(G).

or that memorializes the basis for any conclusions as to suitability. The MSRB believes that the proposed amendments to Rule G-8 related to recordkeeping (with the ensuing application of existing Rule G-9 on records preservation) would promote compliance and facilitate enforcement of Proposed Rule G-42, other MSRB rules, and other applicable securities laws and regulations.

4. Self-Regulatory Organization's Statement on Burden on Competition

Section 15B(b)(2)(C)[43] of the Exchange Act requires that MSRB rules not be designed to impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. In addition, Section 15B(b)(2)(L)(iv)[44] of the Exchange Act provides that MSRB rules may not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

In determining whether these standards have been met, the MSRB was guided by the Board's Policy on the Use of Economic Analysis in MSRB Rulemaking.[45] In accordance with this policy, the Board evaluated the potential impacts of the proposed rule, including in comparison to reasonable alternative regulatory approaches, relative to the baseline that, inter alia, deemed municipal advisors to owe a fiduciary duty to their municipal entity clients and established a registration requirement. Based on this evaluation, the MSRB does not believe that the proposed rule change would impose any additional burdens on competition that are not necessary or appropriate in furtherance of the purposes of the Exchange Act.

The proposed rule may also provide a range of benefits to municipal entities, investors and municipal advisors. Municipal entities and obligated persons will have access to more information about municipal advisors and can make better, more informed choices with lower search costs. The availability of additional, objective information and the fostering of merit-based competition among municipal advisors should lead to enhanced issuer protections and improved outcomes. These improvements likely would enhance investor confidence in the integrity of the market. Moreover, the MSRB believes that the proposed rule change will provide a benefit to municipal advisors who could otherwise face greater uncertainty about the standards of conduct and duties required to meet certain of the requirements of the Dodd-Frank Act.

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43 15 U.S.C. 78o-4(b)(2)(C).

44 15 U.S.C. 78o-4(b)(2)(L)(iv).

45 Policy on the Use of Economic Analysis in MSRB Rulemaking, available at http://www.msrb.org/About-MSRB/Financial-and-Other-Information/Financial-Policies/Economic-Analysis-Policy.aspx.

The MSRB considered whether costs associated with the proposed rule change, relative to the baseline, could affect the competitive landscape by leading some municipal advisors to exit the market, curtail their activities, consolidate with other firms, or pass costs on to municipal entity and obligated person clients in the form of higher fees. In addition, the MSRB considered whether the costs associated with the proposed rule, relative to the baseline, could create barriers to entry for firms wishing to offer to engage in municipal advisory activities.

The MSRB recognizes that some municipal advisors may exit the market as a result of the costs associated with the proposed rule relative to the baseline. However, the MSRB believes municipal advisors may exit the market for a number of reasons other than costs associated with the proposed rule. The MSRB also recognizes that some municipal advisors may consolidate with other municipal advisors in order to benefit from economies of scale (e.g., by leveraging existing compliance resources of a larger firm) rather than to incur separately the costs associated with the proposed rule. Finally, the MSRB acknowledges that some potential market entrants may be discouraged from entering the market because of costs or because the requirement to disclose information such as disciplinary events might make attracting business more difficult.

It is also possible that competition for municipal advisory activities may be affected by whether incremental costs associated with requirements of the proposed rule are passed on to advisory clients. The amount of costs passed on may be influenced by the size of the municipal advisory firm. For smaller municipal advisors with fewer clients, the incremental costs associated with the requirements of the proposed rule may represent a greater percentage of annual revenues, and, thus, such advisors may be more likely to pass those costs along to their advisory clients. As a result, the competitive landscape may be altered by the potentially impaired ability of smaller firms to compete for advisory clients.

In addition to the factors noted above that may affect smaller advisory firms, the MSRB understands that some small municipal advisors and sole proprietors may not employ full-time compliance staff and that the cost of ensuring compliance with the requirements of the proposed rule may be proportionally higher for these smaller firms.

The MSRB believes these costs represent only those necessary to achieve the purposes of the Exchange Act. Relative to draft Rule G-42 as initially published for comment,[46] the MSRB has made efforts to minimize costs that could affect the competitive landscape including, narrowing the scope of the conflicts that must be disclosed, specifying a less burdensome method for disclosing conflicts and disciplinary actions and documenting the municipal advisory relationship, clarifying the obligations owed by municipal advisors to obligated persons, and removing a number of other previously considered requirements.

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[46] The MSRB sought comment on the initial draft Rule G-42 ("Initial Draft Rule") and draft amendments to Rules G-8 and G-9 in MSRB Notice 2014-01 (Jan. 9, 2014) ("First Request for Comment").

Further, while exit, consolidation, or a reduced number of new market entrants may lead to a reduced pool of municipal advisors, the SEC concluded in the SEC Final Rule (on the permanent registration of municipal advisors) that the market would be likely to remain competitive despite the potential exit of some municipal advisors (including small entity municipal advisors), consolidation of municipal advisors, or lack of new entrants into the market.[47]

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The MSRB solicited comment on the proposed rule change in the First Request for Comment, requesting comment on a draft of Rule G-42 and draft amendments to Rules G-8 and G-9, and a second notice requesting comment on a revised draft of Rule G-42 and draft amendments to Rules G-8 and G-9.[48]

The MSRB received forty-six comment letters in response to the First Request for Comment,[49] and nineteen comment letters in response to the Second Request for

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47 See SEC Final Rule, 78 FR at 67608.

48 See MSRB Notice 2014-12 (Jul. 23, 2014) ("Second Request for Comment"). The draft rule text published in the Second Request for Comment is hereinafter the "Revised Draft Rule."

49 Comments were received in response to the First Request for Comment from: Acacia Financial Group, Inc.: Letter from Kim M. Whelan, Co-President, dated March 10, 2014 ("Acacia"); American Bankers Association: Letter from Cristeena G. Naser, Vice President and Senior Counsel, dated March 4, 2014 ("ABA"); American Council of Engineering Companies: Letter from David A. Raymond, President and CEO, dated March 7, 2014 ("ACEC"); American Public Transportation Association: Letter from Michael P. Melaniphy, President and CEO, dated March 10, 2014 ("APTA"); Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated March 10, 2014 ("BDA"); Cape Cod Five Cents Savings Bank: Letter from Dorothy A. Savarese, President and Chief Executive Officer, dated March 10, 2014 ("Cape Cod Savings"); Chancellor Financial Associates: E-mail from William J. Caraway, President, dated January 14, 2014 ("Chancellor Financial"); Coastal Securities: Letter from Chris Melton, Executive Vice President, dated March 10, 2014 ("Coastal"); College Savings Foundation: Letter from Mary G. Morris, Chair, dated March 10, 2014 ("CSF"); College Savings Plans Network: Letter from Betty Everitt Lochner, Director, Guaranteed Education Tuition Program, dated March 10, 2014 ("CSPN"); Cooperman Associates: Letter from Joshua G. Cooperman dated March 10, 2014 ("Cooperman"); Erika Miller: E-mail dated February 4, 2015; FCS Group: Letter from Taree Bollinger, Vice President, dated March 17, 2014 ("FCS"); First River Advisory L.L.C.: Letter from Shelley J. Aronson, President, dated January 16,

2014 (“First River Advisory”); First Southwest Company: Letter from Hill A. Feinberg, Chairman and Chief Executive Officer, and Michael G. Bartolotta, Vice Chairman, dated March 7, 2014 (“First Southwest”); Frost Bank: Letter from William H. Sirakos, Senior Executive Vice President, dated March 10, 2014 (“Frost”); George K. Baum & Company: Letter from Guy E. Yandel, EVP and Head of Public Finance, Dana L. Bjornson, EVP, CFO and Chief Compliance Officer, and Andrew F. Sears, SVP and General Counsel, dated March 10, 2014 (“GKB”); Government Finance Officers Association: Letter from Dustin McDonald, Director, Federal Liaison Center, dated March 13, 2014 (“GFOA”); Government Investment Officers Association: Letter from Laura Glenn, President, et al., dated March 7, 2014 (“GIOA”); Investment Company Institute: Letter from Tamara K. Salmon, Senior Associate Counsel, dated March 4, 2014 (“ICI”); J.P. Morgan: Letter from Paul N. Palmeri, Managing Director, dated March 10, 2014 (“JP Morgan”); Kutak Rock LLP: Letter from John J. Wagner dated March 10, 2014 (“Kutak”); Lamont Financial Services Corporation: Letter from Robert A. Lamb, President, dated March 10, 2014 (“Lamont”); Lewis Young Robertson & Burningham, Inc.: Letter from Laura D. Lewis, Principal, dated March 3, 2014 (“Lewis Young”); MSA Professional Services, Inc.: Letter from Gilbert A. Hantzsch, CEO, dated March 10, 2014 (“MSA”); National Association of Bond Lawyers: Letter from Allen K. Robertson, President, dated March 18, 2014 (“NABL”); National Association of Health and Educational Facilities Finance Authorities: Letter from Pamela Lenane, President, David J. Kates, Chapman and Cutler LLP, and Charles A. Samuels, Mintz Levin, dated March 10, 2014 (“NAHEFFA”); National Association of Independent Public Finance Advisors: Letter from Jeanine Rodgers Caruso, President, dated March 10, 2014 (“NAIPFA”); National Healthcare Capital LLC: Letter from Richard Plumstead, dated March 10, 2014; New York State Bar Association: Letter from Peter W. LaVigne, Chair of the Committee, dated March 12, 2014 (“NY State Bar”); Northland Securities, Inc.: Letter from John R. Fifield, Jr., Director of Public Finance/Senior Vice President, dated March 7, 2014 (“Northland”); Oppenheimer & Co. Inc.: E-mail from John Rodstrom dated March 10, 2014 (“Oppenheimer”); Parsons Brinckerhoff Advisory Services, Inc.: Letter from Mark E. Briggs, President, dated March 10, 2014 (“Parsons”); Piper Jaffray: Letter from Frank Fairman, Managing Director, Head of Public Finance Services, dated March 10, 2014 (“Piper Jaffray”); Public Financial Management, Inc.: Letter from John H. Bonow, Chief Executive Officer, dated March 10, 2014 (“PFM”); Public Resources Advisory Group: Letter from Thomas Huestis dated March 10, 2014 (“PRAG”); Raftelis Financial Consultants, Inc.: Letter from Lex Warmath dated March 10, 2014 (“Raftelis Financial”); Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated March 10, 2014 (“SIFMA”); Sutherland Asbill & Brennan LLP: Letter from Michael B. Koffler dated March 10, 2014 (“Sutherland”); Wells Fargo Advisors, LLC: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated March 10, 2014 (“Wells Fargo”); Winters & Co. Advisors, LLC: Letter from Christopher J. Winters dated March

Comment.[50] The comments are summarized below by topic and MSRB responses are provided. [51]

Standards of Conduct

Under Proposed Rule G-42(a), a municipal advisor would be subject to a duty of care as to its obligated person clients under subsection (a)(i) and a fiduciary duty as to its municipal entity clients under subsection (a)(ii) when engaging in municipal advisory

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10, 2014 ("Winters LLC"); WM Financial Strategies: Letter from Joy A. Howard, Principal, dated March 10, 2014 ("WM Financial"); Woodcock & Associates, Inc.: E-mail from Christopher Woodcock dated January 14, 2014 ("Woodcock"); Wulff, Hansen & Co. : Letter from Chris Charles, President, dated March 17, 2014 ("Wulff Hansen"); Yuba Group: Letter from Linda Fan, Managing Partner, dated March 7, 2014 ("Yuba"); Zion's First National Bank: Letter from W. David Hemingway, Executive Vice President, dated March 10, 2014 ("Zion").

50 Comments were received in response to the Second Request for Comment from: ABA: Letter from Cristeena Naser, Vice President, Center for Securities, Trust & Investments, dated August 25, 2014; ACEC: Letter from David A. Raymond, President and CEO, dated August 25, 2014; BDA: Letter from Michael Nicholas, Chief Executive Officer, dated August 25, 2014; Columbia Capital Management, LLC: Letter from Jeff White, Principal, dated August 25, 2014 ("Columbia Capital"); Dave A. Sanchez: Letter dated August 25, 2014 ("Sanchez"); Financial Services Roundtable: Letter from Richard Foster, Vice President and Senior Counsel for Regulatory and Legal Affairs, dated August 25, 2014 ("FSR"); Florida Division of Bond Finance: Letter from J. Ben Watkins III, Director, dated August 22, 2014 ("FLA DBF"); GFOA: Letter from Dustin McDonald, Director, Federal Liaison Center, dated September 2, 2014; ICI: Letter from Tamara K. Salmon, Senior Associate Counsel, dated August 19, 2014; Mr. Bart Leary: E-mail dated July 23, 2014 ("Leary"); Lewis Young: Letter from Laura D. Lewis, Principal, dated August 25, 2014; NAIPFA: Letter from Jeanine Rodgers Caruso, President, dated August 25, 2014; New York State Bar: Letter from Peter W. LaVigne, Chair of the Committee, dated August 27, 2014; Piper Jaffray: Letter from Frank Fairman, Managing Director, Head of Public Finance Services, dated August 25, 2014; SIFMA: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated August 25, 2014; Southern Municipal Advisors, Inc.: Letter from Michael C. Cawley, Senior Consultant, dated August 25, 2014 ("SMA"); Wells Fargo: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated August 25, 2014; WM Financial: Letter from Joy A. Howard, Principal, dated August 25, 2014; and Zion: Letter from W. David Hemingway, Executive Vice President, dated August 25, 2014.

51 The draft rule text included in the First Request for Comment is referred to herein as the "Initial Draft Rule;" the draft rule text included in the Second Request for Comment is referred to herein as the "Revised Draft Rule."

activities for such clients. Several commenters raised concerns relating to the proposed standards of conduct that would apply to municipal advisors.

Scope of the Fiduciary Relationship

In the First Request for Comment, the MSRB proposed that a municipal advisor be subject to a fiduciary duty when engaging in municipal advisory activities for municipal entity clients. Subsequently, in the Second Request for Comment, the MSRB asked whether the Revised Draft Rule should uniformly apply the proposed fiduciary standard to a municipal advisor in its relationships with all of its clients, including obligated persons. A number of commenters opposed extending the application of the fiduciary standard to municipal advisors in connection with their obligated person clients.[52]

The MSRB believes that the application of the fiduciary standard is appropriately limited to municipal advisors when engaging in municipal advisory activities for or on behalf of municipal entity clients and strikes the appropriate balance. Proposed Rule G-42 establishes a minimum standard, which, as noted by NABL, does not limit an obligated person client and its municipal advisor from agreeing to a higher standard of conduct, or incorporating other requirements or protections in the municipal advisory relationship.

Scope of the Duty/529 Plans

Proposed paragraph .01 of the Supplementary Material provides that a municipal advisor acting in accordance with the duty of care must undertake reasonable investigation to determine that it is not basing any recommendation made to a client on materially inaccurate or incomplete information. In response to the First and Second Request for Comment, ICI stated that municipal advisors to 529 college savings plans ("529 plans") should not be required to verify the veracity or completeness of the information provided to the municipal advisor by authorized state employees or officials who are authorized to act on behalf of the 529 plan. ICI requested that paragraph .01 of the Supplementary Material be revised not to require municipal advisors to investigate whether information is materially inaccurate or incomplete when it is provided to the municipal advisor by persons who are authorized by the client to act on behalf of a state's 529 plan.

Neither the First Request for Comment nor the Second Request for Comment contemplated that municipal advisors in municipal advisory relationships with 529 plans would be exempted or excluded, in whole or in part, from the proposed core standards of

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[52] See, e.g., comment letters from: ABA, BDA, Cape Cod Savings, Cooperman, GKB, Kutak, Lewis Young, NABL, NAHEFFA, Parsons, Piper Jaffray and SIFMA. A few commenters, including First River Advisory, NAIPFA and Yuba, supported the application of a fiduciary duty to a municipal advisor when engaging in municipal advisory activities on behalf of an obligated person client.

conduct, including aspects of the duty of care that a municipal advisor owes to a client. The MSRB believes that exempting municipal advisors from the proposed core standards of conduct would reduce the protections that Congress through the Dodd-Frank Act intended to provide to municipal entity clients and investors in 529 plan securities.

Fiduciary Duty – Authority

In response to the Second Request for Comment, Sanchez commented that the MSRB lacks the statutory authority to define "fiduciary duty" or to prescribe means designed to effectuate the performance of that duty.

As discussed above, the Exchange Act grants the MSRB statutory authority to adopt rules with respect to municipal advisors engaging in municipal advisory activities that are designed to, among other things, prevent fraudulent and manipulative acts and practices, and acts, practices or courses of business that are not consistent with a municipal advisor's fiduciary duty to its clients.[53] Accordingly, the MSRB has concluded that it is properly exercising the authority granted to it by statute.

Fiduciary Duty – Standards

In response to the First Request for Comment, NABL stated that the Initial Draft Rule should draw on established common law and similar standards that NABL believes are intended to provide substantive guidance regarding fiduciary duties (e.g., the standards applicable to attorneys), rather than the standards applicable to broker-dealers or registered investment advisers. NABL argued that the attorney-client relationship is more comparable to the municipal advisor-client relationship because both can have a wide spectrum of scopes of responsibilities, similar contexts in which there are interactions with the client, and a longer duration over which the representation occurs. BDA similarly believed that the fiduciary standards set forth in the Initial Draft Rule would not operate like other well-established standards, such as those for attorneys, and that the MSRB did not justify why the standards for municipal advisors would deviate from those standards as outlined in the Model Rules of Professional Conduct for attorneys ("Model Rules"). Accordingly, BDA suggested that Proposed Rule G-42 should adopt or parallel the same fiduciary duty standards used by other similarly situated professionals.

In developing Proposed Rule G-42, the MSRB consulted various codes of conduct and sources of federal and state law regarding the duties and obligations of a fiduciary that apply to professionals who are, or, in certain relationships, may be, fiduciaries. Some provisions of the proposed rule reflect principles incorporated from MSRB Rule G-17, including the duties of dealers to issuers, while other provisions were based on principles and requirements in the Investment Advisers Act. The MSRB believes the Investment Advisers Act is particularly relevant in developing a rule regarding fiduciary duties and

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[53] See, e.g., 15 U.S.C. 78o-4(b)(2)(C); and 15 U.S.C. 78o-4(b)(2)(L)(i).

obligations, and notes that the SEC also considered the Investment Advisers Act informative as it developed the SEC Final Rule.[54] Moreover, the MSRB believes it is important to establish rules and standards that address the practices of various types of municipal advisors and their clients, and that the provisions addressing the duties and obligations of a fiduciary are tailored to address the unique characteristics of the municipal securities market and the variety of responsibilities undertaken by municipal advisors in their relationships with municipal entity and obligated person clients. The MSRB notes that, to the extent that Proposed Rule G-42 does not specifically prescribe or prohibit certain conduct, or address certain activity, common law regarding fiduciary obligations and duties may be referenced by a judicial or adjudicatory decision-maker.

Fiduciary Duty – Obligated Persons

A number of commenters raised concerns that Proposed Rule G-42 implicitly and inappropriately imposes fiduciary duty obligations on municipal advisors whose clients are obligated persons without a demonstrated need for a more robust regulatory framework than that adopted by Congress or the SEC.[55] Those commenters believed that the treatment accorded to obligated persons should be distinguished from that accorded to municipal entities because, as they stated, obligated person clients do not handle public funds, are private, domestic and international for-profit companies or not-for-profit businesses, and, therefore, operate with a different level of public accountability. Overall, these commenters believed that fiduciary duties should not be mandatorily extended to benefit obligated persons.

NAHEFFA suggested that the duty of care and the requirements of the Initial Draft Rule G-42(b)-(f) be revised to state that municipal advisors owe a fiduciary duty only to their municipal entity clients. In the alternative, NAHEFFA requested that the MSRB provide clarification on the legal and practical distinctions among the standards and duties and obligations of municipal advisors vis-à-vis both types of clients, including a clarification that an alleged violation of the duty of care would be subject to review under a negligence standard and an alleged violation of the duty of loyalty would require evidence of intent. Generally, NAHEFFA supported either a revised Rule G-42, or a separate rule that would simplify and reflect the duties and obligations of a municipal advisor with respect to its obligated person clients. NAHEFFA suggested that, as to obligated person clients, the duty should be to exercise professional judgment and expertise in providing services and to deal fairly with its clients. Similarly to NAHEFFA, BDA requested that the MSRB revise Proposed Rule G-42 to more clearly state and

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54 See generally, SEC Final Rule, 78 FR 67467.

55 See letters from: ABA, BDA, Cape Cod Savings, GKB, Kutak, Lewis Young, NABL, NAHEFFA, Parsons, Piper Jaffray, Sanchez and SIFMA. On the other hand, NAIPFA, First River Advisory and Yuba supported imposing fiduciary duties upon municipal advisors with respect to the advice they provide to obligated persons.

distinguish between the duties and obligations that municipal advisors would owe to each of the two types of clients.

ABA commented that the MSRB lacked the requisite authority to impose a fiduciary duty on municipal advisors with respect to their obligated person clients, and that even if it had the authority, such a standard would be unworkable since banks would have difficulty identifying which of their many customers were obligated persons. ABA stated that the extension of a fiduciary duty to municipal advisors in their relationship with their obligated person clients would result in a significant risk that banks would inadvertently violate regulatory requirements by becoming an unwitting municipal advisor with respect to a client they did not know was an obligated person. Moreover, the banks would run the corresponding risk of violating the attendant fiduciary duty applicable to such municipal advisor.

More specifically, Sanchez commented that the language in Revised Draft Rule G-42(b)(i)(A) and (b)(i)(G) appeared to import the duty of loyalty and duty of care into representations of obligated persons by using the phrase "unbiased and competent advice" with respect to advice provided to or on behalf of obligated persons. He suggested that these provisions be revised to say "impair its ability to render advice to or on behalf of the obligated person in accordance with the standards of conduct required in clause (a)" in lieu of the phrase referencing "unbiased and competent advice."

Neither the Initial Draft Rule nor the Revised Draft Rule would deem municipal advisors to owe a fiduciary duty to obligated person clients, and the MSRB disagrees with the view that either the Initial or Revised Draft Rule implicitly and inappropriately imposed fiduciary duty obligations to such clients. After carefully considering the comments, the MSRB has not modified Proposed Rule G-42(a), on standards of conduct. Further, Proposed Rule G-42 follows the approach taken in the Dodd-Frank Act, deeming a municipal advisor to owe a fiduciary duty only to its municipal entity clients. However, although the Exchange Act fiduciary duty standard would not apply to a municipal advisor advising an obligated person client, all municipal advisors are subject to fair-dealing obligations under MSRB Rule G-17, which already requires a municipal advisor to deal fairly with all persons and prohibits engaging in any deceptive, dishonest or unfair practice. Moreover, the provisions in Proposed Rule G-42(b)-(f) appropriately establish the duties and obligations of municipal advisors. The MSRB notes that these duties are, in part, based on similar existing duties for other regulated entities (e.g., underwriters' duties to issuers), which are separate and apart from a fiduciary duty. Therefore, the MSRB does not believe Proposed Rule G-42 creates an implicit fiduciary duty for municipal advisors with respect to the advice they provide to obligated person clients.

The MSRB agrees with Sanchez's specific comments regarding paragraphs (b)(i)(A) and (b)(i)(G) of the Revised Draft Rule and has revised the proposed rule change to clearly differentiate between the handling of conflicts of interest under the duty of loyalty, as discussed in paragraph .02 of the Supplementary Material, and conflicts under the disclosure requirements that are applicable to all municipal advisory clients as part of a municipal advisor's duty of care, as discussed in paragraph .01 of the

Supplementary Material. Specifically, under proposed subsection (a)(ii), the duty of loyalty in the proposed rule change, a municipal advisor must not engage in municipal advisory activities with a municipal entity client if it cannot manage or mitigate its conflicts of interest in a manner that will permit it to act in the municipal entity's best interests. Conversely, under proposed section (c) of Proposed Rule G-42 and as discussed further with respect to proposed paragraph .05 of the Supplementary Material, a municipal advisor can continue to serve as a municipal advisor to its municipal entity or obligated person client when an actual or potential conflict of interest that could be reasonably anticipated to impair its ability to provide that advice exists, so long as such conflict of interest is disclosed and addressed in accordance with the relevant provisions of Proposed Rule G-42[56] and the municipal advisor can satisfy the applicable standards of conduct described in section (a).

NAHEFFA requested that the MSRB clarify the legal distinctions between the duty of care and duty of loyalty, and suggested that the state of mind standard to determine a violation of the duty of care should be negligence, and the state of mind standard regarding a violation of the duty of loyalty should be intent. In response to NAHEFFA's request for clarification regarding such standards, the MSRB believes it would be appropriate for the courts and other adjudicatory authorities to determine the "state-of-mind" elements when applying the standards of conduct of Proposed Rule G-42 to specific sets of facts and circumstances presented, drawing on existing jurisprudence regarding analogous duties of care and fiduciary obligations.

In response to ABA's comment, the MSRB again notes that determining which activities constitute municipal advisory activities requires a legal interpretation of the SEC Final Rule. Such authority is vested with the SEC rather than the MSRB.

Finally, the MSRB notes again that the standards of conduct in Proposed Rule G-42 would be minimum requirements, which the MSRB has developed to empower the client to a large extent to determine the scope of services and control the engagement with the municipal advisor, and as suggested by NABL, any municipal advisor and its client may agree to more stringent standards of conduct for their specific engagement.

Duty of Care – Supplementary Material .01

In response to the Second Request for Comment, WM Financial challenged the requirement that a municipal advisor "undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information." While WM Financial agreed that a municipal advisor should make a

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[56] Municipal advisors would be required to disclose and document such a material conflict of interest under Proposed Rule G-42(b) and (c) and paragraph .05 of the Supplementary Material. With respect to municipal entity clients, municipal advisors also would need to provide an explanation to the client of how the municipal advisor intends to manage or mitigate its conflict in a manner that will permit it to act in the municipal entity's best interests.

reasonable investigation in order to determine whether a recommendation is in a client's best interest, WM Financial believed that a municipal advisor should be able to rely on publicly-available documents as being true and accurate, and should be able to assume that any additional information provided to it by the municipal entity is also true and accurate. WM Financial believed that requiring the municipal advisor to verify the accuracy of the information it receives from a client imposes an inappropriate burden. As noted above, ICI similarly opposed the requirement in the context of 529 plans, for which the municipal advisor that is also acting as a plan sponsor would typically work with and rely upon state employees who are authorized to represent a state's plan and requested revisions to paragraph .01 of the Supplementary Material.

Proposed paragraph .01 of the Supplementary Material would provide, as a core general standard, that a municipal advisor must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. There is no exception for information that is provided to the advisor by the client. The MSRB believes that the provisions of proposed paragraph .01 of the Supplementary Material remain appropriate and, as discussed above, does not believe that advisors to 529 plans should be relieved from an obligation to inquire as to the accuracy of material that is relevant to a municipal advisor's recommendation provided by its client or other parties. The MSRB further believes this provision of proposed paragraph .01 of the Supplementary Material would provide an objective standard for when it is appropriate for a municipal advisor to rely on information provided by a client when making a recommendation to such client, including representatives of a 529 plan authorized to act on behalf of the plan. Finally, because proposed paragraph .01 would require municipal advisors to undertake only a "reasonable investigation" of the veracity of the information on which it is basing a recommendation, municipal advisors would not be required to go to the impractical lengths suggested by commenters. The MSRB believes this standard would be sufficient to allow municipal advisors to assess their risk exposure to any reliance on that information and determine what potential mitigating actions need to be taken.

Sanchez also commented that the MSRB should "consider whether the information for which 'a municipal advisor must have a reasonable basis for' incorporated in [subparagraphs] (a) through (c) [of paragraph .01 of the Supplementary Material] is not already addressed in the standards of conduct required of municipal advisors by MSRB Rule G-17 and general antifraud rules related to municipal securities disclosure." As such, he suggested deleting those provisions of paragraph .01 of the Supplementary Material to avoid unnecessarily duplicative regulatory requirements. The MSRB has decided to retain those provisions because it believes they would provide additional guidance regarding the proposed duty of care and would assist municipal advisors in satisfying that duty without unnecessarily duplicating the principles of MSRB Rule G-17 or other federal securities anti-fraud statutes.

Finally, SIFMA noted that, while the requirement for a municipal advisor to make a reasonable inquiry -- regarding the facts that are relevant to a client's determination to pursue a particular course of action or that form the basis of any advice to the client --

could be appropriate in the context of arranging a municipal securities issuance, it could be cost prohibitive in the case of ordinary brokerage and related advice, given the number of trades potentially involved, timing considerations and the general context of broker-related advice. Therefore, SIFMA did not believe that such a standard should be applied in addition to otherwise applicable suitability requirements that would attach to recommendations made in the context of brokerage/securities execution services. The MSRB believes that the duties and standards in the proposed rule are appropriately applied to municipal advisory activities (other than the undertaking of a solicitation), and notes that a municipal advisor to a municipal entity client will owe a statutory fiduciary duty to the client. If the conduct SIFMA describes constitutes the giving of advice under the SEC rules providing for the registration of municipal advisors as discussed in the SEC Final Rule,[57] then Proposed Rule G-42 would apply in its entirety. Likewise, if such conduct did not constitute the giving of advice under those rules, then Proposed Rule G-42 would not apply.

Duty of Loyalty – Supplementary Material .02

In response to the First Request for Comment, ACEC and APTA indicated that they believed there are circumstances when the duty of loyalty could directly conflict with an engineer's professional and ethical responsibilities, and expressed concerns as to how such conflicts could affect engineering firms' business. Both ACEC and APTA specifically stated that, in the course of providing professional engineering services to a client, circumstances could arise in which the engineer would find himself or herself facing a conflict between breaching its fiduciary duty in its role as municipal advisor and violating the ethical obligations to which the engineer is subject under applicable state law and regulation, or one or more professional associations. According to ACEC, in such circumstances, it would be detrimental to the health, safety and welfare of the public to prioritize the fiduciary duty the engineer municipal advisor owed to its client. ACEC argued that paragraph .02 of the Supplementary Material, therefore, would not serve the public interest and requested that the MSRB address how this type of conflict could be managed.

The MSRB notes that SEC Rule 15Ba1-1(d)(2)(v) excludes engineers providing engineering advice from the definition of municipal advisor.[58] The MSRB further notes that the same and similar issues raised by the commenters in response to the First Request for comment also were raised with the SEC during its rulemaking to establish the registration regime for municipal advisors. In the SEC Final Rule, the SEC provided greater clarity to engineers concerning the definition of "municipal advisor" and the scope of the exclusion for engineers.[59] If, given that guidance, an engineer were in fact to

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57 See generally, SEC Final Rule, 78 FR 67467.

58 See 17 CFR 240.15Ba1-1(d)(2)(v). See also 15 U.S.C. 78o-4(e)(4)(C).

59 See SEC Final Rule, 78 FR at 67529-32.

engage in municipal advisory activities, it would be subject to the statutory fiduciary duty to a municipal entity client, and, in the MSRB's view, appropriately subject to the duty of loyalty provisions in Proposed Rule G-42. Under certain circumstances, if a material conflict of interest would prevent the municipal advisor from being able to act in accordance with the standards of conduct of section (a) of Proposed Rule G-42, which the MSRB believes would be rare, the firm might need to determine not to provide municipal advice if it preferred to provide engineering services.

Disclosure of Conflicts of Interest

The MSRB received a number of comments regarding section (b) of Proposed Rule G-42 on required disclosures of material conflicts of interest by municipal advisors to their clients. Generally, commenters were supportive of, or did not express an objection to, requiring municipal advisors to provide written disclosure of material conflicts of interest. However, some commenters did express concerns about some of the facets of the disclosure requirements; those concerns are described below and followed by the MSRB's response.

Compensation Arrangements

Several commenters expressed concern regarding paragraph (b)(i)(F) of Proposed Rule G-42, which requires municipal advisors to disclose conflicts of interest arising from compensation arrangements that are contingent on the size or closing of any transaction as to which the municipal advisor is providing advice.

Commenting on the Initial Draft Rule, Lewis Young stated that contingent fee arrangements benefit clients, particularly smaller municipal entities, because they allow municipal entity clients to finance the costs of the municipal advisor with the proceeds of the issuance. In their view, characterizing a contingent fee arrangement as a conflict of interest requiring disclosure to the client amounted to advising a client that the municipal advisor may not be acting in the client's best interest. They added that they believe the disclosure requirement would serve no useful purpose and could confuse clients. Sutherland stated that the Initial Draft Rule's required disclosure of contingent fee arrangements was duplicative of SEC Form MA[60] and, therefore, unnecessarily burdensome, and should be deleted.

Commenting on the Revised Draft Rule, Columbia Capital stated that the provision "creates the appearance that the MSRB takes the position that one fee modality is less preferable to all others." Columbia Capital, Cooperman and Piper Jaffray commented that the proposed rule change should not single out one fee arrangement as being preferable to others. Columbia Capital, Cooperman and Piper Jaffray also contended that fee arrangements of any sort (hourly, fixed or non-contingent) create an adversarial relationship between the municipal advisor and its client. In Piper Jaffray's view, the potential conflicts of interest that are inherent in all fee arrangements are also

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[60] See SEC Form MA, Items 4.H. - 4.J.

"generally knowable" to both sides of a transaction and, therefore, the Revised Draft Rule's disclosure requirement would not be beneficial. Columbia Capital suggested deleting the provision.

WM Financial also expressed concerns regarding paragraph (b)(i)(F) of the Revised Draft Rule, but differed in its reasoning from Columbia Capital and Piper Jaffray. WM Financial disagreed with the premise that all fee structures create some conflict of interest. Rather, WM Financial stated that, because municipal advisors would be required to "act in the best interest of their clients . . . good advice will prevent a fee arrangement from creating a 'conflict'." In their view, a "conflict of interest does not exist when payment of fees is based on the success of services to be provided . . . ." Like Lewis Young, WM Financial stated that contingent fees serve a valuable function because they allow small municipal entity clients to finance the cost of the municipal advisor with the proceeds from the issuance and ensure that the cost of the municipal advisor is only incurred after the successful completion of the issuance. WM Financial also requested that paragraph (b)(i)(F) be deleted.

The MSRB has considered the arguments and alternatives advanced by commenters and determined that requiring the disclosure of conflicts of interest arising from fee arrangements contingent on the size or closing of the transaction as to which the municipal advisor is providing advice is an appropriate and necessary measure to alert municipal entity and obligated person clients to the potential conflict of interest inherent in such fee arrangements. While the MSRB recognizes, as some commenters pointed out, that other fee arrangements (such as hourly, fixed or otherwise non-contingent) might also give rise to conflicts, the MSRB believes that the potential harm to a client may be particularly acute if a client is not informed of a conflict of interest arising from a contingent fee arrangement. Furthermore, the MSRB does not agree with commenters that have argued that requiring a conflict of interest disclosure would suggest that the municipal advisor is not acting in the best interest of its client. The purpose of the disclosure requirement in proposed paragraph (b)(i)(F) simply would be to allow a municipal advisor's client to make an informed decision based on relevant facts and circumstances. Also, under the proposed rule change, municipal advisors would have the opportunity to provide a client with additional context about the benefits and drawbacks of other fee arrangements in relation to a contingent fee arrangement so that the client could choose a fee arrangement that serves its needs.

Disclosure of Conflicts of Interest to Investors

The MSRB received comments that called for the deletion of a provision set forth previously in the Revised Draft Rule as paragraph .08 of the Supplementary Material. Under the provision, if all or a portion of a document prepared by a municipal advisor or any of its affiliates were included in an official statement for an issue of municipal securities by or on behalf of a client of the municipal advisor, the municipal advisor would have been required to provide written disclosure to investors of any affiliation that would be a material conflict of interest under paragraph (b)(i)(B) of the Revised Draft

Rule. The disclosure requirement also could have been satisfied if the relevant affiliate provided the written disclosure to investors.[61]

SIFMA supported deleting the disclosure requirement, noting that "[m]unicipal advisors and their affiliates may have no contractual or other relationships (and in many cases have no form of privity) with investors, nor do they control the content of the Official Statement." SIFMA stated that it is the obligation of the issuer "to make sure that its disclosure is materially accurate and complete" and the responsibility of broker-dealers to comply with their obligations under applicable law. SIFMA observed that the municipal advisor is already required to provide the issuer with the same conflict disclosure under paragraph (b)(i)(B), arguing that the MSRB should leave the decision of whether to include such information in material distributed to investors to the issuer.

ICI and NABL also commented in favor of deleting the requirement. ICI provided comments similar to SIFMA's comments in response to both the Initial and Revised Draft Rules, but focused on how the required disclosure to investors would impact municipal advisors advising 529 plans. ICI supported requiring municipal advisors to disclose conflicts of interest to the municipal advisor's client but questioned why such information would be relevant to a person investing in 529 plan securities. ICI stated that if "all material terms and conditions of the 529 plan offering already are disclosed in the offering document that is provided to investors and potential investors, this supplemental disclosure would not provide any additional protection to investors." In response to the First Request for Comment, NABL contended that requiring these disclosures would run contrary to the intent of the Dodd-Frank Act, which is to protect issuers. NABL suggested, as an alternative, that issuers be allowed to choose whether to disclose the conflicts of interest to investors.

The MSRB agrees with the commenters and notes that the provision could put municipal advisors in the impractical position of being required to make conflict of interest disclosures directly to investors or include the content of such disclosures in an issuer's official statement, although the municipal advisor may not have the authority or the means to do so. Moreover, because the proposed rule change would already require the municipal advisor to disclose all material conflicts of interest to the issuer, the MSRB believes the issuer will be well positioned to make the determination of whether to include such information in the official statement or other investor disclosure documents, consistent with the issuer's duties under all applicable law. In light of the comments and after a re-evaluation of the purpose and feasibility of the disclosure provision in the supplementary material as described above, the MSRB has deleted the provision.

Acknowledgment or Consent to Conflicts of Interest Disclosure

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[61] Paragraph (b)(i)(B) of the Revised Draft Rule required written disclosure of "any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor."

In response to the First Request for Comment, several commenters suggested differing approaches to the question of whether municipal advisors should be required to obtain some form of acknowledgment from their client of the conflicts of interest disclosures that municipal advisors are required to make under the proposed rule change.

In response to the First Request for Comment, NABL commented that the MSRB should follow the approach taken in the Model Rules of Conduct of the American Bar Association regarding the disclosure of conflicts of interest as stated in the Initial Draft Rule. NABL argued that municipal advisors should be required to obtain "informed consent, confirmed in writing" to each potentially waivable material conflict of interest. NABL stated that this standard is as appropriate for municipal advisors as it is for common law fiduciaries or attorneys. NABL suggested that the "informed consent" it advocated could be accomplished in several ways, including "a writing evidencing an engagement, including a letter of intent, after disclosure to the client sufficient to establish informed consent." NABL contended that informed written consent from a municipal advisor's client is "a necessary corollary to the requirement that an advisor disclose and provide sufficient detail about the nature of all material conflicts of interest." NABL also noted that informed consent confirmed in writing would be consistent with the requirements of the CFTC for commodity trading advisors. NAIPFA stated that it believed municipal advisors should be required to obtain an acknowledgment from their clients of the conflicts of interest that it has disclosed, saying that this would conform to the obligations of underwriters and other "professionals possessing fiduciary duties." GFOA provided similar support for requiring an acknowledgment of the conflicts of interest disclosures from the municipal advisor's client but stated that, if such a requirement was added to the proposed rule change it would expect an explanation within the proposed rule change detailing how the acknowledgements of such conflicts relate to a municipal advisor's fiduciary duty.

In contrast to NABL, NAIPFA and GFOA, commenters including Cooperman, Lewis Young and Acacia commented that municipal advisors should not be required to obtain a written acknowledgment of disclosures before proceeding with the engagement. Cooperman stated that acknowledgement of conflicts of interest disclosures from municipal entity clients is an unnecessary and unjustified requirement that should be removed. Lewis Young stated that such written disclosure should not be required "so long as the disclosures provided are not objected to by the client." Proposing a somewhat different approach, Acacia stated that municipal advisors should not be required to obtain a written acknowledgement of the conflicts disclosed but should be required to (i) provide such information (and record such provision), (ii) request receipt and consent but (iii) be permitted to proceed with a municipal advisory engagement in the absence of such receipt and consent if the municipal advisor has a reasonable belief that such information has been received. Acacia reasoned that its approach would be analogous to existing MSRB guidance for underwriters under MSRB Rule G-17.

The proposed rule change would not require a municipal advisor to obtain written acknowledgement from its client of the disclosure of conflicts of interest. While the MSRB understands the concerns expressed by commenters, the MSRB believes that the

proposed rule change sufficiently obligates municipal advisors to ensure that their clients receive proper notice of material conflicts of interest. Proposed paragraph .05 of the Supplementary Material, for instance, would require municipal advisors to provide information sufficiently detailed to inform a client of the nature, implications and potential consequences of each conflict, and include an explanation of how the municipal advisor addresses or intends to manage or mitigate each conflict. Such disclosure would allow a municipal advisor's client to make an informed decision as to whether such conflicts can be adequately managed or mitigated. Furthermore, a municipal advisor's duty of care would require an advisor to have a reasonable basis for believing that its client received the disclosure and understood the nature, implications and potential consequences of the conflicts of interest that the municipal advisor disclosed. Further, the MSRB believes that obtaining some form of written acknowledgement from municipal entities and obligated persons would prove to be a significant procedural burden to both municipal advisors and their clients that would likely not result in a substantiated benefit.

Explanation of Mitigating Conflicts of Interest

As discussed above, proposed paragraph .05 of the Supplementary Material to Proposed Rule G-42, on conflicts of interest, would require a municipal advisor to include an explanation of how the municipal advisor would address, or manage or mitigate, the material conflicts of interest that it has disclosed to its client. In response to the Second Request for Comment, Sanchez challenged the value and purpose of this requirement by opining that municipal securities brokers and dealers are not subjected to the burden of making such disclosures. Sanchez requested that the MSRB revise the proposed rule change to require such disclosures only if requested by the client.

The MSRB has considered Sanchez's comments and determined not to amend proposed paragraph .05 of the Supplementary Material because the MSRB believes that the provision would serve a beneficial and protective function for clients. The municipal advisor's explanation would allow its client to adequately assess the potential effects the conflicts of interest could have on an engagement with the municipal advisor and to determine whether the actions the municipal advisor proposes to take to mitigate the conflicts of interest are sufficient and will not overly impair the quality and neutrality of the services to be performed by the municipal advisor.

Services for Conduit Issuers and Obligated Person Clients

Under subsection (e)(ii) of Proposed Rule G-42, a municipal advisor would be precluded from serving its municipal entity client as underwriter for a transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice to the municipal entity.

In response to the Second Request for Comment, BDA commented that the proposed rule should explicitly allow a dealer/municipal advisor to serve as an underwriter for a conduit issuer and as a municipal advisor for the conduit borrower, even with respect to directly related matters.

Underwriting such a transaction would not be specifically prohibited by the ban on principal transactions in subsection (e)(ii) of Proposed Rule G-42, because it applies only in cases of municipal entity clients. A conduit borrower is typically not a municipal entity. Thus, depending on the specific facts and circumstances, this scenario could be permissible with appropriate disclosure and consent. Still, it is not clear that, even with disclosure and consent, such activity would be categorically consistent with all of the duties of a municipal advisor to an obligated person in all circumstances. Therefore, the MSRB has not amended the proposed rule as suggested by BDA.

Material Conflicts of Interest Required to be Disclosed

Section (b) of Proposed Rule G-42 would include a non-exhaustive list of matters that would always constitute material conflicts of interest and that would be required to be disclosed by municipal advisors under the proposed rule change. Matters that must be disclosed as material conflicts of interest under section (b) include, among others: any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client; any payments made by the municipal advisor, directly or indirectly, to obtain or retain an engagement to perform municipal advisory activities for the client; any conflicts of interest arising from compensation for municipal advisory activities to be performed that is contingent on the size or closing of any transaction as to which the municipal advisor is providing advice; and any legal or disciplinary event that is material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel.

In response to the First Request for Comment, Lewis Young stated that the proposed rule should only require disclosure when an actual conflict of interest exists because providing tailored explanations of potential or hypothetical situations would be "expensive, time consuming, and not very helpful." The MSRB disagrees and believes that the likely benefits from these disclosures will outweigh the cost associated with providing them to a municipal advisor's clients because the proposed rule change limits the required disclosure to only material conflicts of interest, both actual and potential, of which a municipal advisor is aware of after a reasonable inquiry. The MSRB also believes that requiring a municipal advisor to disclose conflicts of interest, actual and potential, that the municipal advisor becomes aware of after reasonable inquiry and that could reasonably be anticipated to impair the municipal advisor's ability to provide advice in accordance with the standards of conduct in section (a) of the rule, is necessary to provide clients with the requisite information to make an informed decision regarding the selection of their municipal advisor.

ICI suggested adding prefatory language to section (b) that would clarify that a municipal advisor would be required to disclose only conflicts of interest that are applicable to its relationship with the specific client. ICI stated that adding such language would harmonize section (b) with the approach taken in the Investment Advisers Act

regarding the delivery of brochures,[62] which it believed permits an investment adviser to omit "inapplicable information" from a disclosure it is required to provide to clients. The MSRB believes that Proposed Rule G-42 makes clear that municipal advisors are required only to make disclosure of material conflicts of interest and that this would exclude inapplicable information.

First Southwest expressed concern regarding the requirement of subsection (b)(i) that municipal advisors must provide written notice when they have no material conflicts of interest to disclose to their clients. First Southwest stated that the requirement would increase administrative requirements and provide little, if any, benefit in the event a conflict of interest were later discovered. The MSRB disagrees and believes that an affirmative written statement by the municipal advisor that it has no known material conflicts of interest would remove potential ambiguities about the completeness of the conflicts disclosure.

Sutherland commented that the conflicts of interest required to be disclosed would be duplicative of information that could be found in SEC Forms MA and MA-I and, therefore, would be unnecessary. As an example, Sutherland stated that SEC Form MA requires the disclosure of affiliated business entities; compensation arrangements; and proprietary interests in municipal advisor client transactions.[63] While some overlap could exist, the MSRB believes that the SEC forms do not solicit all of the information that would be required by the proposed rule change and, thus, would not serve as a sufficient substitute. Specifically, the SEC forms would not be a viable proxy for disclosing potential conflicts of interest that the municipal advisor could have, nor would the forms contain an explanation of how they intend to mitigate the material conflicts of interest that they disclose. The MSRB expects that the written disclosure of material conflicts of interest will be a useful tool to municipal advisor clients that will allow them to readily assess the impact of actual or potential conflicts of interest of potential or ongoing municipal advisory activities.

In response to the Second Request for Comment, SIFMA requested clarification regarding the standard for determining the materiality of the conflicts of interest described in paragraphs (b)(i)(A) and (G), and when disclosure is required. Under the Revised Draft Rule, paragraphs (b)(i)(A) and (G) required municipal advisors to disclose "any . . . potential conflicts of interest . . . that might impair" a municipal advisor's advice or its ability to provide advice in accordance with section (a) of Proposed Rule G-42. The language in these paragraphs concerned certain commenters, such as SIFMA, because they believed that such a standard would include nearly all imaginable conflicts of interest and result in overly broad disclosure that could distract from the provision's purpose. Therefore, to clarify, the MSRB has amended these paragraphs to state that disclosure is required, in paragraph (A) for "any actual or potential conflicts of interest," and, in paragraph (G), for "any other engagements or relationships." The MSRB believes

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62 See 17 CFR 275.204-3.

63 See SEC Form MA, Items 1.K., 4.H.-4.J. and 7.A.-7.F., respectively.

that this revised language would more clearly establish a limiting, objective standard for disclosing certain conflicts of interest that would be relevant to a municipal advisor's client.

Further, paragraphs (b)(i)(A) and (G), as proposed, are revised to limit the disclosure of conflicts required under paragraphs (b)(i)(A) and (G) to those that potentially impact the advisor's ability to provide "advice to or on behalf of the client in accordance with the standards of conduct of section (a) of this rule, as applicable." Previously, under the Revised Draft Rule, paragraphs (b)(i)(A) and (G) required a municipal advisor to provide disclosure of conflicts of interest that "might impair its ability either to render unbiased and competent advice to" its clients. This revision was made after re-evaluation of the phrasing used in the paragraphs and consideration of comments received from Sanchez. Sanchez stated that the use of the phrase "unbiased and competent advice" in the Revised Draft Rule ". . . . appear[s] to import the duty of loyalty and duty of care into the representations of obligated persons. . . ." The MSRB agrees that the use of the phrasing "unbiased and competent advice" does not encompass all of the duties municipal advisors owe their clients, nor would it sufficiently differentiate between the standards of conduct owed by municipal advisors to their municipal entity clients and obligated person clients. The MSRB believes that the revised standard for identifying material conflicts of interest under proposed paragraphs (b)(i)(A) and (G) will more clearly reflect the standards of conduct in proposed section (a) and appropriately differentiate between municipal entity and obligated person clients.

In response to the Second Request for Comment, Sanchez also suggested a revision to clarify the last sentence of subsection (b)(i) of the Revised Draft Rule. Sanchez suggested deleting the term "written documentation" and using "written statement" instead to clarify for municipal advisors the action required to comply with subsection (b)(i). To remove any ambiguity, the MSRB has revised proposed subsection (b)(i) to clarify that, when appropriate, a municipal advisor must provide a "written statement" that the municipal advisor has no known material conflicts of interest.

Columbia Capital requested clarification regarding whether the disclosures required by the Revised Draft Rule may be made in more than one document. The required disclosures indeed may be provided to clients in more than one document, as long as the document and its delivery otherwise comply with the proposed rule. Because the language of the proposed rule is not to the contrary, the MSRB has not made any revisions in response to this comment.

FSR commented that use of the term "indirectly" in paragraph (b)(i)(B) in the Revised Draft Rule, which required disclosure of "any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor," expanded the scope of the required disclosures unnecessarily and would make compliance difficult for a municipal advisor that is part of a large multi-service financial conglomerate. FSR believed that the Revised Draft Rule did not provide municipal advisors with sufficient guidance to identify activity that could be indirectly

related to municipal advisory activities, and, taken in its plain meaning, could lead to a substantial burden on firms having numerous affiliates that provide a wide array of services. After further consideration of the purpose and intent of the proposed paragraph, the MSRB has removed the clause "or indirectly." The MSRB believes revised proposed paragraph (b)(i)(B) will provide the appropriate notice to clients of the relationships of any affiliates of the municipal advisor that are likely to present material conflicts of interest.

Disclosure of Legal or Disciplinary Events

Several commenters addressed the draft requirements to disclose legal or disciplinary events. FSR commented that subsection (b)(ii) of the Revised Draft Rule would require a separate written disclosure of legal or disciplinary events that is redundant of the requirements of subsection (c)(iii) of the Revised Draft Rule. FSR requested that "these disclosure requirements be deemed satisfied if an advisor provides information about where clients may access electronically the advisor's most recent [SEC] Forms MA and MA-I, along with the date of the last material amendment to any legal or disciplinary event disclosure on such forms." SIFMA, in response to the Second Request for Comment, similarly stated that requiring "[duplicative] disclosure of specific events that are already disclosed in [SEC] Forms MA and MA-I provides little, if any, benefit to municipal entities or obligated persons, while it imposes unnecessary additional burdens on municipal advisors." SIFMA suggested that providing clients with the information regarding how to obtain electronic access to a municipal advisor's legal and disciplinary history on SEC Forms MA and MA-I should suffice. Sanchez stated, regarding the Revised Draft Rule, that "[t]his requirement appears to be overly burdensome . . . , [and] it should be sufficient for purposes of this rule that a municipal advisor be required to direct clients to their EDGAR filings by providing clients with sufficiently specific information to locate their EDGAR filings." [64]

The MSRB contemplated that municipal advisors would be able to satisfy their disclosure of legal and disciplinary events under sections (b) and (c) of the Revised Draft Rule with specific reference to the relevant portions of their most recent SEC Forms MA or MA-I filed with the Commission. Proposed Rule G-42(b)(ii) further clarifies this intention, and requires the municipal advisor to provide detailed information specifying where the client may electronically access such forms. The MSRB believes this approach will address the issue of duplicative disclosure of the disciplinary and other legal events contained in SEC Forms MA and MA-I. This revision also clarifies that municipal

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64 In response to the First Request for Comment, Sutherland suggested that there is sufficient disclosure about disciplinary history provided in a municipal advisor's SEC Forms MA and MA-I filed with the SEC, and Parsons stated that disclosure should not be required in the rule given such public disclosure on those forms. Similarly, Lewis Young and NAIPFA believed the disclosure of legal or disciplinary events would be duplicative and unnecessarily burdensome and also suggested that municipal advisors should be able to satisfy the requirement by referencing SEC Forms MA or MA-I.

advisors may satisfy the disclosure requirements of subsections (b)(ii) and (c)(iii) in a similar fashion.

A municipal advisor could, conceivably, simultaneously satisfy the requirements of proposed subsections (b)(ii) and (c)(iii) in one document if it were provided to the client prior to or upon engaging in municipal advisory activities for the client. However, if combined written disclosure and relationship documentation were made after a municipal advisor engages in municipal advisory activities, the municipal advisor would only be in compliance with proposed subsection (c)(iii) and not subsection (b)(ii).

SIFMA also suggested that subsection (c)(iv) of the Revised Draft Rule should be removed. The subsection would require municipal advisors to document the date of the last material change, including any addition, to the legal or disciplinary event disclosures on any SEC Form MA or MA-I filed with the Commission. Specifically, SIFMA believed that requiring municipal advisors to update their written disclosures and documentation with each of their municipal advisory clients whenever a material change to a legal or disciplinary event was made to any SEC Forms MA or MA-I would be unjustified.

Proposed section (c) requires the documentation of the municipal advisory relationship to be promptly amended or supplemented to reflect any material changes or additions, and requires the amended documentation or supplement to be promptly delivered to the municipal entity or obligated person client. However, the MSRB does not believe the update requirement under proposed section (c) is overly burdensome because municipal advisors need only provide the date of the last material change, including any addition, to their legal or disciplinary event disclosure to their clients, as they would be permitted to reference their SEC Forms MA and MA-I for the details of such material changes. Additionally, the required documentation of the municipal advisory relationship could be satisfied through the use of more than one writing and updates or amendments to such documents could be additional, separate writings that either amend or supplement earlier writings. The MSRB believes these accommodations sufficiently address the concern that municipal advisors would be required to amend and redistribute a single writing every time a material change or addition needed to be included. Further, the MSRB believes that, by requiring municipal advisors to update the written documentation relating to legal or disciplinary event disclosures provided to municipal entities and obligated persons, proposed subsection (c)(iv) would help ensure that those clients have sufficient, accurate and current information to better inform their decisions to engage and/or continue engaging a municipal advisor. The MSRB notes that the requirements of proposed section (c) must be made in writing and delivered to the municipal advisor's client in accordance with the duty of care and, as applicable, the duty of loyalty.

Coastal, Kutak and Parsons objected to the Initial Draft Rule's requirement to disclose the legal and disciplinary events for all individuals at a municipal advisory firm for which the firm is required to submit an SEC Form MA-I. They suggested that municipal advisors should not be required to disclose to a client legal and disciplinary events that relate to an individual that is employed by the municipal advisor, if that

individual is not a part of (or reasonably expected to be a part of) the advisor's team working for the client. Although there could be numerous municipal advisors with large numbers of employees, as Coastal indicated, the MSRB believes there is insufficient cause to narrow the requirement of this disclosure obligation. Specifically, the MSRB notes that, although all of a municipal advisor's employees might not be a part of the team working on a particular client matter, the number of employees with legal or disciplinary events that a municipal advisor employs and the nature of any past legal or disciplinary events related to those employees could be material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel. In any event, since a municipal advisor could satisfy Proposed Rule G-42(b)(ii) and (c)(iii) by providing information specifying where the client can electronically access SEC Forms MA and MA-I, there would be little additional burden imposed on municipal advisors by leaving the scope of these requirements unchanged.

Type of Writing(s) Required to Document the Municipal Advisory Relationship

Several commenters discussed the matter of documenting the municipal advisory relationship and the type of writing that should be required to evidence the municipal advisory relationship between the municipal advisor and its client.

FLA DBF, correctly recognizing that the Revised Draft Rule's reference to a "writing" does not require a written contract, suggested that the proposed rule change should be amended to require municipal advisors to enter into written contracts with their municipal entity clients regarding their municipal advisory relationships. In contrast, GFOA, while also correctly recognizing that the Revised Draft Rule does not require a written contract, supported the absence of a contract requirement. GFOA noted that although entering into a bilateral contract is a GFOA best practice, "there may not always be a need for a specific contract." GFOA agrees with the MSRB that the municipal advisory relationship should be stated in writing as it would allow the issuer to clearly delineate the scope of work it intends its municipal advisor to provide.

A number of other commenters, including ABA, BDA, ICI, Lewis Young, MSA, NAIPFA and SIFMA, however, construed section (c) of the proposed rule as requiring a written contract, leading them to raise various concerns about the proposed rule applying to existing contracts that might need to be revised. As a result, these commenters suggested the inclusion of various kinds of transitional rule provisions to address these issues. ABA and Lewis Young, for example, requested a transitional provision to permit advisors to honor their existing agreements with their clients until they expire. ICI recommended that the MSRB clarify that, if approved, Proposed Rule G-42 would only apply prospectively. SIFMA requested that the MSRB limit or eliminate the need for municipal advisors to re-document their municipal advisory relationships and apply the disclosure requirements of the proposed rule only to future agreements. MSA requested guidance on whether the obligations of section (c) of Proposed Rule G-42 could be satisfied by a contract (such as a Master Services or Professional Services Agreement) between the municipal advisor and its client.

The documentation requirement of section (c) of Proposed Rule G-42, as with the Revised Draft Rule, would not require the creation of new contractual relationships or the modification of existing contracts or agreements between municipal advisors and their clients. The purpose of the requirement is to help ensure that certain terms of each municipal advisory relationship would be reduced to writing and delivered to the municipal advisor's municipal entity or obligated person client. So long as the content of the documentation adheres to the requirements of the proposed rule (including the standards of conduct in section (a)), municipal advisors and their clients have some latitude in deciding the exact form the documentation and writing might take. If municipal advisors have already delivered documentation meeting some or all of the requirements of proposed section (c), then municipal advisors would be able to rely on such documents to satisfy some or all of their obligations under section (c). While certainly permitted, the proposed rule would not require municipal advisors to enter into written contracts with their municipal entity or obligated person clients and municipal advisors could satisfy the requirements of provision (c) by providing separate or supplemental documents to any preexisting contract, agreement or writing previously provided that might be in place between the municipal advisor and its client. The relevant part of proposed section (c) has been further revised to delete the phrase "enter into" (which could have connoted the formation of a contract) and reads as follows: "A municipal advisor must evidence each of its municipal advisory relationships by a writing or writings created and delivered to the municipal entity or obligated person client prior to, upon or promptly after the establishment of the municipal advisory relationship." The MSRB believes that requiring the documentation to take the form of a bilateral contract would be unnecessary and could lead to some of the burdensome consequences identified by commenters. The amendments to the Revised Draft Rule should clarify that municipal advisors would not be required to alter or re-execute any existing contract and that, in the future, the documentation and disclosure requirements could be satisfied in writings that are either included in a contract or separate and independent of any contract entered into between the municipal advisor and its municipal entity or obligated person client.

In response to the First Request for Comment, BDA and GKB stated that they generally supported the documentation and disclosure requirements of section (c) of the Initial Draft Rule but believed, with respect to municipal financial products, that a "written agreement" (as they believed was required by section (c)) should only be required when municipal advisory activities are engaged in for compensation. Based on their comments, it appears that BDA and GKB understood section (c) to implicitly require the municipal advisor and its client to evidence their municipal advisory relationship with a bilateral contract. NAIPFA, in its response to the Initial Draft Rule, asked the related question: "Does this mean that the writing must be a two party agreement?" NAIPFA also suggested that the MSRB amend section (c) to allow municipal advisors to satisfy the requirements of the section through an engagement letter. As previously stated, section (c) would not require, or preclude the use of a bilateral contract or engagement letter to evidence the municipal advisory relationship. So long as the content adheres to the requirements of Proposed Rule G-42 (including the standards of conduct of section (a)), municipal advisors and their clients would have some latitude in deciding the exact form the documentation and writings might take.

NAIPFA expressed concerns regarding the amount of information that would be required to be included in the documentation required by section (c), stating that municipal advisors would be put at a "significant competitive disadvantage to their [underwriting] counterparts . . . [because] underwriters are not mandated to include any particular contract-related terms within their engagement letter, such as clauses relating to the termination of the relationship or their obligations relating to certain aspects of the transaction . . . ." The MSRB does not believe the proposed documentation requirement would result in the competitive disadvantages described by NAIPFA. First, underwriters are required to make similar disclosures to issuers of municipal securities under MSRB's fair dealing rule, Rule G-17, which includes certain disclosures regarding the underwriter's compensation. Second, to the extent any of the requirements of section (c) are included in a written agreement, contract, engagement letter or similar document already in possession of the client, such information would not need to be included in a separate writing delivered to the municipal advisor's client. Instead, municipal advisors would be able to supplement existing writings to comply with section (c). Finally, because a municipal advisor generally would be prohibited from acting as an underwriter for a transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice, the MSRB believes it would be unlikely that a municipal advisor would be in direct competition with an underwriter as suggested by NAIPFA.

In response to the Initial Draft Rule, ICI suggested that section (c) be revised to specify that only material changes to the information provided in the documentation required by section (c) would trigger the updating requirement. The MSRB did not intend by section (c) to require the supplementation of immaterial information and section (c) of the proposed rule has been revised to provide this clarification.

Triggering the Documentation Required by Section (c)

Under the Initial Draft Rule, a municipal advisor would have been required to evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship. In response to the First Request for Comment, Northland commented that section (c) of the Initial Draft Rule should require that the documentation be in place prior to engaging in municipal advisory activities rather than being permitted to be created and provided subsequently (i.e., after the establishment of a municipal advisory relationship (as defined by the Initial Draft Rule)). Northland opined that its approach would align the proposed rule change with analogous requirements and principles of the SEC Final Rule. Northland also argued that earlier documentation of the municipal advisory relationship is warranted for the same reasons it believes justify the proposed rule change's requirement to disclose conflicts of interest upon or prior to engaging in municipal advisory activities. The MSRB has considered when municipal advisors should be required to document their relationship with their clients and determined that documentation should only be required after both parties have agreed that the municipal advisor would engage in municipal advisory activities for or on behalf of the client. It is understood by the MSRB that a

municipal advisor could engage in municipal advisory activities while seeking an engagement to perform municipal advisory activities but then might ultimately not be engaged by the client. Also, in some instances, a municipal advisor could be called upon to engage in municipal advisory activities on behalf of its client on short notice for a time-sensitive matter. In such scenarios, the MSRB does not believe it would be appropriate, or necessary, to require documentation of the municipal advisory relationship because, as with the first case, there is a reasonable possibility that no municipal advisory relationship would materialize and, with regard to the second, the MSRB does not want to inhibit a municipal advisor from performing its municipal advisory activities for municipal entities and obligated persons when time is short and documenting the municipal advisory relationship might not be feasible. The MSRB believes that, when balanced against the potential benefits of requiring earlier documentation of the municipal advisory relationship, the timely disclosure of material conflicts of interest (in accordance with section (b) of Proposed Rule G-42) will sufficiently mitigate the potential consequences identified by Northland and will serve as sufficient protection to a municipal advisor's client to make an informed decision about whether to accept the advice provided by the municipal advisor until such time that documentation containing the information required by section (c) can be created and delivered.

On a separate but related matter, Northland stated that the use of the term "municipal advisory relationship" would likely lead to confusion between how Northland believes the term is used by municipal advisors and other industry participants and how the term had been defined for purposes of the Initial Draft Rule. Northland believed that it would be difficult for municipal advisors to parse apart and document "municipal advisory relationships" when some of those relationships are "historical and ongoing" and are rarely thought of as separate relationships. The MSRB believes that the definition provided in Proposed Rule G-42(f)(vi) would provide sufficient guidance to municipal advisors in this regard. That provision would state that a municipal advisory relationship is deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person and ends on, the earlier of, the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship, or the date on which the municipal advisor withdraws from the municipal advisory relationship.

In response to the Second Request for Comment, Piper Jaffray, while generally supportive of the documentation requirement of section (c) of the Revised Draft Rule, expressed concern that it could require premature documentation of a municipal advisory relationship. Specifically, Piper Jaffray stated that section (c) could require documentation when the municipal advisor has not been selected by its client to be its municipal advisor and, instead, is, in fact, engaging in municipal advisory activities as a means to obtain the engagement with the client to perform municipal advisory activities. Section (c) of the Revised Draft Rule, however, explicitly stated that the documentation requirement would only be triggered "prior to, upon or promptly after the establishment of the municipal advisory relationship" (emphasis added). As defined in subsection (f)(vi), a municipal advisory relationship would only be deemed to exist when the

"municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person." Thus, Proposed Rule G-42 would not necessarily require the provision of relationship documentation during an early stage of municipal advisory activities when the municipal advisor is still pursuing an engagement to perform municipal advisory activities.

Other Comments Regarding the Documentation Requirement

Consolidation. In response to the Revised Draft Rule, Piper Jaffray suggested that the disclosure and documentation requirements of sections (b) and (c) could be more clearly established if the sections were merged. In particular, Piper Jaffray found it confusing that a municipal advisor providing "advice," but that has not yet been engaged by an issuer, must provide disclosures related to its compensation under paragraph (b)(i)(F). Piper Jaffray then posed the question: "[I]s the intention of the [MSRB] to assure that municipal advisors must provide conflicts disclosure when providing information that would constitute 'advice' prior to [being] engaged[?]" Piper Jaffray suggested that the intention and purpose of the proposed rule change could be better served if the required disclosures and documentation of the municipal advisory relationship were provided when the advisor is selected by the issuer to provide it with advice.

The MSRB has considered Piper Jaffray's recommendation to merge sections (b) and (c) and modify the timing of the disclosure requirement, but believes such amendments would conflict with the intention of having municipal advisors disclose conflicts of interest upon or prior to engaging in municipal advisory activities for the client. Combining the paragraphs could cause municipal advisors to delay making the proposed rule's required disclosures until the municipal advisory relationship has been reduced to writing, which could be a significant amount of time after the client has received, and potentially acted on, advice from the municipal advisor. For these reasons, the suggested changes are not included in Proposed Rule G-42.

Indirect Compensation and Treatment of Incidental Informal Advice. Regarding the documentation of the municipal advisory relationship, SIFMA requested that Proposed Rule G-42 include a definition of "indirect compensation" as it is used in subsection (c)(i). On a related topic, SIFMA requested that the MSRB "clarify that informal advice that is incidental to providing brokerage/securities [services] would not, alone, trigger a written documentation requirement under [section (c) of the Revised Draft Rule] . . . ."

The MSRB believes that additional clarification within the proposed rule change is not necessary because the phrase "indirect compensation" is widely used and understood in the municipal advisory and securities industry and is well established in securities statutes and jurisprudence. Providing a definition of "indirect compensation" within Proposed Rule G-42 might reduce clarity regarding the general understanding of the phrase and lead to unnecessary confusion in an instance where sufficient guidance is already available.

Regarding SIFMA's request pertaining to advice that is incidental to providing brokerage/securities services, the MSRB notes that the proposed rule change would apply to a scope of municipal advisory activities as defined in the SEC Final Rule. Whether certain activities constitute "advice" under the SEC Final Rule is a legal interpretation within the authority of the SEC, and not the MSRB, to make.

Recommendations and Review of Recommendations of Other Parties

Section (d) of Proposed Rule G-42 would provide that if a municipal advisor makes a recommendation of a municipal securities transaction or municipal financial product to its client, the municipal advisor must determine, based on the information obtained through reasonable diligence, whether the transaction or product is suitable for the client. Section (d) also would contemplate that a municipal advisor could be asked to evaluate a recommendation made to its client by another party, such as a recommendation by an underwriter of a new financing structure or a new financial product. Section (d) would require municipal advisors to conduct a suitability analysis – when requested by the client and within the scope of the engagement – of the recommendations of these third parties, guided by the requirements and principles contained in relevant portions of the supplementary material (such as paragraphs .01, .08 and .09).

Commenters raised a number of issues with section (d) of Proposed Rule G-42 (sections (d) and (e) of the Initial Draft Rule) and the related paragraphs .01 (Duty of Care), .08 (Suitability) and .09 (Know Your Client) of the Supplementary Material to Proposed Rule G-42. Below is a summary of, and response to, these comments.

General Comments Regarding Section (d)

In response to the Second Request for Comment, NAIPFA and GFOA expressed their general support for the Revised Draft Rule's suitability standard of section (d) of Proposed Rule G-42. NAIPFA believed it appropriately reflects a municipal advisor's fiduciary duties to its municipal entity clients.

Compliance and Examination. BDA, in response to the Second Request for Comment, expressed its support of the Revised Draft Rule's requirement to have municipal advisors review recommendations of other parties, but requested specific guidance on how municipal advisors would develop reasonable policies to comply with section (d). BDA also expressed concern about how FINRA examiners would test a dealer's compliance with the requirements of section (d) when serving as a municipal advisor.

The MSRB believes it has provided sufficient guidance to municipal advisors about the principles and requirements that should inform, and be incorporated in, a municipal advisor's policies and procedures by identifying the matters in the proposed rule text (such as in subsections (d)(i)-(iii) and paragraphs .01, .08 and .09 of the Supplementary Material) that a municipal advisor must, as applicable, consider when

forming its advice or recommendation. The MSRB recognizes the diversity of the population of municipal advisors and the municipal advisory activities in which they engage in and believes the primarily principles-based approach taken by the proposed rule change will accommodate that diversity. The MSRB also believes this approach will clearly establish the minimum requirements and principles, which financial regulators could then consistently apply in their examination of municipal advisors.

Updating Recommendations. In response to the Second Request for Comment, SMA requested that the MSRB clarify that the suitability of a recommendation would be determined by the facts and circumstances at the time a client enters into the municipal securities transaction and that the municipal advisor should not have continuing responsibility to update its determination.

The MSRB believes that whether advice given or recommendations made by municipal advisors would need to be updated would depend on the facts and circumstances surrounding the advice and recommendation, including, but not limited to, the scope of the services that the municipal advisor agreed to provide its client. The MSRB believes that the reasonableness of a municipal advisor's recommendation or advice would be determined by considering the information relied upon by, and available to, the municipal advisor at the time the recommendation is made or advice is given to its client. However, over the course of an ongoing municipal advisory relationship, it is possible that a municipal advisor would, as part of its duty of care, need to apprise its client of changes to the suitability of the advice or recommendation it had previously given. In such cases, a municipal advisor's responsibilities would depend upon the facts and circumstances and the parameters of its municipal advisory relationship. The MSRB believes that the proposed rule change will provide municipal advisors with the requisite guidance to comply with its requirements.

Third-Party Recommendations. Lamont and First Southwest, in response to the First Request for Comment, requested clarification regarding whether a municipal advisor must review any third-party recommendation related to the advice that the municipal advisor has agreed to provide.

Proposed Rule G-42 would require municipal advisors to review a third-party recommendation when such a review is within the scope of the engagement between it and its client or if such a review would be part of the reasonable diligence required to reasonably determine whether a recommendation or advice is suitable for its client. Therefore, a municipal advisor's obligation to review third-party recommendations would depend on the facts and circumstances of each particular instance. The MSRB believes that section (d) and the relevant portions of the supplementary material of the proposed rule change will provide sufficient guidance to municipal advisors presented with such scenarios.

Informing Client of Matters Related to Review of Recommendation. In response to the First Request for Comment, Northland commented that the Initial Draft Rule's requirement that municipal advisors must, under section (d), discuss matters such as the

material risks of a recommendation and the basis upon which the municipal advisor reasonably believes its recommendation is suitable for its client would encourage written documentation of such discussions and create the potential for conflict between the information provided by the municipal advisor and the actions ultimately taken by the client. It appears that Northland's concern is that a municipal advisor could be exposed to liability in an ex post review of its suitability analysis.

The MSRB received other comments related to the Initial Draft Rule's requirement that municipal advisors must discuss these matters with their clients. In response, the Revised Draft Rule included a modification that required municipal advisors to inform their clients of the matters specified in proposed section (d). The modification was made to grant some flexibility to municipal advisors in the manner in which the matters are delivered to their clients. The MSRB understands that a municipal advisor's client could elect to engage in a course of action that deviates from the municipal advisor's recommendation. For purposes of compliance with section (d), however, a client's decision to disregard its municipal advisor's recommendation would alone have no bearing on whether the municipal advisor conducted an adequate analysis of the recommendation it provided. An examination for compliance with section (d) would focus on the adequacy of the suitability analysis provided by the municipal advisor, not whether the client ultimately pursued the municipal advisor's recommendation.

Limiting Duty to Review Recommendations of Others. In response to the First and Second Request for Comment, NAIPFA stated that, when a municipal entity or obligated person has engaged an independent registered municipal advisor[65] and is also obtaining advice from a third party that is relying upon the independent registered municipal advisor exemption from the SEC registration requirement[66] to provide advice to the municipal entity or obligated person, the independent registered municipal advisor should not be permitted to limit the scope of the engagement with its client so as not to include the review of recommendations made by the third-party.

The MSRB has considered, yet disagrees with, NAIPFA's position. The MSRB believes that municipal advisor clients, with the agreement of the municipal advisor, should be able to define the scope of their municipal advisory relationships and thus determine what services the municipal advisor will provide. Furthermore, requiring municipal advisors to review all third-party recommendations could result in a costly burden to municipal entities and obligated persons that do not expect to derive sufficient value from such review. However, the MSRB acknowledges that limiting the scope of the engagement between a municipal entity or obligated person and its independent

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65 See SEC Rule 15Ba1-1(d)(3)(vi) (17 CFR 240.15Ba1-1(d)(3)(vi)). "Independent registered municipal advisor" is defined in SEC Rule 15Ba1-1(d)(3)(vi)(A) (17 CFR 240.15Ba1-1(d)(3)(vi)(A)).

66 See SEC Rule 15Ba1-1(d)(3)(iv) (17 CFR 240.15Ba1-1(d)(3)(iv)).

registered municipal advisor could affect a third party's ability to qualify and make use of exemptions discussed in the SEC Final Rule, including the exemption mentioned by NAIPFA.[67]

Request for Definition of "Independent" as Used in Paragraph .03 of the Supplementary Material

BDA, in response to the First Request for Comment, requested that the MSRB define the term "independent" for purposes of paragraph .03 of the Supplementary Material, action independent of or contrary to advice, to the Initial Draft Rule. Proposed paragraph .03 states that a municipal advisor would not be required to disengage from a municipal advisory relationship if its client were to elect a course of action that is "independent or contrary" to the advice provided by the municipal advisor. BDA asked if "independent" would mean that the municipal advisor's client is not relying on or considering the advice of the municipal advisor; that the client is not seeking advice from the municipal advisor; or, that the client is acting contrary to advice given by the municipal advisor.

Proposed paragraph .03 of the Supplementary Material was designed to address instances when a municipal advisor's client has decided either not to accept, rely on or consider the municipal advisor's advice or to take an approach or position that varies (completely or partially) from advice provided by the municipal advisor. In the event of such occurrences, paragraph .03 would allow a municipal advisor to continue in its advising capacity so long as doing so would not otherwise be precluded by MSRB rules or federal, state or other laws, as applicable.

Scope of the Recommendations Analysis. Proposed section (d) and paragraph .08 of the Supplementary Material address municipal advisors' recommendations of municipal securities transactions or municipal financial products. However, as part of the duty of care articulated under proposed paragraph .01 of the Supplementary Material, a municipal advisor would be required to have a reasonable basis for any advice provided to its client.

Northland requested clarification regarding whether section (d) of the Initial Draft Rule would be applicable to all recommendations provided by the municipal advisor or only when a recommendation is related to entering into a municipal securities transaction or municipal financial product. NABL stated, in response to the First Request for Comment, that "suitability," as a general matter, is a regulatory concept that could not be appropriately applied to municipal advisors in all instances. NABL suggested that a municipal advisor should be permitted to make a recommendation as to a limited aspect of the transaction, even if the municipal advisor does not agree that the transaction is suitable.

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67 17 CFR 240.15Ba1-1.

Section (d) of Proposed Rule G-42 would provide that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product unless the municipal advisor has determined, based on the information obtained through the reasonable diligence of the municipal advisor, whether the transaction or product is suitable for the client. A municipal advisor could provide advice regarding an aspect of a municipal securities transaction or municipal financial product that the municipal advisor believes to be unsuitable for its client so long as the municipal advisor adhered to the duty of care, duty of loyalty, and all other laws, as applicable, and either did not recommend the unsuitable transaction or product or informed the client of the basis on which the municipal advisor reasonably believed the transaction or product to be unsuitable.

Documenting Recommendations. Lewis Young expressed concern that section (d) of the Initial Draft Rule would require excessive and "defensive" recordkeeping and documentation in order to evidence compliance with the section's requirement that municipal advisors inform their clients of certain matters pertaining to their recommendations. Lewis Young argued that such documentation would be a "waste of time and resources" because the client has already determined to pursue a particular municipal securities transaction or municipal financial product. Accordingly, Lewis Young believed documenting such discussions "so as to have a 'good answer' for the next regulatory audit" would be overly and unnecessarily burdensome.

The MSRB believes that the proposed rule change sufficiently articulates that municipal advisors and their clients would have the discretion to define the parameters of their municipal advisory relationship and, thus, decide between them what municipal advisory activities would be performed by the municipal advisor for its client, including what matters for which a municipal advisor would be providing advice. As such, regarding the scenario proffered by Lewis Young, a municipal advisor that has not been engaged to provide advice about a municipal securities transaction or municipal financial product that was previously selected by its client would not be under an implicit obligation to provide the client with the suitability analysis described in proposed section (d) and the supplementary material. The municipal advisor would remain subject to (among other provisions of the proposed rule change) a duty of care, duty of loyalty (as applicable) and relevant supplementary material such as paragraphs .04 (Limitations on the Scope of the Engagement) and .09 (Know Your Client). Further, the MSRB believes that the documentation required by proposed Rule G-8(h)(iv) is an appropriately tailored recordkeeping requirement that will assist regulatory examiners in assessing the compliance of municipal advisors with the proposed rule change. Also, the MSRB believes the recordkeeping requirements will not be overly burdensome because municipal advisors would only be required to maintain documents created by the municipal advisor that were material to its review of a recommendation by another party or that memorializes the basis for any conclusions as to suitability.

Recommendations of Investment Funds. NY State Bar requested the MSRB to clarify the obligations owed by a municipal advisor to its client when the recommendation is to invest in an investment fund that is managed by a third-party

advisor. NY State Bar's concern was that, under the Initial Draft Rule, a municipal advisor would be obligated to provide a recommendation, and therefore a suitability analysis, of the investment choices made by the manager of the investment fund.

Depending on the facts and circumstance of a particular scenario, such as described by NY State Bar, a municipal advisor could have a multitude of different obligations regarding its recommendation of an investment fund to a client. While the proposed rule change would allow municipal advisors and their clients to negotiate the municipal advisory activities to be performed, the standards of conduct articulated in section (a) and the relevant paragraphs of the supplementary material would not be subject to alteration. Therefore, a municipal advisor that has agreed to provide a recommendation regarding the investment in an investment fund would be required to exercise a duty of care that could, in turn, require the municipal advisor to conduct a suitability analysis that might, depending on the relevant facts and circumstance of a particular instance, require the municipal advisor to conduct a suitability analysis of the investment choices made by the manager of the investment funds. By establishing the applicable standards of conduct for municipal advisors, and providing additional guidance regarding those standards in the supplementary material to Proposed Rule G-42, the MSRB believes that municipal advisors will be able to make a determination regarding what actions they must undertake when making recommendations to clients.

Prescriptive Metrics for Suitability Analysis. In response to the First Request for Comment, MSA asked whether the MSRB would provide the "specific metrics (standard debt issuance options)" that should be used to determine the suitability of a recommendation. MSA also inquired into whether "there [will] be standards set for this quantitative review or will it be the responsibility of the individual [municipal advisor] to define the suitability metrics based on the unique circumstances of each client or project?"

In order to accommodate the diversity of the municipal securities and municipal advisory marketplace, the MSRB has taken a primarily principles-based approach regarding the required suitability analysis so that municipal entities and obligated persons would receive appropriately tailored and relevant advice and recommendations from their municipal advisors. For this reason, the MSRB does not intend to provide the specific metrics requested by MSA and instead will rely upon the principles and requirements provided by the proposed rule change.

Municipal Advisor Reliance on Information Provided by Client

A number of commenters voiced apprehension regarding what they believed to be the high standard set for providing recommendations to their clients or reviewing the recommendation of a third party. Specifically, commenters expressed concern with the portion of paragraph .01 (which would be applicable to recommendations contemplated under section (d)) that would require a municipal advisor to "undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information." Most commenters stated that a municipal advisor

should be able to rely on the accuracy and veracity of the information provided by a client and not be required to validate such information.

Sutherland asked, in response to the First Request for Comment, in the context of 529 plans, what the Initial Draft Rule would require a municipal advisor to do in order to satisfy the proposed obligation to undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. Sutherland also asked whether a municipal advisor must obtain a representation from the issuer that the information it provides does not contain any material misstatements or omissions.

In response to the Second Request for Comment, ICI stated that municipal advisors to 529 plans should not be required to verify the veracity or completeness of the information provided to them by persons who are authorized by the municipal entity client to act on behalf of a state's 529 plan.

NABL commented that a municipal advisor should be free to recommend a transaction based on facts given to it by its client, without exercising any diligence to check the facts, if consistent with the scope of the engagement with its client. Regarding the review of recommendations of others, MSA asked whether it would be necessary to obtain documentation or information used by a third-party to make a recommendation that the municipal advisor has been engaged to review. MSA believed that the Initial Draft Rule should require the third party, who provided the recommendation and that the municipal advisor has been engaged to review, to disclose any documentation relied upon for that recommendation.

The duty of care is a core principle underlying many of the obligations of the proposed rule and is included, among other reasons, to ensure municipal entities and obligated persons are shielded from the potential negative consequences that could result from not receiving well-informed advice and expertly-executed services from their municipal advisors. The MSRB believes that requiring municipal advisors to conduct a reasonable investigation about the accuracy and completeness of the information, including information pertaining to a 529 plan, on which they will be basing their advice is necessary to ensure that clients will be able to make an informed decision based on facts and choose a prudent course of action. As stated in section (d), the municipal advisor would only need to exercise reasonable diligence, thus obviating the need for a municipal advisor to go to impractical lengths to determine the accuracy and completeness of the information on which it will be basing its advice and/or recommendation. The MSRB believes that obtaining a representation from the municipal advisor's client that the information it has provided, with no or insufficient diligence conducted by the municipal advisor, would not satisfy either section (d) or paragraph .01 of the Supplementary Material of Proposed Rule G-42 because such a representation would not sufficiently preclude the potential for the risks associated with providing advice or recommendations without a reasonable inquiry into the accuracy and completeness of the information upon which such advice or recommendations are based. While alone, such a representation would not satisfy the requirements of the proposed

rule change, a municipal advisor would be free to seek and obtain such a representation as a prudent part of its process for conducting a reasonable investigation of the veracity and completeness of the information on which it is basing its recommendation.

Applicability of Suitability Analysis to 529 Plans

Several commenters raised concerns about how section (d) and the related supplementary material that address suitability analysis would generally apply to municipal advisors advising 529 plans.

ICI stated, in response to the Second Request for Comment, that the suitability standard set forth in paragraph .08 of the Supplementary Material should recognize what ICI believes to be differences between advice rendered in connection with municipal securities, generally, and that rendered in connection with 529 plans. Sutherland voiced concerns in its response to the First Request for Comment and stated that the suitability factors listed in paragraph .08 and section (d) are not workable with regard to 529 plans. ICI believed that some of the factors for determining suitability included in paragraph .08 would be "largely irrelevant in the context of rendering advice to a 529 plan" and the MSRB should modify the Revised Draft Rule to explicitly state that such factors would not apply to advice relating to 529 plans. In the absence of exempting 529 plans from needing to consider such factors, ICI asked the MSRB to clarify how it intends the listed factors to apply to 529 plans.

In consideration of these comments, the MSRB has modified proposed paragraph .08 (formerly paragraph .09) of the Supplementary Material to allow municipal advisors to base a suitability determination only on the listed factors that are applicable to the particular type of client being advised. The MSRB, accordingly, has inserted the phrase "as applicable to the particular type of client" as a qualifier to the list of factors in paragraph .08 that must be considered in a suitability analysis. The modifications proposed should address the commenters' concerns such as how factors such as "financial capacity to withstand changes in market conditions" would apply given that 529 plans are not dependent on external sources of revenue or funding to satisfy claims of investors. However, the listed factors in paragraph .08, consistent with the regulation of recommendations in other securities law contexts, are focused on the client and not the product involved.

Request for Clarification of Documentation and Procedural Requirements

In response to the Second Request for Comment, Piper Jaffray requested additional clarification on what a municipal advisor would need to do, and what documents would need to be created, to comply with the Revised Draft Rule's suitability requirements. Specifically, Piper Jaffray asked what the proposed rule change would require with regards to decisions that Piper Jaffray refers to as "smaller decisions" (e.g., call features and whether to utilize a premium bond structure that has a lower yield to call).

The proposed rule change would require, pursuant to the duty of care, a municipal advisor to have a reasonable basis for any advice it provides to or on behalf of its client. Also, municipal advisors would be required to conduct a suitability analysis of recommendations of municipal securities transactions and municipal financial products that would comport with the requirements of proposed paragraph .08 of the Supplementary Material. Whether or not a suitability analysis would be required would depend, as previously discussed in Item 3, on the facts and circumstances surrounding the communication made by the municipal advisor and whether the communication was a recommendation of a municipal securities transaction or municipal financial product. Advice as to the "smaller decisions" asked about by Piper Jaffray might, or might not, depending on the facts and circumstances of a particular instance, rise to the level of being a recommendation that would require a suitability analysis under the proposed rule change, even though such advice may relate to a municipal securities transaction or municipal financial product and therefore trigger other provisions of the proposed rule, because the advice might not reasonably be viewed as a "call to action" that would constitute a recommendation of a municipal securities transaction or municipal financial product. Note that even in the case of advice short of a recommendation, a subsequent communication that does constitute a recommendation requiring a suitability analysis might, depending on the particular facts and circumstances, require analysis at that time of a subject that was addressed in previous advice.

With regard to the recordkeeping requirements that would be required when providing a recommendation of a municipal securities transaction or municipal financial product, proposed MSRB Rule G-8(h)(iv) would require specifically that municipal advisors keep a copy of any document created by a municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any determination as to suitability for a period of not less than five years. The MSRB believes that the proposed recordkeeping requirements will allow regulatory examiners to efficiently assess a municipal advisor's compliance with the suitability obligations of Proposed Rule G-42. The MSRB also believes that the proposed recordkeeping requirements will not overly burden municipal advisors because the MSRB understands that these documents are routinely made and retained by municipal advisors as a part of their normal business operations.

Suitability and Policy Related Considerations

In response to the First Request for Comment, BDA and Piper Jaffray stated that the factors to be considered by municipal advisors when determining whether a municipal securities transaction or municipal financial product is suitable for its municipal entity or obligated person client discussed in paragraph .08 (Suitability) of the Supplementary Material overlooks the effect that "policy and political considerations" could have on a suitability determination. Piper Jaffray requested that the MSRB clarify whether the determination of suitability should "incorporate the policy directives and decisions of the issuer at the time the issue is undertaken." BDA requested that the MSRB clarify that, if a municipal advisor's client states its objective, the municipal advisor, in making its

recommendation, does not need to assess the appropriateness of the client's stated objective but could "generally accept the [objective]."

Section (a) and paragraph .01 of the Supplementary Material to Proposed Rule G-42 would require that municipal advisors exercise due care in performing their municipal advisory activities with respect to all of their clients. This duty would require, among other things, municipal advisors to provide their clients with informed advice. The MSRB believes that informed advice regarding the suitability of a municipal securities transaction or municipal financial product is the result of a municipal advisor making a reasonable inquiry into certain relevant information about the municipal advisor's client. For this reason, the MSRB has included in proposed paragraph .08 the requirement that a municipal advisor base its determination of suitability on any material information known by the municipal advisor after reasonable inquiry. Furthermore, proposed paragraph .09 of the Supplementary Material would obligate a municipal advisor to know and retain the essential facts concerning its client to allow the municipal advisor to effectively service the client. The MSRB believes that policy considerations could be materially relevant information under all of the particular facts and circumstances that municipal advisors may consider when determining the suitability of a municipal securities transaction or municipal financial product. A stated objective of the client as BDA posits could be made most clear by reducing it to writing and including it in the relationship documentation on the scope of the engagement.

Evidencing Evaluations and Delivery of Required Information Regarding Recommendations

Several commenters, including BDA, MSA, Northland and Lewis Young, commented on records and documentation requirements of the proposed rule change that would be applicable to municipal advisors.

In response to the First Request for Comment, BDA requested clarification regarding what books and records a municipal advisor would need to maintain to evidence evaluations or recommendations made by the municipal advisor. BDA commented that some evaluations or recommendations could be delivered orally to a client and that requiring a municipal advisor to memorialize each recommendation or evaluation in writing could prove impractical and/or costly. MSA asked, in response to the First Request for Comment, whether the information regarding recommendations and evaluations of which a municipal advisor is required to "inform" its client could be "transmitted to the client orally or will each alternative require empirical evidence demonstrating the material risks, potential benefits, structure and characteristics?" If oral transmission is acceptable, MSA then asked whether it would need to be documented by both parties. Also in response to the First Request for Comment, Northland expressed concerns regarding the Initial Draft Rule's requirement to discuss matters with the client, because it believed there is an implicit need to document these discussions therefore necessitating the use of written communications. However, Northland argued that written communications could result in a conflicting record that shows what the municipal advisor recommended as possibly in opposition to the course of action ultimately taken

by its client. Northland was concerned that these potential conflicts could result in some exposure to liability in the event the justification of the decided upon course of action is challenged. Lewis Young contended that requiring municipal advisors, in section (d) of the Initial Draft Rule, to inform their clients of the risks and benefits of a particular structure or product when the client has already decided on a course of action (prior to engaging or seeking the advice of the municipal advisor) would yield little, if any, benefit. Lewis Young suggested only requiring the municipal advisor to inform its client of the matters discussed in section (d) when the client is considering, or presented with a recommendation of, a financial product, transaction or mechanism that is "novel to the client."

Proposed Rule G-8(h)(iv) would require a municipal advisor to maintain a copy of any document it created that was material to its review of a recommendation by another party or that memorializes the basis for any determination as to suitability. Section (d) of Proposed Rule G-42 would require a municipal advisor to inform its clients of the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is, or is not, suitable for the client; and whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives. The MSRB notes that municipal advisors, under Proposed Rule G-42, would be required to "inform" their clients of such matters, rather than "discuss," as previously required under the Initial Draft Rule. Under Proposed Rule G-42, a municipal advisor would be allowed to choose the appropriate method in which to communicate its evaluation of the material risks and benefits attendant to the recommendation. The method selected and used by the municipal advisor must, however, comport with the duty of care and duty of loyalty (as applicable) that is owed to its client and should, therefore, result in the municipal advisor's client receiving timely, full and fair notification of the matters provided for in proposed subsections (d)(i)-(iii) and that adhere to the guidance provided in proposed paragraph .08 of the Supplementary Material.

Exemption from Suitability Standard, "Sophisticated" Issuers

In response to the First Request for Comment, First Southwest expressed general support for a suitability standard for recommendations by municipal advisors but stated that certain clients of municipal advisors are capable of independently evaluating recommendations of municipal advisors and these clients should be exempt from the suitability standard in a manner similar to the "sophisticated municipal market professional" under MSRB Rule G-48. Lamont voiced a similar concern stating that many of its "large sophisticated" issuer clients do not want, or need, a review of the transaction they have already decided to undertake. Lamont commented that these types of clients are "sufficiently capable of weighing the risks in a transaction and making their own decision about whether to proceed."

In response to the Second Request for Comment, SMA stated that when a municipal securities transaction or municipal financial product has been decided upon by a municipal advisor's client and: (a) is related to a project or event determined by the governing body of the municipal entity or its citizens to be in its interest and consistent with its goals; (b) is permitted by state statute as determined by municipal or bond counsel; and (c) involves a transaction or product which the municipality has employed in the past, then it seems suitability has been determined and the advisor ought to be able to rely on these facts and the closing documents as establishing a reasonable basis for suitability. Southern MA suggested that a municipal advisor should not be put in the position of substituting its judgment as to the suitability of a municipal securities transaction or municipal financial product for that of the municipal policy makers, citizens or state lawmakers.

The MSRB has determined that the requirements of section (d), and the related paragraphs of the supplementary material, should be applicable regardless of the municipal advisor's perception of the sophistication of its client or the client's perception of its own degree of sophistication. The proposed rule change is aimed at protecting municipal entities, obligated persons and the public interest and, as a result, the MSRB believes that exemptions such as those described by these commenters would frustrate that objective. However, in designing Proposed Rule G-42, the MSRB did incorporate many of the concepts that commenters believed were indicia of the sophistication of an issuer into the factors to be considered when determining the suitability of a recommendation. Under those factors, the considerations proffered by SMA could be relevant to, and therefore be part of, a municipal advisor's suitability analysis depending on all of the particular circumstances, though they might not alone be sufficient to support a suitability determination under the proposed rule change.

Specified Prohibitions

Several commenters provided input on Proposed Rule G-42(e)(i), which sets forth certain activities in which municipal advisors would be prohibited from engaging.

General Comments

In response to the First Request for Comment, NAIPFA and GFOA expressed general support for the specified prohibitions, NAIPFA stated that the section includes prohibitions that are "important measures that are needed to eliminate certain practices that often carry unmanageable conflicts of interest inconsistent with Municipal Advisor fiduciary duties," and the prohibitions are appropriately tailored and would not impose undue regulatory burdens. Other commenters noted their general support for the prohibitions, but suggested some revisions or limitations, which are discussed in the section below.

Cooperman commented that the MSRB should determine, after a monitoring period since the passage of the Dodd-Frank Act, what, if any, abuses or inappropriate conduct remain that would require the regulation set forth in the proposed rule change.

Alternatively, Cooperman suggested that the MSRB consider, at least initially, "limiting the [proposed rule] to an enumeration of prohibited forms of conduct and practices" rather than imposing extensive compliance, supervision and other requirements. In response to the Second Request for Comment, Lewis Young commented that the specified prohibitions subsections (e)(i) and (ii) (on the ban of certain principal transactions) are unnecessary because the matters addressed in those sections are adequately attended to in section (a) and should be intrinsic to a reputable municipal advisor's business practices. As such, Lewis Young recommended that these prohibitions be set forth in the supplementary material in order not to detract from the focus of the proposed rule. In response to such comments, the MSRB notes that, in many respects, Proposed Rule G-42 adopts a principles-based approach, enumerating prohibited forms of conduct and practice. However, regarding certain arrangements that the MSRB has identified as particularly prone to conflict with, or risk of breach of, the fiduciary duty and duty of care, the MSRB believes that the proposed rule change appropriately incorporates more specific requirements and prohibitions.

Excessive Compensation

In response to the First Request for Comment, SIFMA, Lewis Young and MSA commented that the provision that would prohibit receiving compensation that is excessive in relation to the municipal advisory activities actually performed (now Proposed Rule G-42(e)(i)(A)), did not include a sufficiently clear standard for how excessive compensation would be determined and failed to provide adequate amount of guidance to facilitate compliance. SIFMA expressed concern that without a clear standard or more guidance, such determinations would be made in hindsight, presumably by financial regulatory examiners, and to the detriment of municipal advisors. Lewis Young called the prohibition unworkable, expressed concern that it would require advisors to document all of their work and requested that the paragraph be deleted. SIFMA and Lewis Young also commented that municipal advisor compensation is subject to market forces, and therefore its reasonableness should be determined by a negotiation between the client and the municipal advisor. PRAG stated that the proposed rule change fails to contemplate instances where transaction fees are included in a municipal advisor's compensation to compensate the municipal advisor for services that it has provided but that were unrelated to the issuance of municipal securities. SIFMA and Lewis Young asked whether the practice of including fees for services a municipal advisor provided, if not related to the issuance of municipal securities, would be permitted under the proposed rule change. Columbia Capital commented that the MSRB should strike the phrase "whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product," in paragraph .10 of the Supplementary Material of Proposed Rule G-42, and add, as an additional factor to be considered when determining whether compensation is excessive, a comparison of the municipal advisor's compensation to other professionals providing services on the transaction in question.

After carefully considering the comments submitted in response to the First Request for Comment, the MSRB incorporated guidance regarding excessive compensation in paragraph .10 of the Supplementary Material of the Revised Draft Rule

and solicited further comment. Paragraph .10 of Proposed Rule G-42 sets forth various factors that municipal advisors should consider when determining the reasonableness of their compensation. These factors include: the municipal advisor's expertise, the complexity of the municipal securities transaction or the financial product, whether the fee is contingent upon the closing of the transaction or financial product, the length of time spent on the engagement and whether the advisor is paying any other costs related to the transaction or financial product. Furthermore, Proposed Rule G-42 would prohibit receiving compensation that is excessive in relation to the municipal advisory activities actually performed. Depending on the facts and circumstances of a particular municipal advisory relationship, either or both of these provisions could apply to a scenario like that posited by PRAG. The proposed rule change, however, would not prescribe the source of funds that could be used to pay the municipal advisor for its services. Finally, the phrase regarding contingent fees is not deleted from paragraph .10 of the Supplementary Material as the MSRB believes it is a relevant factor and appropriately included in a non-exhaustive list of other relevant factors.

Inaccurate Invoicing

In response to the First Request for Comment, Wulff Hansen commented that the prohibition on the delivery of inaccurate invoices (now Proposed Rule G-42(e)(i)(B)) should be modified to clarify that it would apply only to any overstatements of fees, expenses or activities, and not to any fee discounting by a municipal advisor. SIFMA commented that the prohibition should stand but should be modified to add materiality and knowledge qualifiers (i.e., a municipal advisor may not intentionally deliver a materially inaccurate invoice).

The MSRB believes that the proposed rule change clearly implies that offering a payment discount from the services actually performed is a permissible activity because a municipal advisor would be able to accurately describe such a discount on its invoice. In response to the SIFMA comment, the MSRB notes that the scope of inaccuracy targeted by the proposed provision is limited to the significant subjects of the services performed and personnel who performed those services, and the MSRB believes any inaccuracy in an invoice on those subjects should be proscribed. In addition, the MSRB believes that the addition to the proposed provision of the state-of-mind elements that SIFMA suggested would not sufficiently protect municipal entity and obligated person clients.

Prohibition on Fee-Splitting

The Initial Draft Rule included a prohibition on making or participating in any fee-splitting arrangement with underwriters, and any undisclosed fee-splitting arrangement with providers of investments or services to a municipal entity or obligated person client (now Proposed Rule G-42(e)(i)(D)). In response to the First Request for Comment, GFOA supported the fee-splitting prohibition in the Initial Draft Rule, noting that it "appears to be an inherent conflict, and should be avoided." NAIPFA supported the prohibition, but asked the MSRB to provide a definition of "fee-splitting arrangements," under which independent contractors and subcontractors would fall outside of the

prohibition. Lewis Young and Winters LLC stated that fee-splitting arrangements should be disclosed but not prohibited. SIFMA commented that fee-splitting arrangements with affiliates, if fully and fairly disclosed, should be permissible. SIFMA stated that there could be legitimate reasons for such arrangements, including fee structures requested by clients of an affiliate, and, with such disclosure, the parties should be free to engage in the fee arrangement believed to be most economical and efficient under the circumstances. NABL commented that the provision appears to apply to transactions even when the advice provided is exempted or excluded from that which would cause one to be a "municipal advisor" under the SEC Final Rule. Based on this assumption, NABL argued that the prohibition should apply only when a municipal advisor is giving "non-exempt" advice as part of the same transaction, not when it is giving advice that is exempt under the SEC Final Rule.

Several commenters provided examples of fee-splitting arrangements that they believed should not be prohibited. Cooperman stated that a municipal advisor should not be prohibited from outsourcing certain parts of its municipal advisory activities to independent contractors and subcontractors, including those that may have advisors on their staffs, when payment to those third parties is not dependent upon successful conclusion of the financing or payment to the municipal advisor of its fee. In addition, Cooperman stated the fee-splitting prohibition should not prevent two advisor firms from contracting with an issuer to perform services for a predetermined fee that is disclosed to the issuer. Lewis Young, who favored disclosure of fee-splitting in lieu of a complete prohibition, wrote that municipal advisors should be permitted to enter into a fee-splitting arrangement with a structuring agent that provides specific quantitative services on a transaction. Winters LLC asserted that a municipal entity or obligated person should be able to have its municipal advisor or other professionals (including underwriters, if after the underwriting period) receive compensation from investment providers or other service providers for providing oversight and performing other services so long as there is full and fair written disclosure of the fee-splitting or sharing arrangements. Lamont stated that allowing an investment provider to pay fees related to the solicitation of the investment by the municipal advisor, and that are within the permitted limits of the Internal Revenue Service rules, should be acceptable as long as the payments are disclosed to the issuer and each investment provider on the bid list. Wulff Hansen asked whether it would be permissible under the provision for a municipal advisor to arrange for a routine purchase of services on behalf of the advised client in a transaction with an entity in which the advisor has an interest (e.g., a purchase of services from DTCC when the advisor is also a DTCC Participant and thus a part owner of DTCC). Finally, Piper Jaffray requested that the MSRB clarify that the fee-splitting prohibition, with regards to underwriters, applies to "any issue for which it is serving as municipal advisor" because the failure to link the prohibition to the actual advisory engagement could lead to unintended and adverse consequences.

The MSRB agrees with Piper Jaffray's comment and amended the provision in the Revised Draft Rule (now Proposed Rule G-42 (e)(i)(D)) to prohibit a municipal advisor from making or participating in any fee-splitting arrangement with underwriters on any municipal securities transaction as to which it has provided or is providing advice.

The MSRB believes that the proposed rule change would help prevent violations of fiduciary duties and the duty of care by clearly identifying and prohibiting specific fee-splitting arrangements that are particularly prone to conflict with such duties. Other fee-splitting arrangements would be permitted, provided they are fully and fairly disclosed.

Payments to Obtain/Retain an Engagement to Perform Municipal Advisory Activities

In response to the First Request for Comment, NABL commented that the Initial Draft Rule G-42 should not prohibit or require the disclosure of payments made to obtain or retain municipal advisory business, if those activities are engaged in by persons exempted from registration as a municipal advisor under SEC Rule 15Ba1-1.[68] Similarly, the NY State Bar commented that the prohibition on making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities under subsection (g)(v) of the Initial Draft Rule (now proposed Rule G-42(e)(i)(E)) is unnecessarily restrictive with too narrow of an exemption. The NY State Bar stated that the provision should also permit payments to persons subject to comparable regulatory regimes (e.g., banks, trust companies, broker-dealers and investment advisors) as well as to affiliates of the municipal advisor so long as, in either case, the payments are disclosed to the client. SIFMA commented that the proposed rule should allow for reasonable fees to be paid to affiliates because soliciting on behalf of affiliates does not trigger a requirement for a person to register as a municipal advisor under the SEC Final Rule. In response to the Second Request for Comment, Sanchez made a similar comment. In addition, SIFMA commented that the prohibition should not cover expenditures for normal business entertainment expenses as well as marketing and sales activities.

In light of the comments received, the MSRB modified the provision (now Proposed Rule G-42(e)(i)(E)(1)) so that it would not specifically prohibit municipal advisors from making payments to an affiliate

> for a direct or indirect communication with a municipal entity or obligated person on behalf of the municipal advisor where such communication is made for the purpose of obtaining or retaining an engagement to perform municipal advisory activities….

The modification also would align the paragraph with Section 15B(e)(9) of the Exchange Act,[69] which allows affiliates of the municipal advisor to solicit on behalf of the municipal advisor without triggering the municipal advisor registration requirement for the affiliate. The MSRB would clarify, in proposed subparagraph (e)(i)(E)(2), that a municipal advisor may pay reasonable fees to another municipal advisor registered as such with the Commission and the Board for making a similar communication on behalf

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68 17 CFR 240.15Ba1-1.

69 15 U.S.C. 78o-4(e)(9).

of the municipal advisor making such payments. The MSRB would also clarify, in proposed subparagraph (e)(i)(E)(3), that payments that would qualify as permissible normal business dealings under current MSRB Rule G-20 also would not violate the prohibition. The revisions would harmonize the proposed rule change with relevant federal securities laws and rules.

Additional Comments on Specified Prohibitions

BDA and Piper Jaffray suggested adding two prohibitions to Proposed Rule G-42. In response to the First and Second Requests for Comment, Piper Jaffray suggested adding a specified prohibition that would prohibit a municipal advisor from taking into account whether it competes with other firms when the advisor makes a recommendation to its client (e.g., a recommendation to the client regarding which broker-dealer the client should hire as underwriter). In response to the First Request for Comment, BDA and Piper Jaffray suggested a second prohibition, which would prohibit a municipal advisor that is not also registered as, or affiliated with, a dealer, from using the term "independent," if used in a manner intended to convey to potential clients that the municipal advisor is free from any potential conflicts of interest, and imply that, in contrast to advisors also registered as dealers, the municipal advisor would provide better advice. Piper Jaffray also stated that continued use of the term "independent" to connote an advisor free from conflicts should be specifically prohibited in light of the issues its continued use could create if market participants confused such advisors with a person acting as an "independent registered municipal advisor" as used in the SEC Final Rule.[70]

The MSRB has not incorporated the prohibitions suggested by BDA and Piper Jaffray. To the extent the described conduct constitutes a material misrepresentation, the MSRB believes it is already appropriately addressed by Proposed Rule G-42 and existing MSRB Rule G-17, under which municipal advisors, in the conduct of their municipal advisory activities, must not engage in any deceptive, dishonest or unfair practice with any person.

Prohibition on Principal Transactions

The MSRB received extensive comments on the proposed provision to prohibit a municipal advisor (and its affiliates) from engaging in certain principal transactions (as defined in the proposed rule) with a municipal entity client of the municipal advisor ("prohibition on principal transactions" or "ban"). Specifically, Proposed Rule G-42(e)(ii) generally would prohibit a municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing, or has provided, advice.[71] Three related

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[70] See, e.g., SEC Final Rule, 78 FR at 67471.

[71] In the Initial Draft Rule, the ban is set forth in section (f); in the Revised Draft Rule and the proposed rule change, the ban is set forth in subsection (e)(ii).

provisions of the proposed rule, subsection (f)(i) and paragraphs .07 and .11 of the Supplementary Material, would, respectively, define the phrase, "engaging in a principal transaction," clarify the relationship between the proposed ban and Rule G-23, and provide guidance regarding the term "other similar financial products" in connection with principal transactions as defined in subsection (f)(i). Comments regarding the ban and the related provisions are discussed below.

General

In response to the First Request for Comment, many commenters raised concerns regarding: (1) the application of the ban to obligated person clients of municipal advisors; (2) the scope of the ban; (3) the meaning of "principal transaction" and "principal capacity;" (4) the ban's application to transactions by affiliates of municipal advisors; (5) the absence of an exception to the ban for an advisor or its affiliate based upon full and fair disclosure and the written consent of a client; and (6) the relationship between the ban and Rule G-23. In response to the Second Request for Comment, most of the comments focused on: (1) the scope of principal transactions that would be considered "directly related" to the advised transaction and come within the ban; (2) the ban's application to transactions by affiliates of municipal advisors; and (3) the relationship between the ban and Rule G-23.

Ban Does Not Apply to Obligated Person Clients

In the Initial Draft Rule, the ban prohibited a municipal advisor and its affiliates from engaging in principal transactions with municipal entity and obligated person clients. The ban in Proposed Rule G-42(e)(ii) no longer would apply to principal transactions with obligated person clients. As a result, the comments urging that the ban not apply to obligated persons are not incorporated in this discussion, except to note that such comments were considered and the MSRB modified the proposed ban such that it would not apply to principal transactions with such persons.

Scope and "Directly Related To"

In Initial Draft Rule G-42, the prohibition on principal transactions was significantly broader than the ban as modified in the Revised Draft Rule and as further narrowed in this proposed rule change. In the Initial Draft Rule, a municipal advisor (and its affiliates) generally were prohibited from engaging in any transaction in a principal capacity to which an obligated person client or a municipal entity client of the municipal advisor would be the counterparty. In response to the First Request for Comment, many commenters[72] interpreted the proposed prohibition quite broadly and expressed concerns

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[72] Commenters that expressed such concerns include ABA, BDA, Cape Cod Savings, Coastal, Frost, GFOA, GKB, JP Morgan, Kutak, NABL, NY State Bar, Parsons, Piper Jaffray, SIFMA and Zion.

regarding the scope of the proposed prohibition on principal transactions by municipal advisors (and their affiliates) with the clients of such municipal advisors.[73] Commenters, including ABA, BDA, NABL and Piper Jaffray, interpreted the ban as covering activities and transactions that were unrelated to the municipal advisory relationship. The ABA commented that "because banks almost always provide banking products and services in a principal capacity, the prohibition would prevent commercial banks and their affiliates from providing any other banking products, such as deposit accounts, loans, or cash management services . . . despite the fact that these products and services are exempt from the municipal advisor regulatory regime." BDA, Frost, SIFMA and Zion, among others, raised similar concerns regarding the broad reach of the prohibition.

After carefully considering the comments, the prohibition on principal transactions was significantly narrowed and clarified, as set forth in Revised Draft Rule G-42(e)(ii). The MSRB limited the ban to "a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice" (emphasis added). The Revised Draft Rule would thus prohibit a municipal advisor (and its affiliates) to a municipal entity client from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice. The modification was designed to exclude many of the transactions that some commenters read as potentially covered by the Initial Draft Rule, including the taking of a cash deposit or the payment by a client solely for professional services.

In response to the Second Request for Comment, some commenters supported the changes to the proposed rule text. Several other commenters continued to raise concerns regarding what they believed to be the overly broad scope of the ban. Conversely, one commenter stated that the ban in Revised Draft Rule G-42(e)(ii) had become too narrow. GFOA approved of the modification narrowing the proposed ban to "a principal

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[73] SIFMA suggested narrowing the proposed provision to:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the advice rendered by such municipal advisor (emphasis added).

BDA suggested the following alternative:

> A municipal advisor, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction with a municipal entity client if the structure, timing or terms of such principal transaction was [sic] established on the advice of the municipal advisor in connection with a municipal advisory relationship with such municipal entity client.

transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice," and Wells Fargo noted that the modification mitigated the impact of the proposed ban. ABA also welcomed the revision, but suggested additional changes. In addition, BDA, NY State Bar, Piper Jaffray and SIFMA suggested that the ban be modified further to narrow or clarify the scope of the ban. ABA recommended that the provision require the advice provided by the municipal advisor be provided pursuant to a municipal advisory relationship; NY State Bar recommended that the prohibition not apply where the municipal advisor does not make a recommendation to the municipal advisory client to enter into a transaction with the advisor or its affiliate; and SIFMA recommended that the provision ban only those principal transactions that are directly related to the advice the municipal advisor is providing, not merely the same municipal securities transaction or municipal financial product in connection with which the advice is provided. [74] BDA and Piper Jaffray commented that the term "directly related" was unclear, and recommended alternative language. In Piper Jaffray's view, the ban should be limited to a transaction or issuance where a firm served as a municipal advisor and about which advice was rendered. Alternatively, Piper Jaffray suggested that the ban should cover transactions "directly related to the advice given rather than directly related to the transaction itself." Applying the proposed "directly related to" standard to certain hypothetically paired transactions, BDA asked whether one of each pair of such transactions would be considered directly related to the second transaction and therefore subject to the proposed prohibition, and also proposed a modification to the ban.[75] Conversely, Lewis Young

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74 In response to the Second Request for Comment, ABA recommended the provision be modified to read:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice <u>pursuant to a municipal advisory relationship</u>.

SIFMA recommended the provision be modified to read:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from knowingly engaging in a [prohibited] principal transaction.

75 In connection with interpreting the scope of the "directly related to" standard, BDA asked whether: (1) selling securities as a principal after winning a competitive bid for an open market refunding escrow on a refunding bond issue for which the firm was a municipal advisor would be a transaction "directly related to" the refunded bond issue and therefore a prohibited principal transaction; (2) acting as the underwriter on a series of variable rate bonds would be directly related to acting as the municipal advisor for a related swap, and be

argued that, with the changes set forth in the Revised Draft Rule, the scope of the prohibition on principal transactions has gone from "too broad to too narrow" because the definition of "engaging in a principal transaction" (discussed in greater detail below) does not extend fully to the variety of principal transactions in which a municipal advisor could engage, which would be in conflict with its municipal advisory role and fiduciary duty (e.g., a bank loan as a substitute for an issuance of municipal securities).

The principal transactions ban is incorporated in the proposed rule change as Proposed Rule G-42(e)(ii). The MSRB has determined not to narrow, broaden or otherwise modify the standard--"directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice"--in response to the comments received. The MSRB believes that the various alternative rule texts proposed by commenters would not be more effective or efficient means for achieving the stated objective of Proposed Rule G-42(e)(ii), which is to eliminate a category of particularly acute conflicts of interest that would arise in the fiduciary relationship between a municipal advisor and its municipal entity client. The alternatives offered by various commenters are similar in that they would seek to limit the scope of prohibited transactions to those pertaining to the advice rendered by the municipal advisor. If adopted, such a change could leave transactions that have a high risk of self-dealing insufficiently addressed. For example, a municipal advisor that provided advice to a municipal entity regarding the timing and structure of a new issuance arguably would not be prohibited from acting as principal in entering into an interest rate swap for the same issuance so long as the advisor refrained from advising on the swap. In addition, in response to the comments that the standard would continue to raise questions whether a transaction was prohibited under Proposed Rule G-42(e)(ii) and the suggestion that the MSRB further amend the provision to clarify the provision, the MSRB does not believe it would be feasible or desirable, given the principled nature of the provision, to specify in advance its application in all circumstances. As noted above, the proposed principal transactions ban is revised to clarify that the prohibition applies both to principal transactions that occur while the municipal advisor is providing advice with respect to a directly related municipal securities transaction or municipal financial product, and after the municipal advisor has provided such advice.

"Engaging in a Principal Transaction" and "Other Similar Financial Products"

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prohibited; and, (3) underwriting a refunding issue years after serving as a municipal advisor for the initial issue would be a transaction that would be considered directly related to the initial issue and prohibited.

BDA recommended the provision be modified to delete the "directly related to" standard and substitute: "if the structure, timing or terms of such principal transaction was established on the advice of the municipal advisor in connection with a municipal advisory relationship with such municipal entity client."

In response to the First Request for Comment, certain commenters, including GFOA, NAIPFA, SIFMA and Wulff Hansen, commented that the MSRB should provide additional guidance regarding the meaning of various terms (e.g., "principal capacity" and "principal transaction") for purposes of interpreting the proposed prohibition on principal transactions. Several commenters, including GFOA, Wulff Hansen and First Southwest, sought clarification regarding the types of transactions that would constitute principal transactions. For example, the GFOA requested that the MSRB provide examples of prohibited and acceptable practices; Wulff Hansen asked that the MSRB specify whether the sale of other additional municipal advisory or related services would constitute a prohibited principal transaction; and First Southwest asked whether a municipal advisor that also facilitates private placements would be engaged in a principal transaction.

In response to comments, the Revised Draft Rule G-42(f)(i) added, for purposes of the Revised Draft Rule, a defined term, "engaging in a principal transaction" to mean: "when acting as principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client."

In response to the Second Request for Comment, ABA and GFOA expressed support for the proposed defined term. Another commenter, Sanchez, asked the MSRB to include a non-exhaustive list of specific common roles (such as underwriter) in addition to the general description. NY State Bar recommended two significant changes intended to narrow the scope of the prohibition and the definition of principal transaction: (1) the "somewhat open-ended" phrase "other similar financial product" should be amended to refer exclusively to municipal financial products, as defined in the Exchange Act; and (2) the definition of "engaging in a principal transaction" should be amended to make clear that the term does not include any of the banking activities as to which a bank may provide advice without being registered as a municipal advisor pursuant to the exemption in the SEC Rule 15Ba1-1(d)(3)(iii),[76] including holding investments in a deposit or savings account, certificate of deposit or other deposit instrument issued by a bank; extensions of credit by a bank to a municipal entity or obligated person, including the issuance of a letter of credit; the making of a direct loan, or the purchase of a municipal security by the bank for its own account; holding funds in a sweep account; or investments made by a bank acting in the capacity of an indenture trustee or similar capacity.

In response to comments filed regarding the Second Request for Comment, including Lewis Young's, the proposed rule would provide additional guidance regarding the term, "other similar financial products." Proposed Supplemental Material paragraph .11 would provide that, as used in Proposed Rule G-42(f)(i), "other similar financial products," "includes a bank loan, but only if it is in an aggregate principal amount of $1,000,000 or more and it is economically equivalent to the purchase of one or more municipal securities." The MSRB notes that the term "other similar financial products" is

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[76] 17 CFR 240.15Ba1-1(d)(3)(iii).

not limited to refer exclusively to municipal financial products, as defined in the Exchange Act, in that a fiduciary's obligation to its client -- not to engage in principal transactions in which the fiduciary's financial interests and concerns conflict with those of the client -- is not so limited. For the same reason, the MSRB has determined not to limit the scope of banned transactions, which are covered based generally on conflicts principles, to the category of transactions as to which advising triggers a registration requirement as a municipal advisor.

Exceptions to Ban

In the First Request for Comment, the MSRB specifically sought comments on whether a ban on principal transactions by municipal advisors was the appropriate regulatory approach, or whether a municipal advisor should be permitted to engage in certain types of principal transactions with its client, with full and fair disclosure and written client consent, and, if so, what types of principal transactions should be allowed.

In response to the First Request for Comment, several commenters, including ABA, First Southwest, Frost, GKB, Kutak, JP Morgan, NABL and SIFMA, expressed concerns regarding what they viewed as the overly broad prohibition on principal transactions between municipal advisors and their clients. Several commenters, including the ABA, Cape Cod Savings, Frost, NABL, SIFMA and Zion, stated that the prohibition could do a disservice to municipal entities by unnecessarily and substantially restricting the choices available to municipal entities that engage their municipal advisors (or their affiliates) in other types of transactions that would be prohibited by the Initial Draft Rule. In addition, several commenters, including ABA, Kutak, NABL, Parsons, SIFMA, Sutherland and Wells Fargo, believed that a municipal advisor should be permitted to engage in certain types of principal transactions with its clients if the municipal advisor provides its client with full and fair disclosure and then receives informed consent from the client. NABL stated that the proposed ban would conflict with common law, under which an agent's fiduciary duties of loyalty and care could be waived or otherwise modified by the principal if the principal is not legally incompetent. Kutak commented that the Initial Draft Rule should not prohibit all principal transactions with municipal entities when the client is sufficiently sophisticated to adequately assess the risks of the transactions. Kutak believed transactions involving an investment in an instrument where an established market exists and a municipal entity client could readily ascertain the reasonableness and fairness of the price should be allowed under the Initial Draft Rule.

Also, multiple commenters, including ABA, Kutak, NABL and SIFMA (in response to the First Request for Comment) and FSR and Zion (in response to the Second Request for Comment), noted that under Section 206(3) of the Investment Advisers Act and other regulatory regimes, certain principal transactions are permitted based upon full and fair disclosure and client consent.[77] The commenters suggested that a similar

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[77] See 15 U.S.C. 80b-6 and the rules adopted thereunder, which prohibit an adviser, acting as a principal for its own account, from knowingly selling any security to or purchasing any security from a client for its own account, without disclosing to

mechanism should be included in the ban that would allow municipal advisors to engage in principal transactions with their municipal entity clients, subject to similar disclosure and consent requirements. NABL also commented that, if the MSRB adopted a provision that was consistent with the SEC's guidance under the Investment Advisers Act regarding an exception to a ban based on disclosure and informed consent, the MSRB should provide clear guidance to market participants to avoid confusion.

In contrast, commenters Lewis Young and NAIPFA supported the proposed ban on principal transactions and did not recommend creating exceptions or narrowing its scope. Lewis Young commented that the ban was appropriate, stating that a party cannot be both a fiduciary and a principal party in a buyer/seller relationship if the sale is an asset, financial product or something other than services that are compatible with the fiduciary role.

The MSRB carefully considered the comments received that urged the MSRB to include one or more exceptions to the prohibition on principal transactions. After considering the fiduciary duty of the municipal advisor in its relationship to a municipal entity client and the possibilities for self-dealing, the MSRB believes that the proposed prohibition on principal transactions is sufficiently targeted and should be retained. In addition, the MSRB believes that exceptions to the prohibition based on disclosure and client consent, even if limited to sophisticated municipal entities, would not sufficiently protect municipal entity clients from potential self-dealing-related abuses. The prohibition has been narrowed to ban only those transactions that (1) are "directly related" to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice and (2) are purchases or sales of a security or involve entering into a derivative, guaranteed investment contract, or other similar financial product with the municipal entity client (as discussed, supra). In the MSRB's view, the prohibition on principal transactions should not at this juncture be modified or narrowed, given the acute conflicts of interest presented and the risk of self-dealing by a regulated entity (or its affiliate).[78]

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the client in writing the capacity in which it (or an affiliate) is acting and obtaining the client's consent before the completion of the transaction.

SIFMA also referred to the regulation of swap dealers and security-based swap dealers that also serve as advisors to Special Entities (which includes municipal entities) under the CEA. See 7 U.S.C. 1 et seq. According to SIFMA, the CEA does not preclude such advisors from entering, in a principal capacity, into derivatives transactions with the Special Entities that they advise, including municipal entities, subject to the duty of the advisor to act in the best interests of the Special Entity.

78 Similar concerns regarding conflicts of interests arising when a regulated entity would provide financial advice to a municipal issuer and also serve as underwriter were raised by the MSRB and commenters in connection with SR-MSRB-2011-03, a proposed rule change to amend MSRB Rule G-23 relating to the activities of

Affiliates

In response to the First Request for Comment, a number of commenters commented on the ban's coverage of principal transactions by affiliates of a municipal advisor, including ABA, Frost, JP Morgan, Parsons, Piper Jaffray, SIFMA, Wells Fargo and Zion.

The ABA, SIFMA and other commenters commented generally that other fiduciary regimes do not prohibit all affiliates of a fiduciary from engaging in principal transactions with the party owed the fiduciary duty. Wells Fargo also sought to limit the coverage of the ban, commenting that the ban should not apply to certain affiliates. In Wells Fargo's view, affiliates of large financial institutions often offer substantially different services, operate with distinct governance structures and employ information barriers, and, in such instances, if a non-municipal advisor affiliate is not connected to the municipal advisor relationship, the risk of a conflict of interest in a principal transaction between a municipal advisor client and the non-municipal advisor affiliate is significantly diminished. Wells Fargo suggested that the MSRB not apply the ban to affiliates or, at a minimum, limit the ban to principal transactions of affiliates that are directly related to the municipal advisory relationship that the municipal advisor affiliate has with the client. ABA, NABL, SIFMA, Wells Fargo, Zion and other commenters generally expressed concerns related to regulating conduct of affiliates of municipal advisors, specifically the imposition of compliance burdens on the affiliates and possible unintended consequences to clients if certain products and services offered by affiliates of the municipal advisor were no longer available to clients. ABA and NABL commented that the MSRB does not have apparent authority to regulate the conduct of affiliates of municipal advisors that are not brokers, dealers or municipal securities dealers, and thus, any ban should be narrowly-tailored and addressed to the municipal advisor's right to advise, rather than its affiliates' rights to engage in unrelated transactions.

In response to the Second Request for Comment, ABA, FSR, SIFMA and Wells Fargo included significant comments that focused on the ban's application to transactions by affiliates. With respect to affiliates, among the concerns raised was the difficulty that municipal advisors and their affiliates might have in identifying transactions that are related to an advised transaction, particularly within large organizations, and the likely

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financial advisors, which was approved by the Commission. See Exchange Act Release No. 64564 (May 27, 2011), 76 FR 32248, 32249 (June 3, 2011) (order approving File No. SR-MSRB-2011-03) ("[T]he proposed rule change resulted from a concern that a dealer financial advisor's ability to underwrite the same issue of municipal securities, on which it acted as financial advisor, presented a conflict that is too significant for the existing disclosure and consent provisions of Rule G-23 to cure. Even in the case of a competitive underwriting, the perception on the part of issuers and investors that such a conflict might exist was sufficient to cause concern that permitting such role switching was not consistent with 'a free and open market in municipal securities'" (emphasis added)).

significant cost of compliance. Commenters, such as SIFMA and Wells Fargo, also questioned the value of extending the prohibition to affiliates of a municipal advisor, stating that, in scenarios where the affiliate has no knowledge of the municipal advisory relationship, or where the municipal advisor has no knowledge of an affiliate's contemplated principal transaction, the parties would not be likely to engage in self–dealing or profit from the affiliation.

SIFMA suggested that the MSRB include the emphasized modifier in subsection (e)(ii) as follows: "A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from knowingly engaging in a principal transaction . . . ." (emphasis added), which is the same modifier contained in the provision on principal transactions in the Investment Advisers Act.[79] Wells Fargo suggested a modification to exempt municipal advisor affiliates operating with information barriers, stating that such entities are unlikely to engage in the self-dealing that the rule is aimed at preventing.

After considering the fiduciary duty of the municipal advisor in its relationship to a municipal entity client and the risk of self-dealing, the MSRB believes that the proposed prohibition on principal transactions, including its application to affiliates, is sufficiently targeted. In the MSRB's view, the proposed prohibition should be retained without exceptions, including one based on disclosure and consent, for the reasons set forth above, given the acute nature of the conflicts of interest presented and the risks of self-dealing by affiliates in transactions that are "directly related" to the same municipal securities transaction or municipal financial product as to which the affiliated municipal advisor is providing or has provided advice. Significantly, the prohibition is limited to certain types of transactions (i.e., purchases or sales of a security or those involving entering into a derivative, guaranteed investment contract, or other similar financial product). Finally, in connection with affiliates, if the prohibition on principal transactions were modified by "knowingly," the MSRB believes the standard would be overly stringent, which could hinder regulatory examinations and enforcement.

Relationship between the Ban and Rule G-23

In the First Request for Comment, the ban prohibiting municipal advisors (and their affiliates) from engaging in principal transactions with the municipal advisor's clients included the exception: "Except for an activity that is expressly permitted under [MSRB] Rule G-23" ("Rule G-23 exception"). The Rule G-23 exception was included to address the interrelationship between the proposed specific prohibition on principal transactions in Initial Draft Rule G-42 and principal transactions that are permitted by underwriters under Rule G-23.

Commenters sought clarity regarding the relationship between Rule G-23 and the prohibition on principal transactions in the Initial Draft Rule. In response to the First Request for Comment, commenters asked whether the prohibition on principal

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[79] See 15 U.S.C. 80b-6(3).

transactions was in conflict with principal transactions discussed in Rule G-23, under which a municipal advisor could acquire, as a principal, all or any portion of an issuance of municipal securities for which the municipal advisor had provided advice, as long as the municipal advisor complied with Rule G-23. BDA and GKB noted that, although the provision in the proposed ban referenced an exception for activities that are expressly permitted under Rule G-23, it was unclear what principal transactions would be permitted. Lamont commented that MSRB rules applicable to municipal advisors should not conflict with MSRB rules applicable to dealers regarding principal transactions, observing that, in its view, a fiduciary duty to the issuer will require additional steps to ensure that the pricing has been at least as favorable as having a third party in the transaction.

After careful consideration of the comments, the MSRB developed the Revised Draft Rule to clarify the relationship between the proposed ban on principal transactions and those principal transactions currently permitted under Rule G-23. Specifically, paragraph .07 to the Supplementary Material of the Revised Draft Rule described the Rule G-23 exception to the ban, providing that subsection (e)(ii) would not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities, provided that the municipal advisor complied with the requirements of Rule G-23. Thus, the Rule G-23 exception was more clearly described using the particular terminology in Rule G-23, rather than solely cross-referencing Rule G-23.

Several of the comments received in response to the Second Request for Comment continued to seek clarification regarding the Rule G-23 exception, desiring to avoid confusion regarding any express and direct conflict between the ban and Rule G-23. GFOA sought additional amendments to paragraph .07 of the Supplementary Material, seeking to "ensure that no component of a final Rule on G-42 removes the authority of issuers to decide for themselves how they utilize a [municipal advisor] or underwriter on a transaction so long as compliance with MSRB Rule G-23, MSRB Rule G-42 and the SEC's Municipal Advisor Rule are maintained." In BDA's view, the Revised Draft Rule language did not clarify the provision compared with the prior language regarding when a municipal advisor could act as a principal on the same transaction for which it is providing advice.

Sanchez appeared to interpret the provision to mean that a transaction permitted by Rule G-23 would be deemed in all cases to be lawful vis-a-vis other requirements under proposed Rule G-42 (such as the duty of loyalty) and under other laws (such as the statutory fiduciary duty). Columbia Capital commented that the sentence regarding the Rule G-23 exception in paragraph .07 of the Supplementary Material should be deleted because it "contemplates a situation where an MA could serve as a principal in a transaction for which it provides MA services, creating a conflict" with the proposed prohibition on principal transactions. Finally, ABA commented that the clarification regarding the conflict between Rule G-23 and draft Rule G-42(e)(ii) is unnecessary, or, if the clarification is retained, the phrase, "provided that the municipal advisor complies

with all of the provisions of Rule G-23," should be deleted and the phrase, "provided that such a transaction is not prohibited by the provisions of Rule G-23," should be incorporated.

The MSRB notes that the purpose of the sentence regarding the Rule G-23 exception in paragraph .07 of the Supplementary Material is to avoid a potential inconsistency in the MSRB's rules by providing specifically in Proposed Rule G-42, until such time as the MSRB may further review and potentially revise Rule G-23, that the specific ban on principal transactions in proposed subsection (e)(ii) does not prohibit a type of principal transaction that is already addressed and prohibited to a certain extent by Rule G-23. To further clarify this point, and respond to the comment by ABA, the MSRB has deleted the phrase "provided that the municipal advisor complies with all the provisions of Rule G-23" from the end of paragraph .07, and substituted the phrase "that is a type of transaction that is addressed by Rule G-23." Also, in response to the comments requesting additional clarification, the MSRB has included the phrase "on the basis that the municipal advisor provided advice as to the issuance." Proposed paragraph .07 of the Supplementary Material, as revised, would provide:

> In addition, the specific prohibition in subsection (e)(ii) . . . shall not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities <u>on the basis that the municipal advisor provided advice as to the issuance because that is a type of transaction that is addressed and prohibited in certain circumstances by Rule G-23</u> (emphasis added).

The MSRB cautions that this provision is quite limited, providing an exception only to the specific prohibition in subsection G-42(e)(ii); and it would not mean, for example, that a transaction not prohibited by Rule G-23 is deemed in all cases to be lawful vis-a-vis all other requirements under Proposed Rule G-42 (such as the duty of loyalty) and under other laws (such as the statutory fiduciary duty).

Inadvertent Advice – Supplementary Material .06

In response to the Second Request for Comment, several commenters expressed concerns and suggested changes to the inadvertent advice exclusion in paragraph .06 of the Supplementary Material to the Revised Draft Rule. First, NAIPFA believed the paragraph impermissibly creates an additional exemption from the Commission's definition of the term "municipal advisor" and is inconsistent with Rule G-23, allowing broker-dealers to provide advice to municipal entities and obligated persons as municipal advisors without becoming subject to corresponding fiduciary responsibilities and ultimately allowing such municipal advisors to serve as underwriters of the securities being issued. Similarly, WM Financial believed paragraph .06 negated Rule G-23 and effectively allowed broker-dealers to serve as municipal advisors and then switch to serving as underwriters, undermining the definition of "municipal advisor" and the exemptions thereto provided by the SEC. Contrary to NAIPFA and WM Financial,

Sanchez stated that "it appears reasonably clear at the moment that Supplementary Material .06 is only intended to provide relief from subsections (b) and (c) of Proposed Rule G-42;" however, he believed it would be useful for the MSRB to also include an affirmative statement that even inadvertent advice is subject to all other rules and requirements applicable to municipal advisory activities and financial advisory relationships entered into by broker-dealers under Rule G-23, Commission rules, and the fiduciary duty set forth in the Exchange Act.

NAIPFA and WM Financial misinterpreted the safe harbor provided by paragraph .06 as broadly relieving a municipal advisor of other regulatory requirements. To address such confusion, the MSRB has revised paragraph .06 of the Supplementary Material to include a clarifying statement that the relief the paragraph provides "has no effect on the applicability of any provisions" of Proposed Rule G-42, other than sections (b) and (c) (relating to documentation of the municipal advisory relationship and the disclosure of conflicts of interest, respectively) or any other legal requirements applicable to municipal advisory activities, which would include, but are not limited to, SEC rules and Rule G-23.

Second, SIFMA suggested that the MSRB broaden the limited safe harbor provided by paragraph .06 to relieve municipal advisors that inadvertently engage in municipal advisory activities from compliance with section (d) and subsection (e)(ii) of the Revised Draft Rule. Section (d) would require a suitability analysis of recommendations made by the municipal advisor or by a third party while subsection (e)(ii) would prohibit principal transactions directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice. The MSRB believes that, despite inadvertently engaging in municipal securities activities, a municipal advisor should not be relieved of complying with the suitability analysis requirement to the extent the municipal advisor made or reviewed a recommendation as contemplated by Proposed Rule G-42(d). Further, the MSRB does not believe, as SIFMA suggested, that firms would be less likely to perform the disclaimer process under paragraph .06 because doing so would not permit them to engage in a principal transaction prohibited under Proposed Rule G-42(e)(ii). Specifically, use of the exemption under paragraph .06 would only relieve a municipal advisor of compliance with the requirements of Proposed Rule G-42(b) and (c), and the prohibition on principal transactions would apply to the municipal advisor regardless. Therefore, the MSRB has not revised paragraph .06 in response to these comments.

Third, NAIPFA highlighted the importance of prompt use of the safe harbor provided by paragraph .06, suggesting that the proposed rule require utilization within ten days of discovery of the inadvertent advice. The MSRB has not prescribed a strict time frame for when the documentation must be provided by the municipal advisor beyond the general "promptly" standard, as doing so would create an arbitrary bright line that would be of limited benefit to municipal advisors or their clients. In response to the comment and to ensure that municipal advisors seeking to obtain the relief provided under paragraph .06 do so in a timely manner after having discovered that they inadvertently provided advice, the MSRB modified paragraph .06 to require municipal advisors to

provide the documentation it prescribes "as promptly as possible after discovery" (emphasis added).

Fourth, SIFMA noted that there are circumstances in which a registered municipal advisor could be engaged in municipal advisory activities for some clients, but inadvertently provide advice to another client, and, therefore, could not state that it "has ceased engaging in municipal advisory activities" to comply with paragraph .06. In response to the comment, the MSRB has revised the disclaimer required by subparagraph (a) of paragraph .06 of the Supplementary Material to state that, effective immediately, the municipal advisor has ceased engaging in municipal advisory activities "with respect to that municipal entity or obligated person in regard to all transactions and municipal financial products as to which advice was inadvertently provided . . . ." (emphasis added). This revision would clarify that the municipal advisor is not required to cease all municipal advisory activities to obtain the relief provided by paragraph .06.

Fifth, NAIPFA highlighted the importance of the identification of the inadvertent advice, suggesting requiring the identification of absolutely all of the inadvertent advice. In response to this comment, the MSRB revised subparagraph (c) of paragraph .06 to require that the municipal advisor identify all of the advice that was provided inadvertently, based on a reasonable investigation. This objective standard for the investigation would avoid requiring municipal advisors to go to impractical lengths to ensure that all inadvertent advice was identified, and the MSRB believes this would be sufficient to allow municipal advisor clients to assess risk exposure from any reliance on the advice and determine what potential mitigating actions need to be taken.

Finally, SIFMA suggested that the MSRB should carve out an exception for all advice that is incidental to brokerage/securities execution services. In the MSRB's view, SIFMA's request, as noted above, is a request that the MSRB interpret the SEC Final Rule and the definition of "municipal advisor," therein. The authority to interpret the Commission's rule lies with the Commission and the request should be directed to the Commission. As such, the MSRB declines to revise paragraph .06 of the Supplementary Material in this manner.

Trigger for Municipal Advisor Relationship

Subsection (f)(vi) would define "municipal advisory relationship" for purposes of Proposed Rule G-42 and states that a municipal advisory relationship will "be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person." In response to the Second Request for Comment, Columbia Capital objected to the deletion of "engages" from the definition of "municipal advisory relationship" in subsection (f)(vi) of the Revised Draft Rule. Specifically, Columbia Capital stated that, "[i]f a person provides 'advice' he/she should trigger the [municipal advisor] duties at the time of providing that advice and should be considered [a municipal advisor] unless that person qualifies for an exemption or exclusion at the time such advice is provided." Under the proposed rule change, the municipal advisory relationship would begin at the time a municipal advisor enters into

an agreement to engage in municipal advisory activities, which then triggers the documentation requirements of Proposed Rule G-42(c).

The MSRB believes Columbia Capital's concern is moot because the other duties required by Proposed Rule G-42, including, but not limited to, providing written disclosures to clients, would be triggered when a municipal advisor engages in municipal advisory activities. The MSRB also notes that engaging in municipal advisory activities would subject a firm to municipal advisor registration requirements and any other legal requirements applicable to municipal advisory activities. Accordingly, the MSRB has not revised subsection (f)(vi) of the Revised Draft Rule, as incorporated into the proposed rule, in response to this comment.

Economic Analysis of Comments on Economic Implications of Proposed Rule

Economic Analysis – Cost of Compliance

Several commenters stated that the cost of complying with the proposed rule would be "burdensome" or "significant." In some cases, commenters identified alternative approaches that they considered to be less costly. No commenter provided specific cost information or data that would support an improved estimate of the costs of compliance.

FSR and SIFMA both stated that the requirement on municipal advisors to provide disclosure of all material conflicts of interest including any of its affiliates that provides any advice, service, or product directly or indirectly related to performing municipal advisory activities would be burdensome, particularly for municipal advisors that are part of large financial conglomerates. Sanchez commented that a "written statement" would be less burdensome than "written documentation" when municipal advisors conclude that material conflicts of interest exist. FSR, SIFMA, and Sanchez commented that the detailed disclosure of disciplinary events material to the client's evaluation of the municipal advisor could be accomplished at a lower cost by allowing municipal advisors to reference the documentation provided to the SEC on Forms MA and MA-I. Columbia Capital requested that the MSRB consider allowing municipal advisors to use more than one document to meet the requirement for documentation of the municipal advisory relationship.

The MSRB agrees that municipal entities and obligated persons can be made aware of relevant conflicts of interest at a lower cost by revising some of the requirements. To that end, the MSRB amended Proposed Rule G-42(b)(i)(A) to narrow the scope of potential conflicts that would need to be disclosed from those that "might" impair the advisor's ability to provide advice to those that "could reasonably be anticipated to impair" the advisor's ability and Proposed Rule G-42(b)(i)(B) to remove the requirement to disclose potential conflicts that might arise from advice, service, or products provided by affiliates and indirectly related to the performance of municipal advisory activities. The MSRB also amended Rule G-42(b)(i) to allow for a written statement instead of written documentation if a municipal advisor concludes that no

known material conflicts of interest exist. The MSRB also agrees that information regarding disciplinary events may be disclosed by identification of the specific type of the event and specific reference to the relevant portions of Forms MA and MA-I and has amended Proposed Rule G-42(b)(ii) to reflect this. Finally, the MSRB has clarified that a municipal advisor may use multiple documents to document the relationship by adding the plural "writings" to Proposed Rule G-42(c).

Economic Analysis – Transition Period

Lewis Young urged the MSRB to adopt a transitional period to permit advisors to honor their existing financial advisory agreements. They stated that many financial advisory agreements are longer-term arrangements and that advisors should be provided with a reasonable opportunity to conform existing arrangements to the requirements of the proposed rule when they are renewed or after a reasonable phase-in period after the rule is finalized. Zion also urges the MSRB to include a transitional provision to permit advisors to honor existing contracts, including many that are multi-year contracts. Zion notes the significant time, effort, and expense that would be involved to supplement or amend existing contracts with additional content and disclosure required by the proposed rule. Zion states that under particular state and/or local procurement laws, the alterations to existing agreements may reopen the request for proposal process for issuers to hire municipal advisors, requiring additional (and significant) time, effort, and expense.

The MSRB believes that the required disclosure can generally be accomplished without formal amendments and, therefore, that the costs imposed will be less significant than generally anticipated.

Economic Analysis – Burden on Small Municipal Advisors

MSRB did not receive any comments specific to the Dodd-Frank Act requirement that MSRB rules not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons provided that there is robust protection of investors against fraud.[80]

Nonetheless, the MSRB has been sensitive to the potential impact of the requirements contained in Proposed Rule G-42. To that end, the MSRB has made efforts to minimize costs, particularly those that might be expected to disproportionately impact smaller firms. In addition to the amendments discussed above that will reduce compliance costs, the MSRB has made changes to proposals included in prior Requests for Comment such as clarifying the obligations owed by municipal advisors to obligated persons, narrowing the circumstances under which disclosures related to the municipal advisory relationship and compensation arrangements need to be made, and removing disclosure requirements related to professional liability insurance.

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[80] See 15 U.S.C. 78o-4(b)(2)(L)(iv).

The MSRB acknowledges that there will be costs associated with complying with this proposed rule and that some municipal advisors, including smaller firms, may exit the market as a result. However, the MSRB believes the costs and burdens are limited to those necessary to meet the objectives of the rule, consistent with its statutory basis.

6. Extension of Time Period for Commission Action

The MSRB declines to consent to an extension of the time period specified in Section 19(b)(2)[81] or Section 19(b)(7)(D)[82] of the Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

11. Exhibits

Exhibit 1	Completed Notice of Proposed Rule Change for Publication in the Federal Register
Exhibit 2	Notices Requesting Comment and Comment Letters
Exhibit 5	Text of Proposed Rule Change

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81 15 U.S.C. 78s(b)(2).

82 15 U.S.C. 78s(b)(7)(D).

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-_____; File No. SR-MSRB-2015-03)

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change Consisting of Proposed New Rule G-42, on Duties of Non-Solicitor Municipal Advisors, and Proposed Amendments to Rule G-8, on Books and Records to be Made by Brokers, Dealers, Municipal Securities Dealers, and Municipal Advisors

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on the Municipal Securities Rulemaking Board (the "MSRB" or "Board") filed with the Securities and Exchange Commission (the "SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the MSRB. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The MSRB filed with the Commission a proposed rule change consisting of proposed new Rule G-42, on duties of non-solicitor municipal advisors, and proposed amendments to Rule G-8, on books and records to be made by brokers, dealers, municipal securities dealers, and municipal advisors (the "proposed rule change"). The MSRB requests that the proposed rule change be approved with an implementation date six months after the Commission approval date for all changes.

The text of the proposed rule change is available on the MSRB's website at www.msrb.org/Rules-and-Interpretations/SEC-Filings/2015-Filings.aspx, at the MSRB's

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1 15 U.S.C. 78s(b)(1).

2 17 CFR § 240.19b-4.

principal office, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the MSRB included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The MSRB has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Following the financial crisis of 2008, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").[3] The Dodd-Frank Act establishes a new federal regulatory regime requiring municipal advisors to register with the SEC, deeming them to owe a fiduciary duty to their municipal entity clients and granting the MSRB rulemaking authority over them. The MSRB, in the exercise of that authority, is currently developing a comprehensive regulatory framework for municipal advisors. A significant element of that regulatory framework is Proposed Rule G-42, which would establish core standards of conduct for municipal advisors that engage in municipal advisory activities, other than municipal advisory solicitation activities (hereinafter, "municipal advisors").[4] Proposed Rule G-42 is accompanied by associated proposed amendments to Rule G-8.

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3 Pub. Law No. 111-203, 124 Stat. 1376 (2010).

4 See Registration of Municipal Advisors, Rel. No. 34-70462 (Sept. 20, 2013), 78 FR 67467, at 67519, note 679 (Nov. 12, 2013) ("SEC Final Rule") (recognizing that the regulation of municipal advisors includes the "application of standards of conduct . . .

Proposed Rule G-42

Proposed Rule G-42 would establish the core standards of conduct and duties of municipal advisors when engaging in municipal advisory activities. The proposed rule draws on aspects of existing law and regulation under other relevant regulatory regimes, including those applicable to brokers, dealers and municipal securities dealers under MSRB rules and the Exchange Act, investment advisers under the Investment Advisers Act of 1940[5] ("Investment Advisers Act") and commodity trading advisors under the Commodity Exchange Act ("CEA").[6]

In summary, the core provisions of Proposed Rule G-42 would:

- Establish certain standards of conduct consistent with the fiduciary duty owed by a municipal advisor to its municipal entity clients, which includes, without limitation, a duty of care and of loyalty;
- Establish the standard of care owed by a municipal advisor to its obligated person clients;
- Require the full and fair disclosure, in writing, of all material conflicts of interest and legal or disciplinary events that are material to a client's evaluation of a municipal advisor;
- Require the documentation of the municipal advisory relationship, specifying certain aspects of the relationship that must be included in the documentation;

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that may be required by the Commission or the MSRB, and other requirements unique to municipal advisors that may be imposed by the MSRB"). The proposed rule change would not apply to municipal advisors when engaging in the solicitation of a municipal entity or obligated person within the meaning of Exchange Act Section 15B(e)(9) (15 U.S.C. 78o-4(e)(9)).

5 15 U.S.C. 80b-1 et seq.

6 7 U.S.C. 1 et seq.

- Require that recommendations made by a municipal advisor are suitable for its clients, or determine the suitability of recommendations made by third parties when appropriate; and
- Specifically prohibit a municipal advisor from engaging in certain activities, including, in summary:
    - receiving excessive compensation;
    - delivering inaccurate invoices for fees or expenses;
    - making false or misleading representations about the municipal advisor's resources, capacity or knowledge;
    - participating in certain fee-splitting arrangements with underwriters;
    - participating in any undisclosed fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client of the municipal advisor;
    - making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities, with limited exceptions; and
    - entering into certain principal transactions with the municipal advisor's municipal entity clients.

In addition, the proposed rule change would define key terms used in Proposed Rule G-42 and provide supplementary material. The supplementary material would provide additional guidance on the core concepts in the proposed rule, such as the duty of care, the duty of loyalty, suitability of recommendations and "Know Your Client" obligations; provide context for issues such as the scope of an engagement, conflicts of interest disclosures, excessive compensation and the impact of client action that is independent of or contrary to the advice of a municipal

advisor, and the applicability of the proposed rule change to 529 college savings plans ("529 plans") and other municipal entities; provide guidance regarding the definition of "engage in a principal transaction;" the continued applicability of state and other laws regarding fiduciary and other duties owed by municipal advisors; and, finally, include information regarding requirements that must be met for a municipal advisor to be relieved of certain provisions of Proposed Rule G-42 in instances when it inadvertently engages in municipal advisory activities.

Standards of Conduct

Section (a) of Proposed Rule G-42 would establish the core standards of conduct and duties applicable to municipal advisors. The approach toward the core standards and duties in Proposed Rule G-42 flows from the distinctions drawn in the Dodd-Frank Act between a municipal advisor's duties owed to clients that are municipal entities and those duties owed to clients that are obligated persons. The Dodd-Frank Act specifically deems a municipal advisor to owe a fiduciary duty to its municipal entity clients.[7] In contrast, the Dodd-Frank Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients.[8]

Subsection (a)(i) of Proposed Rule G-42 would provide that each municipal advisor in the conduct of its municipal advisory activities for an obligated person client is subject to a duty of care. Subsection (a)(ii) would provide that each municipal advisor in the conduct of its

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7 See Section 15B(c)(1) of the Exchange Act, 15 U.S.C. 78o-4(c)(1) which provides:

> A municipal advisor and any person associated with such municipal advisor shall be deemed to have a fiduciary duty to any municipal entity for whom such municipal advisor acts as a municipal advisor, and no municipal advisor may engage in any act, practice, or course of business which is not consistent with a municipal advisor's fiduciary duty or that is in contravention of any rule of the Board.

8 See SEC Final Rule, 78 FR at 67475, note 100.

municipal advisory activities for a municipal entity client is subject to a fiduciary duty, which includes, without limitation, a duty of loyalty and a duty of care. The standards contained in these subsections would not supersede any more restrictive provisions of state or other laws applicable to the activities of municipal advisors.

Proposed supplementary material would provide guidance on the duty of care and the duty of loyalty. Generally, in lieu of providing detailed requirements, the duties would be described in terms that would empower the client to, in large part, determine the scope of services and control the engagement with the municipal advisor (with the municipal advisor's agreement).

Paragraph .01 of the Supplementary Material would describe the duty of care to require, without limitation, a municipal advisor to: (1) exercise due care in performing its municipal advisory activities; (2) possess the degree of knowledge and expertise needed to provide the municipal entity or obligated person client with informed advice; (3) make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client; and (4) undertake a reasonable investigation to determine that the municipal advisor is not basing any recommendation on materially inaccurate or incomplete information. The duty of care that would be established in section (a) of Proposed Rule G-42, would also require the municipal advisor to have a reasonable basis for: any advice provided to or on behalf of a client;[9] any representations made in a certificate that it signs that will be reasonably foreseeably relied upon by the client,

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[9] The duty of care, which is applicable to all municipal advisory activities, would apply to the provision of comments following the review of any document and the provision of language for use in any document -- including an official statement -- to the extent that conduct constituted municipal advisory activity. Furthermore, such conduct would be required to comport with the fiduciary duty owed in the case of a municipal entity client.

any other party involved in the municipal securities transaction or municipal financial product, or investors in the municipal entity client's securities or securities secured by payments from an obligated person client; and, any information provided to the client or other parties involved in the municipal securities transaction in connection with the preparation of an official statement for any issue of municipal securities as to which the advisor is advising.

Paragraph .02 of the Supplementary Material would describe the duty of loyalty to require, without limitation, a municipal advisor, when engaging in municipal advisory activities for a municipal entity, to deal honestly and with the utmost good faith with the client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. Paragraph .02 would also provide that the duty of loyalty would preclude a municipal advisor from engaging in municipal advisory activities with a municipal entity client if it cannot manage or mitigate its conflicts of interest in a manner that will permit it to act in the municipal entity's best interests.

Paragraph .03 of the Supplementary Material would specify that a municipal advisor is not required to disengage from a municipal advisory relationship if a municipal entity client or an obligated person client elects a course of action that is independent of or contrary to advice provided by the municipal advisor.

Paragraph .04 of the Supplementary Material would specify that a municipal advisor could limit the scope of the municipal advisory activities to be performed to certain specified activities or services if requested or expressly consented to by the client, but could not alter the standards of conduct or impose limitations on any of the duties prescribed by Proposed Rule G-42. Paragraph .04 would provide that, if a municipal advisor engages in a course of conduct that

is inconsistent with the mutually agreed limitations to the scope of the engagement, it may result in negating the effectiveness of the limitations.

Paragraph .07 of the Supplementary Material would state, as a general matter, that, municipal advisors may be subject to fiduciary or other duties under state or other laws and nothing in Proposed Rule G-42 would supersede any more restrictive provision of state or other laws applicable to municipal advisory activities.

Disclosure of Conflicts of Interest and Other Information

Section (b) of Proposed Rule G-42 would require a municipal advisor to fully and fairly disclose to its client in writing all material conflicts of interest, and to do so prior to or upon engaging in municipal advisory activities. The provision would set forth a non-exhaustive list of scenarios under which a material conflict of interest would arise or be deemed to exist and that would require a municipal advisor to provide written disclosures to its client.

Paragraph (b)(i)(A) would require a municipal advisor to disclose any actual or potential conflicts of interest of which the municipal advisor becomes aware after reasonable inquiry that could reasonably be anticipated to impair the municipal advisor's ability to provide advice to or on behalf of the client in accordance with the applicable standards of conduct (i.e., a duty of care or a fiduciary duty). Paragraphs (b)(i)(B) through (F) would provide more specific scenarios that give rise to conflicts of interest that would be deemed to be material and require proper disclosure to a municipal advisor's client. Under the proposed rule change, a material conflict of interest would always include: any affiliate of the municipal advisor that provides any advice, service or product to or on behalf of the client that is directly related to the municipal advisory activities to be performed by the disclosing municipal advisor; any payments made by the municipal advisor, directly or indirectly, to obtain or retain an engagement to perform municipal

advisory activities for the client; any payments received by the municipal advisor from a third party to enlist the municipal advisor's recommendations to the client of its services, any municipal securities transaction or any municipal financial product; any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client; and any conflicts of interest arising from compensation for municipal advisory activities to be performed that is contingent on the size or closing of any transaction as to which the municipal advisor is providing advice. Paragraph (b)(i)(G) would require municipal advisors to disclose any other engagements or relationships of the municipal advisor that could reasonably be anticipated to impair its ability to provide advice to or on behalf of its client in accordance with the applicable standards of conduct established by section (a) of the proposed rule.

Under subsection (b)(i), if a municipal advisor were to conclude, based on the exercise of reasonable diligence, that it had no known material conflicts of interest, the municipal advisor would be required to provide a written statement to the client to that effect.

Subsection (b)(ii) would require disclosure of any legal or disciplinary event that would be material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel. To facilitate the use of existing records, a municipal advisor would be permitted to fulfill this disclosure obligation by identifying the specific type of event and specifically referring the client to the relevant portions of the municipal advisor's most recent SEC Forms MA or MA-I[10] filed with the Commission, if the municipal advisor provides detailed information specifying where the client could access such forms electronically. The requirement to specifically refer to the relevant portions of the forms would not be satisfied by a broad reference to the section of the forms containing such disclosures. Similarly, the specific-

[10] See 17 CFR 249.1300 (SEC Form MA); 17 CFR 249.1310 (SEC Form MA-I).

information requirement for access to the forms would not be satisfied by a general reference to the SEC's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR"). A municipal advisor could alternatively meet this latter requirement, for example, by publishing its most recent forms on its own website and then providing the client with the direct web link or internet address.

Paragraph .05 of the Supplementary Material would provide that the required conflicts of interest disclosures must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict and must include an explanation of how the municipal advisor addresses or intends to manage or mitigate each conflict.[11] Coupled with its duty to disclose material conflicts of interest, a municipal advisor's obligation to explain how it addresses or intends to manage or mitigate its material conflicts of interest was included in the proposed rule to reflect the Board's intent to eliminate, or at least to expose and reduce the occurrence of, material conflicts of interest that might incline a municipal adviser to provide advice or a recommendation which was not disinterested.[12] If not properly managed or mitigated, material conflicts of interest could lead to a failure to protect a municipal advisor's client's interest, thereby causing a breach of the duty of care and/or loyalty that would be established by proposed section (a).

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[11] This requirement is analogous to the requirement of Form ADV (17 CFR 279.1) under the Investment Advisers Act (15 U.S.C. 80b-1 et seq.) that obligates an investment adviser to describe how it addresses certain conflicts of interest with its clients. See, e.g., Form ADV, Part 2, Item 5.E.1 of Part 2A (requiring an investment adviser to describe how it will address conflicts of interest that arise in regards to fees and compensation it receives, including the investment adviser's procedures for disclosing the conflicts of interest with its client). See also, Form ADV, Part 2A Items 6, 10, 11, 14 and 17.

[12] See, e.g., SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191-92 (1963).

Paragraph .06 of the Supplementary Material would provide that a municipal advisor that inadvertently engages in municipal advisory activities but does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship[13] would not be required to comply with sections (b) and (c) of Proposed Rule G-42 (relating to disclosure of conflicts of interest and documentation of the relationship), if the municipal advisor takes the prescribed actions listed under paragraph .06 promptly after it discovers its provision of inadvertent advice. The municipal advisor would be required to provide to the client a dated document that would include: a disclaimer stating that the municipal advisor did not intend to provide advice and that, effective immediately, the municipal advisor has ceased engaging in municipal advisory activities with respect to that client in regard to all transactions and municipal financial products as to which advice was inadvertently provided; a notification that the client should be aware that the municipal advisor has not provided the disclosure of material conflicts of interest and other information required under section (b); an identification of all of the advice that was inadvertently provided, based on a reasonable investigation; and a request that the municipal entity or obligated person acknowledge receipt of the document. The municipal advisor also would be required to conduct a review of its supervisory and compliance policies and procedures to ensure that they are reasonably designed to prevent inadvertently providing advice to municipal entities and obligated persons. The final sentence of paragraph .06 of the Supplementary Material would also clarify that the satisfaction of the requirements of paragraph

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13 Under subsection (f)(vi) of Proposed Rule G-42, a municipal advisory relationship would be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person, and would be deemed to have ended on the earlier of (i) the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship required in section (c) of Proposed Rule G-42 or (ii) the date on which the municipal advisor withdraws from the municipal advisory relationship.

.06 would have no effect on the applicability of any provisions of Proposed Rule G-42 other than sections (b) and (c), or any other legal requirements applicable to municipal advisory activities. Such other legal requirements, would include, but would not be limited to, other MSRB rules (including Rule G-23), Financial Industry Regulatory Authority ("FINRA") rules or federal or state laws that apply to municipal advisory activities.[14]

Documentation of the Municipal Advisory Relationship

Section (c) of Proposed Rule G-42 would require each municipal advisor to evidence each of its municipal advisory relationships by a writing, or writings created and delivered to the municipal entity or obligated person client prior to, upon or promptly after the establishment of the municipal advisory relationship. The documentation would be required to be dated and include, at a minimum:[15]

- the form and basis of direct or indirect compensation, if any, for the municipal advisory activities to be performed, as provided in proposed subsection (c)(i);
- the information required to be disclosed in proposed section (b), including the disclosures of conflicts of interest, as provided in proposed subsection (c)(ii);
- a description of the specific type of information regarding legal and disciplinary events requested by the Commission on SEC Form MA and SEC Form MA-I, as

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[14] Rule G-23, on activities of financial advisors, generally provides that a dealer that has a financial advisory relationship (as defined by Rule G-23(b)) with respect to the issuance of municipal securities is precluded from acquiring all or any portion of such issue, directly or indirectly, from the issuer as principal, either alone or as a participant in a syndicate or other similar account formed for that purpose. A dealer is also, under Rule G-23, precluded from arranging the placement of an issue with respect to which it has a financial advisory relationship.

[15] While no acknowledgement from the client of its receipt of the documentation would be required, a municipal advisor must, as part of the duty of care it owes its client, reasonably believe that the documentation was received by its client.

provided in proposed subsection (c)(iii), and detailed information specifying where the client may electronically access the municipal advisor's most recent Form MA and each most recent Form MA-I filed with the Commission;[16]

- the date of the last material change to the legal or disciplinary event disclosures on any SEC Forms MA or MA-I filed with the Commission by the municipal advisor, as provided in proposed subsection (c)(iv);
- the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement, as provided in proposed subsection (c)(v);
- the date, triggering event, or means for the termination of the municipal advisory relationship, or, if none, a statement that there is none, as provided in proposed subsection (c)(vi); and
- any terms relating to withdrawal from the municipal advisory relationship, as provided in proposed subsection (c)(vii).

Proposed Rule G-42(c) also would require municipal advisors to promptly amend or supplement the writing(s) during the term of the municipal advisory relationship as necessary to reflect any material changes or additions in the required information. For example, if the basis of compensation or scope of services materially changed during the term of the relationship, the municipal advisor would be required to amend or supplement the writing(s) and promptly deliver

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[16] Compliance with this requirement could be achieved in the same manner, and (so long as done upon or prior to engaging in municipal advisory activities for the client) concurrently with providing to the client the information required under proposed subsection (b)(ii). However, the description of the events contained in Forms MA or MA-I must be sufficiently specific to allow a municipal entity or obligated person client to understand the nature of any disclosed legal or disciplinary event. In addition, the municipal advisor must provide detailed information specifying where the client could access such forms electronically. See supra note 10 and accompanying text.

the amended writing(s) or supplement to the client. The same would be true in the case of material conflicts of interest discovered after the relationship documentation was last provided to the client. The amendment and supplementation requirement in proposed section (c) would apply to any material changes and additions that are discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor. Any amendments or supplementation also would be subject to the requirements of the proposed rule change that would apply as if it were the first relationship documentation provided to the client.

Proposed Rule G-42(c) is modeled in part on Rule G-23, which requires a broker, dealer or municipal securities dealer ("dealer") that enters into a financial advisory relationship with an issuer to evidence that relationship in writing prior to, upon or promptly after the inception of that relationship. Like Rule G-23, proposed section (c) would not require that the writing(s) evidencing the relationship be a bilateral agreement or contract. For example, if state law provided for the procurement of municipal advisory services in a manner that did not require a writing sufficient to establish a bilateral agreement, a municipal advisor could send its client a writing, such as a letter that references the procurement document and contains the terms and disclosures required by proposed Rule G-42(b) and (c) to evidence its municipal advisory relationship with its municipal entity or obligated person client.

Recommendations and Review of Recommendations of Other Parties

Section (d) of Proposed Rule G-42 would provide that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product unless the municipal advisor has determined, based on the information obtained through the reasonable diligence of the municipal advisor, whether the transaction or product is suitable

for the client.[17] Proposed section (d) also contemplates that a municipal advisor may be requested by the client to review and determine the suitability of a recommendation made by a third party to the client. If a client were to request this type of review, and such review were within the scope of the engagement, the municipal advisor's determination regarding the suitability of the third-party's recommendation regarding a municipal securities transaction or municipal financial product would be subject to the same reasonable diligence standard -- requiring the municipal advisor to obtain relevant information through the exercise of reasonable diligence.

As to both types of review, the municipal advisor would be required under proposed section (d) to inform its municipal entity or obligated person client of its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the advisor reasonably believes the recommended transaction or product is, or is not, suitable for the client; and whether the municipal advisor has investigated or considered other reasonably feasible

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[17] Some securities market participants are required to make only recommendations that are "consistent with" their customer's best interests. (See FINRA Notice 12-25, Suitability (May 2012)). As provided in proposed section (a) and paragraph .02 of the Supplementary Material to Proposed Rule G-42, a municipal advisor to a municipal entity client owes the client a fiduciary duty that includes a duty of loyalty in addition to the duty of care, which requires the municipal advisor to deal honestly and with the utmost good faith with the municipal entity client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. A municipal advisor's recommendations of municipal securities transactions and municipal financial products to a municipal entity client, as is the case with all municipal advisory activities performed for a municipal entity client, must comport with the municipal advisor's fiduciary duty and particularly its duty of loyalty. The MSRB considers the duty of loyalty described in Proposed Rule G-42 to be even more rigorous than a standard requiring consistency with a client's best interests.

alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives. The proposed rule does not include requirements regarding how such information must be communicated by the municipal advisor to the client, and a municipal advisor would be permitted to choose the appropriate method by which to communicate the information to its client so long as it comports with the duty of care owed.

Section (d), like other provisions of Proposed Rule G-42, would reflect the basic principle that the client controls the scope of the engagement with its municipal advisor (with the agreement of the municipal advisor). For example, a municipal advisor's engagement may be limited in scope because the municipal advisor's client already reached a decision regarding a particular municipal securities transaction or municipal financial product, or engaged another professional to undertake certain duties in connection with a municipal securities transaction or municipal financial product. Paragraph .04 of the Supplementary Material would provide that a municipal advisor and its client could limit the scope of the municipal advisory relationship to certain specified activities or services. A municipal advisor, however, would not be permitted to alter the standards of conduct or duties imposed by the proposed rule with respect to that limited scope.

The proposed rule change would adopt, and apply to municipal advisors, the existing MSRB interpretive guidance regarding the general principles currently applicable to dealers for determining whether a particular communication constitutes a recommendation of a securities transaction.[18] Consistent with the approach in the case of dealers, a municipal advisor's

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[18] See MSRB Rule G-19. See also MSRB Notice 2002-30 (Sept. 25, 2002) Notice Regarding Application of Rule G-19, on Suitability of Recommendations and Transactions, to Online Communications.

communication to its client that could reasonably be viewed as a "call to action" to engage in a municipal securities transaction or enter into a municipal financial product would be considered a recommendation and obligate the municipal advisor to conduct a suitability analysis of its recommendation. Depending on all of the facts and circumstances, communications by a municipal advisor to a client that concern minor or ancillary matters that relate to, but are not recommendations of, a municipal securities transaction or municipal financial product might constitute advice (and therefore trigger many other provisions of the proposed rule) but would not trigger the suitability obligation set forth in proposed section (d).

Paragraph .08 of the Supplementary Material would provide guidance related to a municipal advisor's suitability obligations. Under this provision, a municipal advisor's determination of whether a municipal securities transaction or municipal financial product is suitable for its client must be based on numerous factors, as applicable to the particular type of client, including, but not limited to: the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued are reasonably expected to be outstanding, and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after the municipal advisor has conducted a reasonable inquiry.

In connection with a municipal advisor's obligation to determine the suitability of a municipal securities transaction or a municipal financial product for a client, which should take into account its knowledge of the client, paragraph .09 of the Supplementary Material would

require a municipal advisor to know its client. The obligation to know the client would require a municipal advisor to use reasonable diligence to know and retain essential facts concerning the client and the authority of each person acting on behalf of the client, and is similar to requirements in other regulatory regimes.[19] The facts "essential" to knowing one's client would include those required to effectively service the municipal advisory relationship with the client; act in accordance with any special directions from the client; understand the authority of each person acting on behalf of the client; and comply with applicable laws, rules and regulations.

As a practical matter, it is understood that a client could at times elect a course of action either independent of or contrary to the advice of its municipal advisor. Paragraph .03 of the Supplementary Material would provide that the municipal advisor would not be required to disengage from the municipal advisory relationship on that basis.

Specified Prohibitions

Subsection (e)(i) of Proposed Rule G-42 would prohibit discrete conduct or activities that would conflict, or would be highly likely to conflict, with the core standards of conduct – the duty of loyalty and the duty of care – applicable to municipal advisors under Proposed Rule G-42 and the Exchange Act.

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19 Similar requirements apply to brokers and dealers under FINRA Rule 2090 (Know Your Customer) and swap dealers under Commodity Futures Trading Commission ("CFTC") Rule 402(b) (General Provisions: Know Your Counterparty), 17 CFR 23.402(b), found in CFTC Rules, Ch. I, Pt. 23, Subpt. H (Business Conduct Standards for Swap Dealers and Major Swap Participants Dealing with Counterparties, including Special Entities) (17 CFR 23.400 et. seq.). Notably, the CFTC's rule applies to dealings with special entity clients, defined to include states, state agencies, cities, counties, municipalities, other political subdivisions of a State, or any instrumentality, department, or a corporation of or established by a State or political subdivision of a State. See CFTC Rule 401(c) (defining "special entity") (17 CFR 23.401(c)).

Paragraph (e)(i)(A) would prohibit a municipal advisor from receiving compensation from its client that is excessive in relation to the municipal advisory activities actually performed for the client. Paragraph .10 of the Supplementary Material would provide additional guidance on how compensation would be determined to be excessive. Included in paragraph .10 are several factors that would be considered when evaluating the reasonableness of a municipal advisor's compensation relative to the nature of the municipal advisory activities performed, including, but not limited to: the municipal advisor's expertise, the complexity of the municipal securities transaction or municipal financial product, whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product, the length of time spent on the engagement and whether the municipal advisor is paying any other relevant costs related to the municipal securities transaction or municipal financial product.

Paragraph (e)(i)(B) would prohibit municipal advisors from delivering an invoice for fees or expenses for municipal advisory activities that does not accurately reflect the activities actually performed or the personnel that actually performed those activities. This provision would not prohibit a municipal advisor from including a discount for the services it actually performed, if accurately disclosed.

Paragraph (e)(i)(C) would prohibit a municipal advisor from making any representation or submitting any information that the municipal advisor knows or should know is either materially false or materially misleading due to the omission of a material fact, about its capacity, resources or knowledge in response to requests for proposals or in oral presentations to a client or prospective client for the purpose of obtaining or retaining an engagement to perform municipal advisory activities. Note that, additionally, the MSRB's existing fundamental fair

practice rule, Rule G-17, precludes municipal advisors, in the conduct of their municipal advisory activities, from engaging in any deceptive, dishonest or unfair practice with any person.

Paragraph (e)(i)(D) would prohibit municipal advisors from making or participating in two types of fee-splitting arrangements: (1) any fee-splitting arrangement with an underwriter on any municipal securities transaction as to which the municipal advisor has provided or is providing advice; and (2) any undisclosed fee-splitting arrangement with providers of investments or services to a municipal entity or obligated person client of the municipal advisor.

Paragraph (e)(i)(E) would, generally, prohibit a municipal advisor from making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities. However, the provision contains three exceptions. The prohibition would not apply to: (1) payments to an affiliate of the municipal advisor for a direct or indirect communication with a municipal entity or obligated person on behalf of the municipal advisor where such communication is made for the purpose of obtaining or retaining an engagement to perform municipal advisory activities; (2) reasonable fees paid to another municipal advisor registered as such with the Commission and MSRB for making such a communication as described in subparagraph (e)(i)(E)(1); and (3) payments that are permissible "normal business dealings" as described in MSRB Rule G-20. The proposed rule change, however, would not prescribe parameters that would effectively limit a client's ability to decide the source of funds for the payment of fees for services rendered by the municipal advisor.

Principal Transactions

Subsection (e)(ii) of Proposed Rule G-42 would prohibit a municipal advisor to a municipal entity, and any affiliate of such municipal advisor, from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial

product as to which the municipal advisor is providing or has provided advice. The ban on principal transactions would apply only with respect to clients that are municipal entities. The ban would not apply to principal transactions between a municipal advisor (or an affiliate of the municipal advisor) and the municipal advisor's obligated person clients. Although such transactions would not be prohibited, importantly, all municipal advisors, including those engaging in municipal advisory activities for obligated person clients, are currently subject to the MSRB's fundamental fair-practice rule, Rule G-17.

Paragraph .07 of the Supplementary Material would provide an exception to the ban on principal transactions in subsection (e)(ii) in order to avoid a possible conflict with existing MSRB Rule G-23, on activities of financial advisors. Specifically, the ban in subsection (e)(ii) would not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities on the basis that the municipal advisor provided advice as to the issuance, because such a transaction is the type of transaction that is addressed, and, in certain circumstances, prohibited by Rule G-23. The purpose of this provision would be to avoid a potential conflict in MSRB rules and provide, until such time as the MSRB may further review and potentially amend Rule G-23, that the specific prohibition against principal transactions contained in subsection (e)(ii) would not prohibit such underwriting transactions, as they are already addressed and prohibited in certain circumstances by Rule G-23.

For purposes of the prohibition in proposed subsection (e)(ii), subsection (f)(i) would define the term "engaging in a principal transaction" to mean "when acting as a principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product

with the municipal entity client." This definition draws on the statutory language regarding principal transactions in the Investment Advisers Act.[20] Among other things, the definition was designed to exclude transactions thought to be potentially covered by some commenters, such as the taking of a cash deposit or the payment by a client solely for professional services. Further, paragraph .11 of the Supplementary Material would clarify that the term "other similar financial products," as used in subsection (f)(i), would include a bank loan but only if it is in an aggregate principal amount of $1,000,000 or more and is economically equivalent to the purchase of one or more municipal securities. Bank loans would be included under the specified circumstances because, as a matter of market practice, they serve as a financing alternative to the issuance of municipal securities and pose a comparable, acute potential for self-dealing and other breaches of the fiduciary duty owed by a municipal advisor to a municipal entity client.

Definitions

Section (f) of Proposed Rule G-42 would provide definitions of the terms "engaging in a principal transaction," "affiliate of the municipal advisor,"[21] "municipal advisory relationship,"[22]

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20 See 15 U.S.C. 80b-6(3).

21 "Affiliate of the municipal advisor" would mean "any person directly or indirectly controlling, controlled by, or under common control with such municipal advisor." See Proposed Rule G-42(f)(iii).

22 Proposed Rule G-42(f)(vi) provides that a "municipal advisory relationship" would

> be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person. The municipal advisory relationship shall be deemed to have ended on the date which is the earlier of (i) the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship required in section (c) of this rule or (ii) the date on which the municipal advisor withdraws from the municipal advisory relationship.

and "official statement."[23] Further, for several terms in Proposed Rule G-42 that have been previously defined by federal statute or SEC rules, proposed section (f) would, for purposes of Proposed Rule G-42, adopt the same meanings. These terms would include "advice;"[24] "municipal advisor;"[25] "municipal advisory activities;"[26] "municipal entity;"[27] and "obligated person."[28]

Applicability of Proposed Rule G-42 to 529 College Savings Plans and Other Municipal

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23 "Official statement" would have the same meaning as in MSRB Rule G-32(d)(vii). See Proposed Rule G-42(f)(ix).

24 "Advice" would have the same meaning as in Section 15B(e)(4)(A)(i) of the Exchange Act (15 U.S.C. 78o-4(e)(4)(A)(i)); SEC Rule 15Ba1-1(d)(1)(ii) (17 CFR 240.15Ba1-1(d)(1)(ii)); and other rules and regulations thereunder. See Proposed Rule G-42(f)(ii).

25 "Municipal advisor" would

> have the same meaning as in Section 15B(e)(4) of the Act, 17 CFR 240.15Ba1-1(d)(1)-(4) and other rules and regulations thereunder; provided that it shall exclude a person that is otherwise a municipal advisor solely based on activities within the meaning of Section 15B(e)(4)(A)(ii) of the Act and rules and regulations thereunder or any solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Act and rules and regulations thereunder.

See Proposed Rule G-42(f)(iv).

26 "Municipal advisory activities" would mean those activities that would cause a person to be a municipal advisor as defined in subsection (f)(iv) (definition of "municipal advisor") of Proposed Rule G-42. See Proposed Rule G-42(f)(v).

27 "Municipal entity" would "have the same meaning as in Section 15B(e)(8) of the Act, 17 CFR 240.15Ba1-1(g) and other rules and regulations thereunder." See Proposed Rule G-42(f)(vii).

28 "Obligated person" would "have the same meaning as in Section 15B(e)(10) of the Act, 17 CFR 240.15Ba1-1(k) and other rules and regulations thereunder." See Proposed Rule G-42(f)(viii).

Fund Securities

The regulation of municipal advisors, as the SEC has recognized,[29] is relevant to municipal fund securities.[30] Paragraph .12 of the Supplementary Material emphasizes the proposed rule's application to municipal advisors whose municipal advisory clients are sponsors or trustees of municipal fund securities.

Proposed Amendments to Rule G-8

The proposed amendments to Rule G-8 would require each municipal advisor to make and keep any document created by the municipal advisor that was material to its review of a recommendation by another party or that memorialize its basis for any conclusions as to suitability.

2. Statutory Basis

Section 15B(b)(2) of the Exchange Act[31] provides that:

> The Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

Section 15B(b)(2)(C) of the Exchange Act[32] provides that the MSRB's rules shall:

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29 See SEC Final Rule, 78 FR at 67472-3.

30 "Municipal fund security" is defined in MSRB Rule D-12 to mean "a municipal security issued by an issuer that, but for the application of Section 2(b) of the Investment Company Act of 1940, would constitute an investment company within the meaning of Section 3 of the Investment Company Act of 1940." The term refers to, among other things, interests in governmentally sponsored 529 college savings plans and local government investment pools.

31 15 U.S.C. 78o-4(b)(2).

> be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

Section 15B(b)(2)(L)(i) of the Exchange Act[33] requires, with respect to municipal advisors, the Board to adopt rules to prescribe means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients.

The MSRB believes that, the proposed rule change is consistent with Sections 15B(b)(2),[34] 15B(b)(2)(C)[35] and 15B(b)(2)(L)(i)[36] of the Exchange Act because it will enhance the protections afforded to municipal bond issuers and investors by providing guidance to municipal advisors that is designed to promote compliance with the standards of conduct, requirements and intent of the Dodd-Frank Act.

In this regard, neither the Dodd-Frank Act nor the recently-adopted SEC Final Rule prescribe the duties and obligations of municipal advisors beyond a general statement that municipal advisors shall be deemed to have a fiduciary duty to any municipal entity for whom

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[32] 15 U.S.C. 78o-4(b)(2)(C).

[33] 15 U.S.C. 78o-4(b)(2)(L)(i).

[34] 15 U.S.C. 78o-4(b)(2).

[35] 15 U.S.C. 78o-4(b)(2)(C).

[36] 15 U.S.C. 78o-4(b)(2)(L)(i).

the municipal advisor acts as a municipal advisor. Adoption of Proposed Rule G-42 will fulfill the need for regulatory guidance with respect to the standards of conduct and duties of municipal advisors and the prevention of breaches of a municipal advisor's fiduciary duty to its municipal entity clients. Proposed Rule G-42 also will establish standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for obligated persons and provide guidance to these municipal advisors as to what conduct would satisfy these duties and obligations.

The MSRB believes that by articulating specific standards of conduct and duties for municipal advisors, Proposed Rule G-42 will assist municipal advisors in complying with the statutorily-imposed requirements of the Dodd-Frank Act, and help prevent failures to meet those requirements. The proposed rule change will aid municipal entities and obligated persons that choose to engage municipal advisors in connection with their issuances of municipal securities as well as transactions in municipal financial products by promoting higher ethical and professional standards of such municipal advisors. The MSRB also believes that articulating standards of conduct and duties of municipal advisors will enhance the ability of the MSRB and other regulators to oversee the conduct of municipal advisors, as contemplated by the Dodd-Frank Act.

The MSRB believes the proposed rule change will enhance municipal entity and obligated person protections by ensuring that these entities have access to sufficient information to make meaningful choices, based on the merits of the municipal advisor, when considering engaging a municipal advisor by requiring municipal advisors to provide detailed disclosures of material conflicts of interest and certain other information prior to or upon the establishment of the municipal advisory relationship. As a result, municipal advisor clients will be able to evaluate municipal advisors on this objective set of information. These protections will also be enhanced

as a result of the proposed rule change's guidance for municipal advisors that could assist advisors in complying with, or help prevent breaches of, their fiduciary duty and duty of care, as well as other applicable obligations such as the duty of fair dealing (which is owed under MSRB Rule G-17 by all municipal advisors to all persons). To the extent that this guidance, provided in the supplementary material in the proposed rule change, would increase the likelihood of compliance by municipal advisors, municipal entities and obligated persons will benefit. Investors in municipal bond offerings will also benefit from the proposed rule change to the extent that a municipal entity or obligated person issuing bonds that uses a municipal advisor is more likely to receive services that reflect a higher ethical and professional standard than otherwise would be the case.

The proposed rule change would also, to some extent, prescribe means for municipal advisors to help prevent breaches of these duties, which would include, among others: requirements for the information that must be included in the documentation of the municipal advisory relationship; specified activities (such as certain principal transactions) that would be explicitly prohibited; and disclosure requirements that must accompany a municipal advisor's recommendation regarding a municipal security or a municipal financial product.

Section 15B(b)(2)(L)(iv) of the Exchange Act[37] requires that rules adopted by the Board:

> not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2)(L)(iv) of the Exchange Act[38] because the proposed rule change would impose on all

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[37] 15 U.S.C. 78o-4(b)(2)(L)(iv).

municipal advisors, including small municipal advisors, only the necessary and appropriate regulatory burdens needed to promote compliance with the proposed rule change. To accomplish this, Proposed Rule G-42 would use both a principles and prescriptive-based approach to establish the core standards of conduct in order to, among other things, accommodate the diversity of the municipal advisor population, including small municipal advisors and sole proprietorships, and to provide uniform protections to its clients, investors and the public.

The MSRB recognizes that municipal advisors would incur costs to meet the standards of conduct and duties contained in the proposed rule changes. These costs also could include additional compliance and recordkeeping costs. To ensure compliance with the disclosure obligations of the proposed rule change, municipal advisors could incur costs by seeking advice from legal and compliance professionals when preparing disclosures to clients. However, the MSRB believes that some of these costs are accounted for in the SEC Final Rule which requires disclosure of at least some similar information, such as the disclosure of disciplinary events. Proposed Rule G-42 could also impose additional costs on municipal advisors by requiring the disclosure of additional information directly to clients, some of which must already be submitted to the SEC on SEC Forms MA[39] and MA-I.[40] The MSRB has considered these costs and that there could be some instances of duplicative disclosure, but believes that the overlap in disclosure requirements between the SEC and MSRB will be minimal and that the disclosure requirements of the proposed rule are important elements of Proposed Rule G-42 that protect municipal advisor clients and foster transparency in the municipal advisory marketplace.

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38 15 U.S.C. 78o-4(b)(2)(L)(iv).

39 17 CFR 249.1300.

40 17 CFR 249.1310.

As to the potential costs associated with additional recordkeeping requirements, the SEC recognized in its economic analysis[41] of its recordkeeping requirements that municipal advisors should already be maintaining books and records as part of their day-to-day operations. In addition, municipal advisors who are also registered as broker-dealers or investment advisers are currently subject to the recordkeeping requirements of those regulatory frameworks. Against this back-drop, the MSRB believes that the costs associated with the few additional recordkeeping requirements associated with Proposed Rule G-42 will not be significant.

The MSRB believes that any increase in municipal advisory fees attributable to the additional costs of the proposed rule change will be minimal and that at least the element of fixed costs per municipal advisory firm will be spread across the number of advisory engagements for each firm. The MSRB recognizes, however, that for smaller municipal advisors with fewer clients, the cost of compliance with the proposed rule change's standards of conduct and duties could represent a greater percentage of annual revenues, and, thus, such advisors could be more likely to pass those costs along to their advisory clients.

The MSRB also recognizes that, as a result of these costs, some municipal advisors could decide to exit the market, curtail their activities, consolidate with other firms, or pass the costs on to municipal entities and obligated persons in the form of higher fees. The MSRB believes, however, that by articulating the core standard of conduct and duties and obligations of municipal advisors and by prescribing means that would prevent breaches of these duties, the proposed rule change will reduce possible confusion and uncertainty about what is required in order to comply with relevant provisions of the Dodd-Frank Act. Therefore, the proposed rule

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41 See SEC Final Rule, 78 FR at 67619.

change likely will reduce certain costs of compliance that might have otherwise been incurred by allowing municipal advisors to more quickly and accurately determine compliance requirements.

The MSRB also believes that the proposed rule change is consistent with Section 15B(b)(2)(G) of the Exchange Act,[42] which provides that the MSRB's rules shall:

> prescribe records to be made and kept by municipal securities brokers, municipal securities dealers, and municipal advisors and the periods for which such records shall be preserved.

The proposed rule change would require, under the proposed amendments to Rule G-8, that a municipal advisor make and keep records of any document created by the municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any conclusions as to suitability. The MSRB believes that the proposed amendments to Rule G-8 related to recordkeeping (with the ensuing application of existing Rule G-9 on records preservation) would promote compliance and facilitate enforcement of Proposed Rule G-42, other MSRB rules, and other applicable securities laws and regulations.

B. Self-Regulatory Organization's Statement on Burden on Competition

Section 15B(b)(2)(C)[43] of the Exchange Act requires that MSRB rules not be designed to impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. In addition, Section 15B(b)(2)(L)(iv)[44] of the Exchange Act provides that MSRB rules may not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

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42 15 U.S.C. 78o-4(b)(2)(G).

43 15 U.S.C. 78o-4(b)(2)(C).

44 15 U.S.C. 78o-4(b)(2)(L)(iv).

In determining whether these standards have been met, the MSRB was guided by the Board's Policy on the Use of Economic Analysis in MSRB Rulemaking.[45] In accordance with this policy, the Board evaluated the potential impacts of the proposed rule, including in comparison to reasonable alternative regulatory approaches, relative to the baseline that, inter alia, deemed municipal advisors to owe a fiduciary duty to their municipal entity clients and established a registration requirement. Based on this evaluation, the MSRB does not believe that the proposed rule change would impose any additional burdens on competition that are not necessary or appropriate in furtherance of the purposes of the Exchange Act.

The proposed rule may also provide a range of benefits to municipal entities, investors and municipal advisors. Municipal entities and obligated persons will have access to more information about municipal advisors and can make better, more informed choices with lower search costs. The availability of additional, objective information and the fostering of merit-based competition among municipal advisors should lead to enhanced issuer protections and improved outcomes. These improvements likely would enhance investor confidence in the integrity of the market. Moreover, the MSRB believes that the proposed rule change will provide a benefit to municipal advisors who could otherwise face greater uncertainty about the standards of conduct and duties required to meet certain of the requirements of the Dodd-Frank Act.

The MSRB considered whether costs associated with the proposed rule change, relative to the baseline, could affect the competitive landscape by leading some municipal advisors to exit the market, curtail their activities, consolidate with other firms, or pass costs on to municipal entity and obligated person clients in the form of higher fees. In addition, the MSRB considered

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45 Policy on the Use of Economic Analysis in MSRB Rulemaking, available at http://www.msrb.org/About-MSRB/Financial-and-Other-Information/Financial-Policies/Economic-Analysis-Policy.aspx.

whether the costs associated with the proposed rule, relative to the baseline, could create barriers to entry for firms wishing to offer to engage in municipal advisory activities.

The MSRB recognizes that some municipal advisors may exit the market as a result of the costs associated with the proposed rule relative to the baseline. However, the MSRB believes municipal advisors may exit the market for a number of reasons other than costs associated with the proposed rule. The MSRB also recognizes that some municipal advisors may consolidate with other municipal advisors in order to benefit from economies of scale (e.g., by leveraging existing compliance resources of a larger firm) rather than to incur separately the costs associated with the proposed rule. Finally, the MSRB acknowledges that some potential market entrants may be discouraged from entering the market because of costs or because the requirement to disclose information such as disciplinary events might make attracting business more difficult.

It is also possible that competition for municipal advisory activities may be affected by whether incremental costs associated with requirements of the proposed rule are passed on to advisory clients. The amount of costs passed on may be influenced by the size of the municipal advisory firm. For smaller municipal advisors with fewer clients, the incremental costs associated with the requirements of the proposed rule may represent a greater percentage of annual revenues, and, thus, such advisors may be more likely to pass those costs along to their advisory clients. As a result, the competitive landscape may be altered by the potentially impaired ability of smaller firms to compete for advisory clients.

In addition to the factors noted above that may affect smaller advisory firms, the MSRB understands that some small municipal advisors and sole proprietors may not employ full-time compliance staff and that the cost of ensuring compliance with the requirements of the proposed rule may be proportionally higher for these smaller firms.

The MSRB believes these costs represent only those necessary to achieve the purposes of the Exchange Act. Relative to draft Rule G-42 as initially published for comment,[46] the MSRB has made efforts to minimize costs that could affect the competitive landscape including, narrowing the scope of the conflicts that must be disclosed, specifying a less burdensome method for disclosing conflicts and disciplinary actions and documenting the municipal advisory relationship, clarifying the obligations owed by municipal advisors to obligated persons, and removing a number of other previously considered requirements.

Further, while exit, consolidation, or a reduced number of new market entrants may lead to a reduced pool of municipal advisors, the SEC concluded in the SEC Final Rule (on the permanent registration of municipal advisors) that the market would be likely to remain competitive despite the potential exit of some municipal advisors (including small entity municipal advisors), consolidation of municipal advisors, or lack of new entrants into the market.[47]

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The MSRB solicited comment on the proposed rule change in the First Request for Comment, requesting comment on a draft of Rule G-42 and draft amendments to Rules G-8 and

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46 The MSRB sought comment on the initial draft Rule G-42 ("Initial Draft Rule") and draft amendments to Rules G-8 and G-9 in MSRB Notice 2014-01 (Jan. 9, 2014) ("First Request for Comment").

47 See SEC Final Rule, 78 FR at 67608.

G-9, and a second notice requesting comment on a revised draft of Rule G-42 and draft amendments to Rules G-8 and G-9.[48]

The MSRB received forty-six comment letters in response to the First Request for Comment,[49] and nineteen comment letters in response to the Second Request for Comment.[50] The comments are summarized below by topic and MSRB responses are provided. [51]

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48 See MSRB Notice 2014-12 (Jul. 23, 2014) ("Second Request for Comment"). The draft rule text published in the Second Request for Comment is hereinafter the "Revised Draft Rule."

49 Comments were received in response to the First Request for Comment from: Acacia Financial Group, Inc.: Letter from Kim M. Whelan, Co-President, dated March 10, 2014 ("Acacia"); American Bankers Association: Letter from Cristeena G. Naser, Vice President and Senior Counsel, dated March 4, 2014 ("ABA"); American Council of Engineering Companies: Letter from David A. Raymond, President and CEO, dated March 7, 2014 ("ACEC"); American Public Transportation Association: Letter from Michael P. Melaniphy, President and CEO, dated March 10, 2014 ("APTA"); Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated March 10, 2014 ("BDA"); Cape Cod Five Cents Savings Bank: Letter from Dorothy A. Savarese, President and Chief Executive Officer, dated March 10, 2014 ("Cape Cod Savings"); Chancellor Financial Associates: E-mail from William J. Caraway, President, dated January 14, 2014 ("Chancellor Financial"); Coastal Securities: Letter from Chris Melton, Executive Vice President, dated March 10, 2014 ("Coastal"); College Savings Foundation: Letter from Mary G. Morris, Chair, dated March 10, 2014 ("CSF"); College Savings Plans Network: Letter from Betty Everitt Lochner, Director, Guaranteed Education Tuition Program, dated March 10, 2014 ("CSPN"); Cooperman Associates: Letter from Joshua G. Cooperman dated March 10, 2014 ("Cooperman"); Erika Miller: E-mail dated February 4, 2015; FCS Group: Letter from Taree Bollinger, Vice President, dated March 17, 2014 ("FCS"); First River Advisory L.L.C.: Letter from Shelley J. Aronson, President, dated January 16, 2014 ("First River Advisory"); First Southwest Company: Letter from Hill A. Feinberg, Chairman and Chief Executive Officer, and Michael G. Bartolotta, Vice Chairman, dated March 7, 2014 ("First Southwest"); Frost Bank: Letter from William H. Sirakos, Senior Executive Vice President, dated March 10, 2014 ("Frost"); George K. Baum & Company: Letter from Guy E. Yandel, EVP and Head of Public Finance, Dana L. Bjornson, EVP, CFO and Chief Compliance Officer, and Andrew F. Sears, SVP and General Counsel, dated March 10, 2014 ("GKB"); Government Finance Officers Association: Letter from Dustin McDonald, Director, Federal Liaison Center, dated March 13, 2014 ("GFOA"); Government Investment Officers Association: Letter from Laura Glenn, President, et al., dated March 7, 2014 ("GIOA"); Investment Company Institute: Letter from Tamara K. Salmon, Senior Associate Counsel, dated March 4, 2014 ("ICI"); J.P. Morgan: Letter from Paul N.

Palmeri, Managing Director, dated March 10, 2014 ("JP Morgan"); Kutak Rock LLP: Letter from John J. Wagner dated March 10, 2014 ("Kutak"); Lamont Financial Services Corporation: Letter from Robert A. Lamb, President, dated March 10, 2014 ("Lamont"); Lewis Young Robertson & Burningham, Inc.: Letter from Laura D. Lewis, Principal, dated March 3, 2014 ("Lewis Young"); MSA Professional Services, Inc.: Letter from Gilbert A. Hantzsch, CEO, dated March 10, 2014 ("MSA"); National Association of Bond Lawyers: Letter from Allen K. Robertson, President, dated March 18, 2014 ("NABL"); National Association of Health and Educational Facilities Finance Authorities: Letter from Pamela Lenane, President, David J. Kates, Chapman and Cutler LLP, and Charles A. Samuels, Mintz Levin, dated March 10, 2014 ("NAHEFFA"); National Association of Independent Public Finance Advisors: Letter from Jeanine Rodgers Caruso, President, dated March 10, 2014 ("NAIPFA"); National Healthcare Capital LLC: Letter from Richard Plumstead, dated March 10, 2014; New York State Bar Association: Letter from Peter W. LaVigne, Chair of the Committee, dated March 12, 2014 ("NY State Bar"); Northland Securities, Inc.: Letter from John R. Fifield, Jr., Director of Public Finance/Senior Vice President, dated March 7, 2014 ("Northland"); Oppenheimer & Co. Inc.: E-mail from John Rodstrom dated March 10, 2014 ("Oppenheimer"); Parsons Brinckerhoff Advisory Services, Inc.: Letter from Mark E. Briggs, President, dated March 10, 2014 ("Parsons"); Piper Jaffray: Letter from Frank Fairman, Managing Director, Head of Public Finance Services, dated March 10, 2014 ("Piper Jaffray"); Public Financial Management, Inc.: Letter from John H. Bonow, Chief Executive Officer, dated March 10, 2014 ("PFM"); Public Resources Advisory Group: Letter from Thomas Huestis dated March 10, 2014 ("PRAG"); Raftelis Financial Consultants, Inc.: Letter from Lex Warmath dated March 10, 2014 ("Raftelis Financial"); Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated March 10, 2014 ("SIFMA"); Sutherland Asbill & Brennan LLP: Letter from Michael B. Koffler dated March 10, 2014 ("Sutherland"); Wells Fargo Advisors, LLC: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated March 10, 2014 ("Wells Fargo"); Winters & Co. Advisors, LLC: Letter from Christopher J. Winters dated March 10, 2014 ("Winters LLC"); WM Financial Strategies: Letter from Joy A. Howard, Principal, dated March 10, 2014 ("WM Financial"); Woodcock & Associates, Inc.: E-mail from Christopher Woodcock dated January 14, 2014 ("Woodcock"); Wulff, Hansen & Co. : Letter from Chris Charles, President, dated March 17, 2014 ("Wulff Hansen"); Yuba Group: Letter from Linda Fan, Managing Partner, dated March 7, 2014 ("Yuba"); Zion's First National Bank: Letter from W. David Hemingway, Executive Vice President, dated March 10, 2014 ("Zion").

[50] Comments were received in response to the Second Request for Comment from: ABA: Letter from Cristeena Naser, Vice President, Center for Securities, Trust & Investments, dated August 25, 2014; ACEC: Letter from David A. Raymond, President and CEO, dated August 25, 2014; BDA: Letter from Michael Nicholas, Chief Executive Officer, dated August 25, 2014; Columbia Capital Management, LLC: Letter from Jeff White, Principal, dated August 25, 2014 ("Columbia Capital"); Dave A. Sanchez: Letter dated August 25, 2014 ("Sanchez"); Financial Services Roundtable: Letter from Richard Foster, Vice President and Senior Counsel for Regulatory and Legal Affairs, dated

Standards of Conduct

Under Proposed Rule G-42(a), a municipal advisor would be subject to a duty of care as to its obligated person clients under subsection (a)(i) and a fiduciary duty as to its municipal entity clients under subsection (a)(ii) when engaging in municipal advisory activities for such clients. Several commenters raised concerns relating to the proposed standards of conduct that would apply to municipal advisors.

Scope of the Fiduciary Relationship

In the First Request for Comment, the MSRB proposed that a municipal advisor be subject to a fiduciary duty when engaging in municipal advisory activities for municipal entity clients. Subsequently, in the Second Request for Comment, the MSRB asked whether the Revised Draft Rule should uniformly apply the proposed fiduciary standard to a municipal advisor in its relationships with all of its clients, including obligated persons. A number of

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August 25, 2014 ("FSR"); Florida Division of Bond Finance: Letter from J. Ben Watkins III, Director, dated August 22, 2014 ("FLA DBF"); GFOA: Letter from Dustin McDonald, Director, Federal Liaison Center, dated September 2, 2014; ICI: Letter from Tamara K. Salmon, Senior Associate Counsel, dated August 19, 2014; Mr. Bart Leary: E-mail dated July 23, 2014 ("Leary"); Lewis Young: Letter from Laura D. Lewis, Principal, dated August 25, 2014; NAIPFA: Letter from Jeanine Rodgers Caruso, President, dated August 25, 2014; New York State Bar: Letter from Peter W. LaVigne, Chair of the Committee, dated August 27, 2014; Piper Jaffray: Letter from Frank Fairman, Managing Director, Head of Public Finance Services, dated August 25, 2014; SIFMA: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated August 25, 2014; Southern Municipal Advisors, Inc.: Letter from Michael C. Cawley, Senior Consultant, dated August 25, 2014 ("SMA"); Wells Fargo: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated August 25, 2014; WM Financial: Letter from Joy A. Howard, Principal, dated August 25, 2014; and Zion: Letter from W. David Hemingway, Executive Vice President, dated August 25, 2014.

[51] The draft rule text included in the First Request for Comment is referred to herein as the "Initial Draft Rule;" the draft rule text included in the Second Request for Comment is referred to herein as the "Revised Draft Rule."

commenters opposed extending the application of the fiduciary standard to municipal advisors in connection with their obligated person clients.[52]

The MSRB believes that the application of the fiduciary standard is appropriately limited to municipal advisors when engaging in municipal advisory activities for or on behalf of municipal entity clients and strikes the appropriate balance. Proposed Rule G-42 establishes a minimum standard, which, as noted by NABL, does not limit an obligated person client and its municipal advisor from agreeing to a higher standard of conduct, or incorporating other requirements or protections in the municipal advisory relationship.

Scope of the Duty/529 Plans

Proposed paragraph .01 of the Supplementary Material provides that a municipal advisor acting in accordance with the duty of care must undertake reasonable investigation to determine that it is not basing any recommendation made to a client on materially inaccurate or incomplete information. In response to the First and Second Request for Comment, ICI stated that municipal advisors to 529 college savings plans ("529 plans") should not be required to verify the veracity or completeness of the information provided to the municipal advisor by authorized state employees or officials who are authorized to act on behalf of the 529 plan. ICI requested that paragraph .01 of the Supplementary Material be revised not to require municipal advisors to investigate whether information is materially inaccurate or incomplete when it is provided to the municipal advisor by persons who are authorized by the client to act on behalf of a state's 529 plan.

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[52] See, e.g., comment letters from: ABA, BDA, Cape Cod Savings, Cooperman, GKB, Kutak, Lewis Young, NABL, NAHEFFA, Parsons, Piper Jaffray and SIFMA. A few commenters, including First River Advisory, NAIPFA and Yuba, supported the application of a fiduciary duty to a municipal advisor when engaging in municipal advisory activities on behalf of an obligated person client.

Neither the First Request for Comment nor the Second Request for Comment contemplated that municipal advisors in municipal advisory relationships with 529 plans would be exempted or excluded, in whole or in part, from the proposed core standards of conduct, including aspects of the duty of care that a municipal advisor owes to a client. The MSRB believes that exempting municipal advisors from the proposed core standards of conduct would reduce the protections that Congress through the Dodd-Frank Act intended to provide to municipal entity clients and investors in 529 plan securities.

Fiduciary Duty – Authority

In response to the Second Request for Comment, Sanchez commented that the MSRB lacks the statutory authority to define "fiduciary duty" or to prescribe means designed to effectuate the performance of that duty.

As discussed above, the Exchange Act grants the MSRB statutory authority to adopt rules with respect to municipal advisors engaging in municipal advisory activities that are designed to, among other things, prevent fraudulent and manipulative acts and practices, and acts, practices or courses of business that are not consistent with a municipal advisor's fiduciary duty to its clients.[53] Accordingly, the MSRB has concluded that it is properly exercising the authority granted to it by statute.

Fiduciary Duty – Standards

In response to the First Request for Comment, NABL stated that the Initial Draft Rule should draw on established common law and similar standards that NABL believes are intended to provide substantive guidance regarding fiduciary duties (e.g., the standards applicable to attorneys), rather than the standards applicable to broker-dealers or registered investment

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[53] See, e.g., 15 U.S.C. 78o-4(b)(2)(C); and 15 U.S.C. 78o-4(b)(2)(L)(i).

advisers. NABL argued that the attorney-client relationship is more comparable to the municipal advisor-client relationship because both can have a wide spectrum of scopes of responsibilities, similar contexts in which there are interactions with the client, and a longer duration over which the representation occurs. BDA similarly believed that the fiduciary standards set forth in the Initial Draft Rule would not operate like other well-established standards, such as those for attorneys, and that the MSRB did not justify why the standards for municipal advisors would deviate from those standards as outlined in the Model Rules of Professional Conduct for attorneys ("Model Rules"). Accordingly, BDA suggested that Proposed Rule G-42 should adopt or parallel the same fiduciary duty standards used by other similarly situated professionals.

In developing Proposed Rule G-42, the MSRB consulted various codes of conduct and sources of federal and state law regarding the duties and obligations of a fiduciary that apply to professionals who are, or, in certain relationships, may be, fiduciaries. Some provisions of the proposed rule reflect principles incorporated from MSRB Rule G-17, including the duties of dealers to issuers, while other provisions were based on principles and requirements in the Investment Advisers Act. The MSRB believes the Investment Advisers Act is particularly relevant in developing a rule regarding fiduciary duties and obligations, and notes that the SEC also considered the Investment Advisers Act informative as it developed the SEC Final Rule.[54] Moreover, the MSRB believes it is important to establish rules and standards that address the practices of various types of municipal advisors and their clients, and that the provisions addressing the duties and obligations of a fiduciary are tailored to address the unique characteristics of the municipal securities market and the variety of responsibilities undertaken by municipal advisors in their relationships with municipal entity and obligated person clients.

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54 See generally, SEC Final Rule, 78 FR 67467.

The MSRB notes that, to the extent that Proposed Rule G-42 does not specifically prescribe or prohibit certain conduct, or address certain activity, common law regarding fiduciary obligations and duties may be referenced by a judicial or adjudicatory decision-maker.

Fiduciary Duty – Obligated Persons

A number of commenters raised concerns that Proposed Rule G-42 implicitly and inappropriately imposes fiduciary duty obligations on municipal advisors whose clients are obligated persons without a demonstrated need for a more robust regulatory framework than that adopted by Congress or the SEC.[55] Those commenters believed that the treatment accorded to obligated persons should be distinguished from that accorded to municipal entities because, as they stated, obligated person clients do not handle public funds, are private, domestic and international for-profit companies or not-for-profit businesses, and, therefore, operate with a different level of public accountability. Overall, these commenters believed that fiduciary duties should not be mandatorily extended to benefit obligated persons.

NAHEFFA suggested that the duty of care and the requirements of the Initial Draft Rule G-42(b)-(f) be revised to state that municipal advisors owe a fiduciary duty only to their municipal entity clients. In the alternative, NAHEFFA requested that the MSRB provide clarification on the legal and practical distinctions among the standards and duties and obligations of municipal advisors vis-à-vis both types of clients, including a clarification that an alleged violation of the duty of care would be subject to review under a negligence standard and an alleged violation of the duty of loyalty would require evidence of intent. Generally,

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55 See letters from: ABA, BDA, Cape Cod Savings, GKB, Kutak, Lewis Young, NABL, NAHEFFA, Parsons, Piper Jaffray, Sanchez and SIFMA. On the other hand, NAIPFA, First River Advisory and Yuba supported imposing fiduciary duties upon municipal advisors with respect to the advice they provide to obligated persons.

NAHEFFA supported either a revised Rule G-42, or a separate rule that would simplify and reflect the duties and obligations of a municipal advisor with respect to its obligated person clients. NAHEFFA suggested that, as to obligated person clients, the duty should be to exercise professional judgment and expertise in providing services and to deal fairly with its clients. Similarly to NAHEFFA, BDA requested that the MSRB revise Proposed Rule G-42 to more clearly state and distinguish between the duties and obligations that municipal advisors would owe to each of the two types of clients.

ABA commented that the MSRB lacked the requisite authority to impose a fiduciary duty on municipal advisors with respect to their obligated person clients, and that even if it had the authority, such a standard would be unworkable since banks would have difficulty identifying which of their many customers were obligated persons. ABA stated that the extension of a fiduciary duty to municipal advisors in their relationship with their obligated person clients would result in a significant risk that banks would inadvertently violate regulatory requirements by becoming an unwitting municipal advisor with respect to a client they did not know was an obligated person. Moreover, the banks would run the corresponding risk of violating the attendant fiduciary duty applicable to such municipal advisor.

More specifically, Sanchez commented that the language in Revised Draft Rule G-42(b)(i)(A) and (b)(i)(G) appeared to import the duty of loyalty and duty of care into representations of obligated persons by using the phrase “unbiased and competent advice” with respect to advice provided to or on behalf of obligated persons. He suggested that these provisions be revised to say “impair its ability to render advice to or on behalf of the obligated person in accordance with the standards of conduct required in clause (a)” in lieu of the phrase referencing “unbiased and competent advice.”

Neither the Initial Draft Rule nor the Revised Draft Rule would deem municipal advisors to owe a fiduciary duty to obligated person clients, and the MSRB disagrees with the view that either the Initial or Revised Draft Rule implicitly and inappropriately imposed fiduciary duty obligations to such clients. After carefully considering the comments, the MSRB has not modified Proposed Rule G-42(a), on standards of conduct. Further, Proposed Rule G-42 follows the approach taken in the Dodd-Frank Act, deeming a municipal advisor to owe a fiduciary duty only to its municipal entity clients. However, although the Exchange Act fiduciary duty standard would not apply to a municipal advisor advising an obligated person client, all municipal advisors are subject to fair-dealing obligations under MSRB Rule G-17, which already requires a municipal advisor to deal fairly with all persons and prohibits engaging in any deceptive, dishonest or unfair practice. Moreover, the provisions in Proposed Rule G-42(b)-(f) appropriately establish the duties and obligations of municipal advisors. The MSRB notes that these duties are, in part, based on similar existing duties for other regulated entities (e.g., underwriters' duties to issuers), which are separate and apart from a fiduciary duty. Therefore, the MSRB does not believe Proposed Rule G-42 creates an implicit fiduciary duty for municipal advisors with respect to the advice they provide to obligated person clients.

The MSRB agrees with Sanchez's specific comments regarding paragraphs (b)(i)(A) and (b)(i)(G) of the Revised Draft Rule and has revised the proposed rule change to clearly differentiate between the handling of conflicts of interest under the duty of loyalty, as discussed in paragraph .02 of the Supplementary Material, and conflicts under the disclosure requirements that are applicable to all municipal advisory clients as part of a municipal advisor's duty of care, as discussed in paragraph .01 of the Supplementary Material. Specifically, under proposed subsection (a)(ii), the duty of loyalty in the proposed rule change, a municipal advisor must not

engage in municipal advisory activities with a municipal entity client if it cannot manage or mitigate its conflicts of interest in a manner that will permit it to act in the municipal entity's best interests. Conversely, under proposed section (c) of Proposed Rule G-42 and as discussed further with respect to proposed paragraph .05 of the Supplementary Material, a municipal advisor can continue to serve as a municipal advisor to its municipal entity or obligated person client when an actual or potential conflict of interest that could be reasonably anticipated to impair its ability to provide that advice exists, so long as such conflict of interest is disclosed and addressed in accordance with the relevant provisions of Proposed Rule G-42[56] and the municipal advisor can satisfy the applicable standards of conduct described in section (a).

NAHEFFA requested that the MSRB clarify the legal distinctions between the duty of care and duty of loyalty, and suggested that the state of mind standard to determine a violation of the duty of care should be negligence, and the state of mind standard regarding a violation of the duty of loyalty should be intent. In response to NAHEFFA's request for clarification regarding such standards, the MSRB believes it would be appropriate for the courts and other adjudicatory authorities to determine the "state-of-mind" elements when applying the standards of conduct of Proposed Rule G-42 to specific sets of facts and circumstances presented, drawing on existing jurisprudence regarding analogous duties of care and fiduciary obligations.

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56 Municipal advisors would be required to disclose and document such a material conflict of interest under Proposed Rule G-42(b) and (c) and paragraph .05 of the Supplementary Material. With respect to municipal entity clients, municipal advisors also would need to provide an explanation to the client of how the municipal advisor intends to manage or mitigate its conflict in a manner that will permit it to act in the municipal entity's best interests.

In response to ABA's comment, the MSRB again notes that determining which activities constitute municipal advisory activities requires a legal interpretation of the SEC Final Rule. Such authority is vested with the SEC rather than the MSRB.

Finally, the MSRB notes again that the standards of conduct in Proposed Rule G-42 would be minimum requirements, which the MSRB has developed to empower the client to a large extent to determine the scope of services and control the engagement with the municipal advisor, and as suggested by NABL, any municipal advisor and its client may agree to more stringent standards of conduct for their specific engagement.

Duty of Care – Supplementary Material .01

In response to the Second Request for Comment, WM Financial challenged the requirement that a municipal advisor "undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information." While WM Financial agreed that a municipal advisor should make a reasonable investigation in order to determine whether a recommendation is in a client's best interest, WM Financial believed that a municipal advisor should be able to rely on publicly-available documents as being true and accurate, and should be able to assume that any additional information provided to it by the municipal entity is also true and accurate. WM Financial believed that requiring the municipal advisor to verify the accuracy of the information it receives from a client imposes an inappropriate burden. As noted above, ICI similarly opposed the requirement in the context of 529 plans, for which the municipal advisor that is also acting as a plan sponsor would typically work with and rely upon state employees who are authorized to represent a state's plan and requested revisions to paragraph .01 of the Supplementary Material.

Proposed paragraph .01 of the Supplementary Material would provide, as a core general standard, that a municipal advisor must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. There is no exception for information that is provided to the advisor by the client. The MSRB believes that the provisions of proposed paragraph .01 of the Supplementary Material remain appropriate and, as discussed above, does not believe that advisors to 529 plans should be relieved from an obligation to inquire as to the accuracy of material that is relevant to a municipal advisor's recommendation provided by its client or other parties. The MSRB further believes this provision of proposed paragraph .01 of the Supplementary Material would provide an objective standard for when it is appropriate for a municipal advisor to rely on information provided by a client when making a recommendation to such client, including representatives of a 529 plan authorized to act on behalf of the plan. Finally, because proposed paragraph .01 would require municipal advisors to undertake only a "reasonable investigation" of the veracity of the information on which it is basing a recommendation, municipal advisors would not be required to go to the impractical lengths suggested by commenters. The MSRB believes this standard would be sufficient to allow municipal advisors to assess their risk exposure to any reliance on that information and determine what potential mitigating actions need to be taken.

Sanchez also commented that the MSRB should "consider whether the information for which 'a municipal advisor must have a reasonable basis for' incorporated in [subparagraphs] (a) through (c) [of paragraph .01 of the Supplementary Material] is not already addressed in the standards of conduct required of municipal advisors by MSRB Rule G-17 and general antifraud rules related to municipal securities disclosure." As such, he suggested deleting those provisions of paragraph .01 of the Supplementary Material to avoid unnecessarily duplicative regulatory

requirements. The MSRB has decided to retain those provisions because it believes they would provide additional guidance regarding the proposed duty of care and would assist municipal advisors in satisfying that duty without unnecessarily duplicating the principles of MSRB Rule G-17 or other federal securities anti-fraud statutes.

Finally, SIFMA noted that, while the requirement for a municipal advisor to make a reasonable inquiry -- regarding the facts that are relevant to a client's determination to pursue a particular course of action or that form the basis of any advice to the client -- could be appropriate in the context of arranging a municipal securities issuance, it could be cost prohibitive in the case of ordinary brokerage and related advice, given the number of trades potentially involved, timing considerations and the general context of broker-related advice. Therefore, SIFMA did not believe that such a standard should be applied in addition to otherwise applicable suitability requirements that would attach to recommendations made in the context of brokerage/securities execution services. The MSRB believes that the duties and standards in the proposed rule are appropriately applied to municipal advisory activities (other than the undertaking of a solicitation), and notes that a municipal advisor to a municipal entity client will owe a statutory fiduciary duty to the client. If the conduct SIFMA describes constitutes the giving of advice under the SEC rules providing for the registration of municipal advisors as discussed in the SEC Final Rule,[57] then Proposed Rule G-42 would apply in its entirety. Likewise, if such conduct did not constitute the giving of advice under those rules, then Proposed Rule G-42 would not apply.

Duty of Loyalty – Supplementary Material .02

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57 See generally, SEC Final Rule, 78 FR 67467.

In response to the First Request for Comment, ACEC and APTA indicated that they believed there are circumstances when the duty of loyalty could directly conflict with an engineer's professional and ethical responsibilities, and expressed concerns as to how such conflicts could affect engineering firms' business. Both ACEC and APTA specifically stated that, in the course of providing professional engineering services to a client, circumstances could arise in which the engineer would find himself or herself facing a conflict between breaching its fiduciary duty in its role as municipal advisor and violating the ethical obligations to which the engineer is subject under applicable state law and regulation, or one or more professional associations. According to ACEC, in such circumstances, it would be detrimental to the health, safety and welfare of the public to prioritize the fiduciary duty the engineer municipal advisor owed to its client. ACEC argued that paragraph .02 of the Supplementary Material, therefore, would not serve the public interest and requested that the MSRB address how this type of conflict could be managed.

The MSRB notes that SEC Rule 15Ba1-1(d)(2)(v) excludes engineers providing engineering advice from the definition of municipal advisor.[58] The MSRB further notes that the same and similar issues raised by the commenters in response to the First Request for comment also were raised with the SEC during its rulemaking to establish the registration regime for municipal advisors. In the SEC Final Rule, the SEC provided greater clarity to engineers concerning the definition of "municipal advisor" and the scope of the exclusion for engineers.[59] If, given that guidance, an engineer were in fact to engage in municipal advisory activities, it would be subject to the statutory fiduciary duty to a municipal entity client, and, in the MSRB's

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58 See 17 CFR 240.15Ba1-1(d)(2)(v). See also 15 U.S.C. 78o-4(e)(4)(C).

59 See SEC Final Rule, 78 FR at 67529-32.

view, appropriately subject to the duty of loyalty provisions in Proposed Rule G-42. Under certain circumstances, if a material conflict of interest would prevent the municipal advisor from being able to act in accordance with the standards of conduct of section (a) of Proposed Rule G-42, which the MSRB believes would be rare, the firm might need to determine not to provide municipal advice if it preferred to provide engineering services.

Disclosure of Conflicts of Interest

The MSRB received a number of comments regarding section (b) of Proposed Rule G-42 on required disclosures of material conflicts of interest by municipal advisors to their clients. Generally, commenters were supportive of, or did not express an objection to, requiring municipal advisors to provide written disclosure of material conflicts of interest. However, some commenters did express concerns about some of the facets of the disclosure requirements; those concerns are described below and followed by the MSRB's response.

Compensation Arrangements

Several commenters expressed concern regarding paragraph (b)(i)(F) of Proposed Rule G-42, which requires municipal advisors to disclose conflicts of interest arising from compensation arrangements that are contingent on the size or closing of any transaction as to which the municipal advisor is providing advice.

Commenting on the Initial Draft Rule, Lewis Young stated that contingent fee arrangements benefit clients, particularly smaller municipal entities, because they allow municipal entity clients to finance the costs of the municipal advisor with the proceeds of the issuance. In their view, characterizing a contingent fee arrangement as a conflict of interest requiring disclosure to the client amounted to advising a client that the municipal advisor may not be acting in the client's best interest. They added that they believe the disclosure requirement

would serve no useful purpose and could confuse clients. Sutherland stated that the Initial Draft Rule's required disclosure of contingent fee arrangements was duplicative of SEC Form MA[60] and, therefore, unnecessarily burdensome, and should be deleted.

Commenting on the Revised Draft Rule, Columbia Capital stated that the provision "creates the appearance that the MSRB takes the position that one fee modality is less preferable to all others." Columbia Capital, Cooperman and Piper Jaffray commented that the proposed rule change should not single out one fee arrangement as being preferable to others. Columbia Capital, Cooperman and Piper Jaffray also contended that fee arrangements of any sort (hourly, fixed or non-contingent) create an adversarial relationship between the municipal advisor and its client. In Piper Jaffray's view, the potential conflicts of interest that are inherent in all fee arrangements are also "generally knowable" to both sides of a transaction and, therefore, the Revised Draft Rule's disclosure requirement would not be beneficial. Columbia Capital suggested deleting the provision.

WM Financial also expressed concerns regarding paragraph (b)(i)(F) of the Revised Draft Rule, but differed in its reasoning from Columbia Capital and Piper Jaffray. WM Financial disagreed with the premise that all fee structures create some conflict of interest. Rather, WM Financial stated that, because municipal advisors would be required to "act in the best interest of their clients . . . good advice will prevent a fee arrangement from creating a 'conflict'." In their view, a "conflict of interest does not exist when payment of fees is based on the success of services to be provided . . . ." Like Lewis Young, WM Financial stated that contingent fees serve a valuable function because they allow small municipal entity clients to finance the cost of the municipal advisor with the proceeds from the issuance and ensure that the cost of the municipal

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60 See SEC Form MA, Items 4.H. - 4.J.

advisor is only incurred after the successful completion of the issuance. WM Financial also requested that paragraph (b)(i)(F) be deleted.

The MSRB has considered the arguments and alternatives advanced by commenters and determined that requiring the disclosure of conflicts of interest arising from fee arrangements contingent on the size or closing of the transaction as to which the municipal advisor is providing advice is an appropriate and necessary measure to alert municipal entity and obligated person clients to the potential conflict of interest inherent in such fee arrangements. While the MSRB recognizes, as some commenters pointed out, that other fee arrangements (such as hourly, fixed or otherwise non-contingent) might also give rise to conflicts, the MSRB believes that the potential harm to a client may be particularly acute if a client is not informed of a conflict of interest arising from a contingent fee arrangement. Furthermore, the MSRB does not agree with commenters that have argued that requiring a conflict of interest disclosure would suggest that the municipal advisor is not acting in the best interest of its client. The purpose of the disclosure requirement in proposed paragraph (b)(i)(F) simply would be to allow a municipal advisor's client to make an informed decision based on relevant facts and circumstances. Also, under the proposed rule change, municipal advisors would have the opportunity to provide a client with additional context about the benefits and drawbacks of other fee arrangements in relation to a contingent fee arrangement so that the client could choose a fee arrangement that serves its needs.

Disclosure of Conflicts of Interest to Investors

The MSRB received comments that called for the deletion of a provision set forth previously in the Revised Draft Rule as paragraph .08 of the Supplementary Material. Under the provision, if all or a portion of a document prepared by a municipal advisor or any of its affiliates

were included in an official statement for an issue of municipal securities by or on behalf of a client of the municipal advisor, the municipal advisor would have been required to provide written disclosure to investors of any affiliation that would be a material conflict of interest under paragraph (b)(i)(B) of the Revised Draft Rule. The disclosure requirement also could have been satisfied if the relevant affiliate provided the written disclosure to investors.[61]

SIFMA supported deleting the disclosure requirement, noting that "[m]unicipal advisors and their affiliates may have no contractual or other relationships (and in many cases have no form of privity) with investors, nor do they control the content of the Official Statement." SIFMA stated that it is the obligation of the issuer "to make sure that its disclosure is materially accurate and complete" and the responsibility of broker-dealers to comply with their obligations under applicable law. SIFMA observed that the municipal advisor is already required to provide the issuer with the same conflict disclosure under paragraph (b)(i)(B), arguing that the MSRB should leave the decision of whether to include such information in material distributed to investors to the issuer.

ICI and NABL also commented in favor of deleting the requirement. ICI provided comments similar to SIFMA's comments in response to both the Initial and Revised Draft Rules, but focused on how the required disclosure to investors would impact municipal advisors advising 529 plans. ICI supported requiring municipal advisors to disclose conflicts of interest to the municipal advisor's client but questioned why such information would be relevant to a person investing in 529 plan securities. ICI stated that if "all material terms and conditions of the

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[61] Paragraph (b)(i)(B) of the Revised Draft Rule required written disclosure of "any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor."

529 plan offering already are disclosed in the offering document that is provided to investors and potential investors, this supplemental disclosure would not provide any additional protection to investors." In response to the First Request for Comment, NABL contended that requiring these disclosures would run contrary to the intent of the Dodd-Frank Act, which is to protect issuers. NABL suggested, as an alternative, that issuers be allowed to choose whether to disclose the conflicts of interest to investors.

The MSRB agrees with the commenters and notes that the provision could put municipal advisors in the impractical position of being required to make conflict of interest disclosures directly to investors or include the content of such disclosures in an issuer's official statement, although the municipal advisor may not have the authority or the means to do so. Moreover, because the proposed rule change would already require the municipal advisor to disclose all material conflicts of interest to the issuer, the MSRB believes the issuer will be well positioned to make the determination of whether to include such information in the official statement or other investor disclosure documents, consistent with the issuer's duties under all applicable law. In light of the comments and after a re-evaluation of the purpose and feasibility of the disclosure provision in the supplementary material as described above, the MSRB has deleted the provision.

Acknowledgment or Consent to Conflicts of Interest Disclosure

In response to the First Request for Comment, several commenters suggested differing approaches to the question of whether municipal advisors should be required to obtain some form of acknowledgment from their client of the conflicts of interest disclosures that municipal advisors are required to make under the proposed rule change.

In response to the First Request for Comment, NABL commented that the MSRB should follow the approach taken in the Model Rules of Conduct of the American Bar Association

regarding the disclosure of conflicts of interest as stated in the Initial Draft Rule. NABL argued that municipal advisors should be required to obtain "informed consent, confirmed in writing" to each potentially waivable material conflict of interest. NABL stated that this standard is as appropriate for municipal advisors as it is for common law fiduciaries or attorneys. NABL suggested that the "informed consent" it advocated could be accomplished in several ways, including "a writing evidencing an engagement, including a letter of intent, after disclosure to the client sufficient to establish informed consent." NABL contended that informed written consent from a municipal advisor's client is "a necessary corollary to the requirement that an advisor disclose and provide sufficient detail about the nature of all material conflicts of interest." NABL also noted that informed consent confirmed in writing would be consistent with the requirements of the CFTC for commodity trading advisors. NAIPFA stated that it believed municipal advisors should be required to obtain an acknowledgment from their clients of the conflicts of interest that it has disclosed, saying that this would conform to the obligations of underwriters and other "professionals possessing fiduciary duties." GFOA provided similar support for requiring an acknowledgment of the conflicts of interest disclosures from the municipal advisor's client but stated that, if such a requirement was added to the proposed rule change it would expect an explanation within the proposed rule change detailing how the acknowledgements of such conflicts relate to a municipal advisor's fiduciary duty.

In contrast to NABL, NAIPFA and GFOA, commenters including Cooperman, Lewis Young and Acacia commented that municipal advisors should not be required to obtain a written acknowledgment of disclosures before proceeding with the engagement. Cooperman stated that acknowledgement of conflicts of interest disclosures from municipal entity clients is an unnecessary and unjustified requirement that should be removed. Lewis Young stated that such

written disclosure should not be required "so long as the disclosures provided are not objected to by the client." Proposing a somewhat different approach, Acacia stated that municipal advisors should not be required to obtain a written acknowledgement of the conflicts disclosed but should be required to (i) provide such information (and record such provision), (ii) request receipt and consent but (iii) be permitted to proceed with a municipal advisory engagement in the absence of such receipt and consent if the municipal advisor has a reasonable belief that such information has been received. Acacia reasoned that its approach would be analogous to existing MSRB guidance for underwriters under MSRB Rule G-17.

The proposed rule change would not require a municipal advisor to obtain written acknowledgement from its client of the disclosure of conflicts of interest. While the MSRB understands the concerns expressed by commenters, the MSRB believes that the proposed rule change sufficiently obligates municipal advisors to ensure that their clients receive proper notice of material conflicts of interest. Proposed paragraph .05 of the Supplementary Material, for instance, would require municipal advisors to provide information sufficiently detailed to inform a client of the nature, implications and potential consequences of each conflict, and include an explanation of how the municipal advisor addresses or intends to manage or mitigate each conflict. Such disclosure would allow a municipal advisor's client to make an informed decision as to whether such conflicts can be adequately managed or mitigated. Furthermore, a municipal advisor's duty of care would require an advisor to have a reasonable basis for believing that its client received the disclosure and understood the nature, implications and potential consequences of the conflicts of interest that the municipal advisor disclosed. Further, the MSRB believes that obtaining some form of written acknowledgement from municipal entities and obligated persons

would prove to be a significant procedural burden to both municipal advisors and their clients that would likely not result in a substantiated benefit.

Explanation of Mitigating Conflicts of Interest

As discussed above, proposed paragraph .05 of the Supplementary Material to Proposed Rule G-42, on conflicts of interest, would require a municipal advisor to include an explanation of how the municipal advisor would address, or manage or mitigate, the material conflicts of interest that it has disclosed to its client. In response to the Second Request for Comment, Sanchez challenged the value and purpose of this requirement by opining that municipal securities brokers and dealers are not subjected to the burden of making such disclosures. Sanchez requested that the MSRB revise the proposed rule change to require such disclosures only if requested by the client.

The MSRB has considered Sanchez's comments and determined not to amend proposed paragraph .05 of the Supplementary Material because the MSRB believes that the provision would serve a beneficial and protective function for clients. The municipal advisor's explanation would allow its client to adequately assess the potential effects the conflicts of interest could have on an engagement with the municipal advisor and to determine whether the actions the municipal advisor proposes to take to mitigate the conflicts of interest are sufficient and will not overly impair the quality and neutrality of the services to be performed by the municipal advisor.

Services for Conduit Issuers and Obligated Person Clients

Under subsection (e)(ii) of Proposed Rule G-42, a municipal advisor would be precluded from serving its municipal entity client as underwriter for a transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice to the municipal entity.

In response to the Second Request for Comment, BDA commented that the proposed rule should explicitly allow a dealer/municipal advisor to serve as an underwriter for a conduit issuer and as a municipal advisor for the conduit borrower, even with respect to directly related matters.

Underwriting such a transaction would not be specifically prohibited by the ban on principal transactions in subsection (e)(ii) of Proposed Rule G-42, because it applies only in cases of municipal entity clients. A conduit borrower is typically not a municipal entity. Thus, depending on the specific facts and circumstances, this scenario could be permissible with appropriate disclosure and consent. Still, it is not clear that, even with disclosure and consent, such activity would be categorically consistent with all of the duties of a municipal advisor to an obligated person in all circumstances. Therefore, the MSRB has not amended the proposed rule as suggested by BDA.

Material Conflicts of Interest Required to be Disclosed

Section (b) of Proposed Rule G-42 would include a non-exhaustive list of matters that would always constitute material conflicts of interest and that would be required to be disclosed by municipal advisors under the proposed rule change. Matters that must be disclosed as material conflicts of interest under section (b) include, among others: any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client; any payments made by the municipal advisor, directly or indirectly, to obtain or retain an engagement to perform municipal advisory activities for the client; any conflicts of interest arising from compensation for municipal advisory activities to be performed that is contingent on the size or closing of any transaction as to which the municipal advisor is providing advice; and any legal or disciplinary event that is material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel.

In response to the First Request for Comment, Lewis Young stated that the proposed rule should only require disclosure when an actual conflict of interest exists because providing tailored explanations of potential or hypothetical situations would be "expensive, time consuming, and not very helpful." The MSRB disagrees and believes that the likely benefits from these disclosures will outweigh the cost associated with providing them to a municipal advisor's clients because the proposed rule change limits the required disclosure to only material conflicts of interest, both actual and potential, of which a municipal advisor is aware of after a reasonable inquiry. The MSRB also believes that requiring a municipal advisor to disclose conflicts of interest, actual and potential, that the municipal advisor becomes aware of after reasonable inquiry and that could reasonably be anticipated to impair the municipal advisor's ability to provide advice in accordance with the standards of conduct in section (a) of the rule, is necessary to provide clients with the requisite information to make an informed decision regarding the selection of their municipal advisor.

ICI suggested adding prefatory language to section (b) that would clarify that a municipal advisor would be required to disclose only conflicts of interest that are applicable to its relationship with the specific client. ICI stated that adding such language would harmonize section (b) with the approach taken in the Investment Advisers Act regarding the delivery of brochures,[62] which it believed permits an investment adviser to omit "inapplicable information" from a disclosure it is required to provide to clients. The MSRB believes that Proposed Rule G-42 makes clear that municipal advisors are required only to make disclosure of material conflicts of interest and that this would exclude inapplicable information.

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62 See 17 CFR 275.204-3.

First Southwest expressed concern regarding the requirement of subsection (b)(i) that municipal advisors must provide written notice when they have no material conflicts of interest to disclose to their clients. First Southwest stated that the requirement would increase administrative requirements and provide little, if any, benefit in the event a conflict of interest were later discovered. The MSRB disagrees and believes that an affirmative written statement by the municipal advisor that it has no known material conflicts of interest would remove potential ambiguities about the completeness of the conflicts disclosure.

Sutherland commented that the conflicts of interest required to be disclosed would be duplicative of information that could be found in SEC Forms MA and MA-I and, therefore, would be unnecessary. As an example, Sutherland stated that SEC Form MA requires the disclosure of affiliated business entities; compensation arrangements; and proprietary interests in municipal advisor client transactions.[63] While some overlap could exist, the MSRB believes that the SEC forms do not solicit all of the information that would be required by the proposed rule change and, thus, would not serve as a sufficient substitute. Specifically, the SEC forms would not be a viable proxy for disclosing potential conflicts of interest that the municipal advisor could have, nor would the forms contain an explanation of how they intend to mitigate the material conflicts of interest that they disclose. The MSRB expects that the written disclosure of material conflicts of interest will be a useful tool to municipal advisor clients that will allow them to readily assess the impact of actual or potential conflicts of interest of potential or ongoing municipal advisory activities.

In response to the Second Request for Comment, SIFMA requested clarification regarding the standard for determining the materiality of the conflicts of interest described in

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63 See SEC Form MA, Items 1.K., 4.H.-4.J. and 7.A.-7.F., respectively.

paragraphs (b)(i)(A) and (G), and when disclosure is required. Under the Revised Draft Rule, paragraphs (b)(i)(A) and (G) required municipal advisors to disclose "any . . . potential conflicts of interest . . . that might impair" a municipal advisor's advice or its ability to provide advice in accordance with section (a) of Proposed Rule G-42. The language in these paragraphs concerned certain commenters, such as SIFMA, because they believed that such a standard would include nearly all imaginable conflicts of interest and result in overly broad disclosure that could distract from the provision's purpose. Therefore, to clarify, the MSRB has amended these paragraphs to state that disclosure is required, in paragraph (A) for "any actual or potential conflicts of interest," and, in paragraph (G), for "any other engagements or relationships." The MSRB believes that this revised language would more clearly establish a limiting, objective standard for disclosing certain conflicts of interest that would be relevant to a municipal advisor's client.

Further, paragraphs (b)(i)(A) and (G), as proposed, are revised to limit the disclosure of conflicts required under paragraphs (b)(i)(A) and (G) to those that potentially impact the advisor's ability to provide "advice to or on behalf of the client in accordance with the standards of conduct of section (a) of this rule, as applicable." Previously, under the Revised Draft Rule, paragraphs (b)(i)(A) and (G) required a municipal advisor to provide disclosure of conflicts of interest that "might impair its ability either to render unbiased and competent advice to" its clients. This revision was made after re-evaluation of the phrasing used in the paragraphs and consideration of comments received from Sanchez. Sanchez stated that the use of the phrase "unbiased and competent advice" in the Revised Draft Rule ". . . . appear[s] to import the duty of loyalty and duty of care into the representations of obligated persons. . . ." The MSRB agrees that the use of the phrasing "unbiased and competent advice" does not encompass all of the duties municipal advisors owe their clients, nor would it sufficiently differentiate between the

standards of conduct owed by municipal advisors to their municipal entity clients and obligated person clients. The MSRB believes that the revised standard for identifying material conflicts of interest under proposed paragraphs (b)(i)(A) and (G) will more clearly reflect the standards of conduct in proposed section (a) and appropriately differentiate between municipal entity and obligated person clients.

In response to the Second Request for Comment, Sanchez also suggested a revision to clarify the last sentence of subsection (b)(i) of the Revised Draft Rule. Sanchez suggested deleting the term "written documentation" and using "written statement" instead to clarify for municipal advisors the action required to comply with subsection (b)(i). To remove any ambiguity, the MSRB has revised proposed subsection (b)(i) to clarify that, when appropriate, a municipal advisor must provide a "written statement" that the municipal advisor has no known material conflicts of interest.

Columbia Capital requested clarification regarding whether the disclosures required by the Revised Draft Rule may be made in more than one document. The required disclosures indeed may be provided to clients in more than one document, as long as the document and its delivery otherwise comply with the proposed rule. Because the language of the proposed rule is not to the contrary, the MSRB has not made any revisions in response to this comment.

FSR commented that use of the term "indirectly" in paragraph (b)(i)(B) in the Revised Draft Rule, which required disclosure of "any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor," expanded the scope of the required disclosures unnecessarily and would make compliance difficult for a municipal advisor that is part of a large multi-service financial conglomerate. FSR believed that

the Revised Draft Rule did not provide municipal advisors with sufficient guidance to identify activity that could be indirectly related to municipal advisory activities, and, taken in its plain meaning, could lead to a substantial burden on firms having numerous affiliates that provide a wide array of services. After further consideration of the purpose and intent of the proposed paragraph, the MSRB has removed the clause "or indirectly." The MSRB believes revised proposed paragraph (b)(i)(B) will provide the appropriate notice to clients of the relationships of any affiliates of the municipal advisor that are likely to present material conflicts of interest.

Disclosure of Legal or Disciplinary Events

Several commenters addressed the draft requirements to disclose legal or disciplinary events. FSR commented that subsection (b)(ii) of the Revised Draft Rule would require a separate written disclosure of legal or disciplinary events that is redundant of the requirements of subsection (c)(iii) of the Revised Draft Rule. FSR requested that "these disclosure requirements be deemed satisfied if an advisor provides information about where clients may access electronically the advisor's most recent [SEC] Forms MA and MA-I, along with the date of the last material amendment to any legal or disciplinary event disclosure on such forms." SIFMA, in response to the Second Request for Comment, similarly stated that requiring "[duplicative] disclosure of specific events that are already disclosed in [SEC] Forms MA and MA-I provides little, if any, benefit to municipal entities or obligated persons, while it imposes unnecessary additional burdens on municipal advisors." SIFMA suggested that providing clients with the information regarding how to obtain electronic access to a municipal advisor's legal and disciplinary history on SEC Forms MA and MA-I should suffice. Sanchez stated, regarding the Revised Draft Rule, that "[t]his requirement appears to be overly burdensome . . . , [and] it should be sufficient for purposes of this rule that a municipal advisor be required to direct clients

to their EDGAR filings by providing clients with sufficiently specific information to locate their EDGAR filings." [64]

The MSRB contemplated that municipal advisors would be able to satisfy their disclosure of legal and disciplinary events under sections (b) and (c) of the Revised Draft Rule with specific reference to the relevant portions of their most recent SEC Forms MA or MA-I filed with the Commission. Proposed Rule G-42(b)(ii) further clarifies this intention, and requires the municipal advisor to provide detailed information specifying where the client may electronically access such forms. The MSRB believes this approach will address the issue of duplicative disclosure of the disciplinary and other legal events contained in SEC Forms MA and MA-I. This revision also clarifies that municipal advisors may satisfy the disclosure requirements of subsections (b)(ii) and (c)(iii) in a similar fashion.

A municipal advisor could, conceivably, simultaneously satisfy the requirements of proposed subsections (b)(ii) and (c)(iii) in one document if it were provided to the client prior to or upon engaging in municipal advisory activities for the client. However, if combined written disclosure and relationship documentation were made after a municipal advisor engages in municipal advisory activities, the municipal advisor would only be in compliance with proposed subsection (c)(iii) and not subsection (b)(ii).

SIFMA also suggested that subsection (c)(iv) of the Revised Draft Rule should be removed. The subsection would require municipal advisors to document the date of the last

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64 In response to the First Request for Comment, Sutherland suggested that there is sufficient disclosure about disciplinary history provided in a municipal advisor's SEC Forms MA and MA-I filed with the SEC, and Parsons stated that disclosure should not be required in the rule given such public disclosure on those forms. Similarly, Lewis Young and NAIPFA believed the disclosure of legal or disciplinary events would be duplicative and unnecessarily burdensome and also suggested that municipal advisors should be able to satisfy the requirement by referencing SEC Forms MA or MA-I.

material change, including any addition, to the legal or disciplinary event disclosures on any SEC Form MA or MA-I filed with the Commission. Specifically, SIFMA believed that requiring municipal advisors to update their written disclosures and documentation with each of their municipal advisory clients whenever a material change to a legal or disciplinary event was made to any SEC Forms MA or MA-I would be unjustified.

Proposed section (c) requires the documentation of the municipal advisory relationship to be promptly amended or supplemented to reflect any material changes or additions, and requires the amended documentation or supplement to be promptly delivered to the municipal entity or obligated person client. However, the MSRB does not believe the update requirement under proposed section (c) is overly burdensome because municipal advisors need only provide the date of the last material change, including any addition, to their legal or disciplinary event disclosure to their clients, as they would be permitted to reference their SEC Forms MA and MA-I for the details of such material changes. Additionally, the required documentation of the municipal advisory relationship could be satisfied through the use of more than one writing and updates or amendments to such documents could be additional, separate writings that either amend or supplement earlier writings. The MSRB believes these accommodations sufficiently address the concern that municipal advisors would be required to amend and redistribute a single writing every time a material change or addition needed to be included. Further, the MSRB believes that, by requiring municipal advisors to update the written documentation relating to legal or disciplinary event disclosures provided to municipal entities and obligated persons, proposed subsection (c)(iv) would help ensure that those clients have sufficient, accurate and current information to better inform their decisions to engage and/or continue engaging a municipal advisor. The MSRB notes that the requirements of proposed section (c) must be made

in writing and delivered to the municipal advisor's client in accordance with the duty of care and, as applicable, the duty of loyalty.

Coastal, Kutak and Parsons objected to the Initial Draft Rule's requirement to disclose the legal and disciplinary events for all individuals at a municipal advisory firm for which the firm is required to submit an SEC Form MA-I. They suggested that municipal advisors should not be required to disclose to a client legal and disciplinary events that relate to an individual that is employed by the municipal advisor, if that individual is not a part of (or reasonably expected to be a part of) the advisor's team working for the client. Although there could be numerous municipal advisors with large numbers of employees, as Coastal indicated, the MSRB believes there is insufficient cause to narrow the requirement of this disclosure obligation. Specifically, the MSRB notes that, although all of a municipal advisor's employees might not be a part of the team working on a particular client matter, the number of employees with legal or disciplinary events that a municipal advisor employs and the nature of any past legal or disciplinary events related to those employees could be material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel. In any event, since a municipal advisor could satisfy Proposed Rule G-42(b)(ii) and (c)(iii) by providing information specifying where the client can electronically access SEC Forms MA and MA-I, there would be little additional burden imposed on municipal advisors by leaving the scope of these requirements unchanged.

Type of Writing(s) Required to Document the Municipal Advisory Relationship

Several commenters discussed the matter of documenting the municipal advisory relationship and the type of writing that should be required to evidence the municipal advisory relationship between the municipal advisor and its client.

FLA DBF, correctly recognizing that the Revised Draft Rule's reference to a "writing" does not require a written contract, suggested that the proposed rule change should be amended to require municipal advisors to enter into written contracts with their municipal entity clients regarding their municipal advisory relationships. In contrast, GFOA, while also correctly recognizing that the Revised Draft Rule does not require a written contract, supported the absence of a contract requirement. GFOA noted that although entering into a bilateral contract is a GFOA best practice, "there may not always be a need for a specific contract." GFOA agrees with the MSRB that the municipal advisory relationship should be stated in writing as it would allow the issuer to clearly delineate the scope of work it intends its municipal advisor to provide.

A number of other commenters, including ABA, BDA, ICI, Lewis Young, MSA, NAIPFA and SIFMA, however, construed section (c) of the proposed rule as requiring a written contract, leading them to raise various concerns about the proposed rule applying to existing contracts that might need to be revised. As a result, these commenters suggested the inclusion of various kinds of transitional rule provisions to address these issues. ABA and Lewis Young, for example, requested a transitional provision to permit advisors to honor their existing agreements with their clients until they expire. ICI recommended that the MSRB clarify that, if approved, Proposed Rule G-42 would only apply prospectively. SIFMA requested that the MSRB limit or eliminate the need for municipal advisors to re-document their municipal advisory relationships and apply the disclosure requirements of the proposed rule only to future agreements. MSA requested guidance on whether the obligations of section (c) of Proposed Rule G-42 could be satisfied by a contract (such as a Master Services or Professional Services Agreement) between the municipal advisor and its client.

The documentation requirement of section (c) of Proposed Rule G-42, as with the Revised Draft Rule, would not require the creation of new contractual relationships or the modification of existing contracts or agreements between municipal advisors and their clients. The purpose of the requirement is to help ensure that certain terms of each municipal advisory relationship would be reduced to writing and delivered to the municipal advisor's municipal entity or obligated person client. So long as the content of the documentation adheres to the requirements of the proposed rule (including the standards of conduct in section (a)), municipal advisors and their clients have some latitude in deciding the exact form the documentation and writing might take. If municipal advisors have already delivered documentation meeting some or all of the requirements of proposed section (c), then municipal advisors would be able to rely on such documents to satisfy some or all of their obligations under section (c). While certainly permitted, the proposed rule would not require municipal advisors to enter into written contracts with their municipal entity or obligated person clients and municipal advisors could satisfy the requirements of provision (c) by providing separate or supplemental documents to any preexisting contract, agreement or writing previously provided that might be in place between the municipal advisor and its client. The relevant part of proposed section (c) has been further revised to delete the phrase "enter into" (which could have connoted the formation of a contract) and reads as follows: "A municipal advisor must evidence each of its municipal advisory relationships by a writing or writings created and delivered to the municipal entity or obligated person client prior to, upon or promptly after the establishment of the municipal advisory relationship." The MSRB believes that requiring the documentation to take the form of a bilateral contract would be unnecessary and could lead to some of the burdensome consequences identified by commenters. The amendments to the Revised Draft Rule should clarify that

municipal advisors would not be required to alter or re-execute any existing contract and that, in the future, the documentation and disclosure requirements could be satisfied in writings that are either included in a contract or separate and independent of any contract entered into between the municipal advisor and its municipal entity or obligated person client.

In response to the First Request for Comment, BDA and GKB stated that they generally supported the documentation and disclosure requirements of section (c) of the Initial Draft Rule but believed, with respect to municipal financial products, that a "written agreement" (as they believed was required by section (c)) should only be required when municipal advisory activities are engaged in for compensation. Based on their comments, it appears that BDA and GKB understood section (c) to implicitly require the municipal advisor and its client to evidence their municipal advisory relationship with a bilateral contract. NAIPFA, in its response to the Initial Draft Rule, asked the related question: "Does this mean that the writing must be a two party agreement?" NAIPFA also suggested that the MSRB amend section (c) to allow municipal advisors to satisfy the requirements of the section through an engagement letter. As previously stated, section (c) would not require, or preclude the use of a bilateral contract or engagement letter to evidence the municipal advisory relationship. So long as the content adheres to the requirements of Proposed Rule G-42 (including the standards of conduct of section (a)), municipal advisors and their clients would have some latitude in deciding the exact form the documentation and writings might take.

NAIPFA expressed concerns regarding the amount of information that would be required to be included in the documentation required by section (c), stating that municipal advisors would be put at a "significant competitive disadvantage to their [underwriting] counterparts . . . [because] underwriters are not mandated to include any particular contract-related terms within

their engagement letter, such as clauses relating to the termination of the relationship or their obligations relating to certain aspects of the transaction . . . .” The MSRB does not believe the proposed documentation requirement would result in the competitive disadvantages described by NAIPFA. First, underwriters are required to make similar disclosures to issuers of municipal securities under MSRB’s fair dealing rule, Rule G-17, which includes certain disclosures regarding the underwriter’s compensation. Second, to the extent any of the requirements of section (c) are included in a written agreement, contract, engagement letter or similar document already in possession of the client, such information would not need to be included in a separate writing delivered to the municipal advisor’s client. Instead, municipal advisors would be able to supplement existing writings to comply with section (c). Finally, because a municipal advisor generally would be prohibited from acting as an underwriter for a transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice, the MSRB believes it would be unlikely that a municipal advisor would be in direct competition with an underwriter as suggested by NAIPFA.

In response to the Initial Draft Rule, ICI suggested that section (c) be revised to specify that only material changes to the information provided in the documentation required by section (c) would trigger the updating requirement. The MSRB did not intend by section (c) to require the supplementation of immaterial information and section (c) of the proposed rule has been revised to provide this clarification.

Triggering the Documentation Required by Section (c)

Under the Initial Draft Rule, a municipal advisor would have been required to evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly

after the inception of the municipal advisory relationship. In response to the First Request for Comment, Northland commented that section (c) of the Initial Draft Rule should require that the documentation be in place prior to engaging in municipal advisory activities rather than being permitted to be created and provided subsequently (i.e., after the establishment of a municipal advisory relationship (as defined by the Initial Draft Rule)). Northland opined that its approach would align the proposed rule change with analogous requirements and principles of the SEC Final Rule. Northland also argued that earlier documentation of the municipal advisory relationship is warranted for the same reasons it believes justify the proposed rule change's requirement to disclose conflicts of interest upon or prior to engaging in municipal advisory activities. The MSRB has considered when municipal advisors should be required to document their relationship with their clients and determined that documentation should only be required after both parties have agreed that the municipal advisor would engage in municipal advisory activities for or on behalf of the client. It is understood by the MSRB that a municipal advisor could engage in municipal advisory activities while seeking an engagement to perform municipal advisory activities but then might ultimately not be engaged by the client. Also, in some instances, a municipal advisor could be called upon to engage in municipal advisory activities on behalf of its client on short notice for a time-sensitive matter. In such scenarios, the MSRB does not believe it would be appropriate, or necessary, to require documentation of the municipal advisory relationship because, as with the first case, there is a reasonable possibility that no municipal advisory relationship would materialize and, with regard to the second, the MSRB does not want to inhibit a municipal advisor from performing its municipal advisory activities for municipal entities and obligated persons when time is short and documenting the municipal advisory relationship might not be feasible. The MSRB believes that, when balanced against the

potential benefits of requiring earlier documentation of the municipal advisory relationship, the timely disclosure of material conflicts of interest (in accordance with section (b) of Proposed Rule G-42) will sufficiently mitigate the potential consequences identified by Northland and will serve as sufficient protection to a municipal advisor's client to make an informed decision about whether to accept the advice provided by the municipal advisor until such time that documentation containing the information required by section (c) can be created and delivered.

On a separate but related matter, Northland stated that the use of the term "municipal advisory relationship" would likely lead to confusion between how Northland believes the term is used by municipal advisors and other industry participants and how the term had been defined for purposes of the Initial Draft Rule. Northland believed that it would be difficult for municipal advisors to parse apart and document "municipal advisory relationships" when some of those relationships are "historical and ongoing" and are rarely thought of as separate relationships. The MSRB believes that the definition provided in Proposed Rule G-42(f)(vi) would provide sufficient guidance to municipal advisors in this regard. That provision would state that a municipal advisory relationship is deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person and ends on, the earlier of, the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship, or the date on which the municipal advisor withdraws from the municipal advisory relationship.

In response to the Second Request for Comment, Piper Jaffray, while generally supportive of the documentation requirement of section (c) of the Revised Draft Rule, expressed concern that it could require premature documentation of a municipal advisory relationship. Specifically, Piper Jaffray stated that section (c) could require documentation when the

municipal advisor has not been selected by its client to be its municipal advisor and, instead, is, in fact, engaging in municipal advisory activities as a means to obtain the engagement with the client to perform municipal advisory activities. Section (c) of the Revised Draft Rule, however, explicitly stated that the documentation requirement would only be triggered "prior to, upon or promptly after the establishment of the municipal advisory relationship" (emphasis added). As defined in subsection (f)(vi), a municipal advisory relationship would only be deemed to exist when the "municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person." Thus, Proposed Rule G-42 would not necessarily require the provision of relationship documentation during an early stage of municipal advisory activities when the municipal advisor is still pursuing an engagement to perform municipal advisory activities.

Other Comments Regarding the Documentation Requirement

Consolidation. In response to the Revised Draft Rule, Piper Jaffray suggested that the disclosure and documentation requirements of sections (b) and (c) could be more clearly established if the sections were merged. In particular, Piper Jaffray found it confusing that a municipal advisor providing "advice," but that has not yet been engaged by an issuer, must provide disclosures related to its compensation under paragraph (b)(i)(F). Piper Jaffray then posed the question: "[I]s the intention of the [MSRB] to assure that municipal advisors must provide conflicts disclosure when providing information that would constitute 'advice' prior to [being] engaged[?]" Piper Jaffray suggested that the intention and purpose of the proposed rule change could be better served if the required disclosures and documentation of the municipal advisory relationship were provided when the advisor is selected by the issuer to provide it with advice.

The MSRB has considered Piper Jaffray's recommendation to merge sections (b) and (c) and modify the timing of the disclosure requirement, but believes such amendments would conflict with the intention of having municipal advisors disclose conflicts of interest upon or prior to engaging in municipal advisory activities for the client. Combining the paragraphs could cause municipal advisors to delay making the proposed rule's required disclosures until the municipal advisory relationship has been reduced to writing, which could be a significant amount of time after the client has received, and potentially acted on, advice from the municipal advisor. For these reasons, the suggested changes are not included in Proposed Rule G-42.

Indirect Compensation and Treatment of Incidental Informal Advice. Regarding the documentation of the municipal advisory relationship, SIFMA requested that Proposed Rule G-42 include a definition of "indirect compensation" as it is used in subsection (c)(i). On a related topic, SIFMA requested that the MSRB "clarify that informal advice that is incidental to providing brokerage/securities [services] would not, alone, trigger a written documentation requirement under [section (c) of the Revised Draft Rule] . . . ."

The MSRB believes that additional clarification within the proposed rule change is not necessary because the phrase "indirect compensation" is widely used and understood in the municipal advisory and securities industry and is well established in securities statutes and jurisprudence. Providing a definition of "indirect compensation" within Proposed Rule G-42 might reduce clarity regarding the general understanding of the phrase and lead to unnecessary confusion in an instance where sufficient guidance is already available.

Regarding SIFMA's request pertaining to advice that is incidental to providing brokerage/securities services, the MSRB notes that the proposed rule change would apply to a scope of municipal advisory activities as defined in the SEC Final Rule. Whether certain

activities constitute "advice" under the SEC Final Rule is a legal interpretation within the authority of the SEC, and not the MSRB, to make.

Recommendations and Review of Recommendations of Other Parties

Section (d) of Proposed Rule G-42 would provide that if a municipal advisor makes a recommendation of a municipal securities transaction or municipal financial product to its client, the municipal advisor must determine, based on the information obtained through reasonable diligence, whether the transaction or product is suitable for the client. Section (d) also would contemplate that a municipal advisor could be asked to evaluate a recommendation made to its client by another party, such as a recommendation by an underwriter of a new financing structure or a new financial product. Section (d) would require municipal advisors to conduct a suitability analysis – when requested by the client and within the scope of the engagement – of the recommendations of these third parties, guided by the requirements and principles contained in relevant portions of the supplementary material (such as paragraphs .01, .08 and .09).

Commenters raised a number of issues with section (d) of Proposed Rule G-42 (sections (d) and (e) of the Initial Draft Rule) and the related paragraphs .01 (Duty of Care), .08 (Suitability) and .09 (Know Your Client) of the Supplementary Material to Proposed Rule G-42. Below is a summary of, and response to, these comments.

General Comments Regarding Section (d)

In response to the Second Request for Comment, NAIPFA and GFOA expressed their general support for the Revised Draft Rule's suitability standard of section (d) of Proposed Rule G-42. NAIPFA believed it appropriately reflects a municipal advisor's fiduciary duties to its municipal entity clients.

Compliance and Examination. BDA, in response to the Second Request for Comment, expressed its support of the Revised Draft Rule's requirement to have municipal advisors review recommendations of other parties, but requested specific guidance on how municipal advisors would develop reasonable policies to comply with section (d). BDA also expressed concern about how FINRA examiners would test a dealer's compliance with the requirements of section (d) when serving as a municipal advisor.

The MSRB believes it has provided sufficient guidance to municipal advisors about the principles and requirements that should inform, and be incorporated in, a municipal advisor's policies and procedures by identifying the matters in the proposed rule text (such as in subsections (d)(i)-(iii) and paragraphs .01, .08 and .09 of the Supplementary Material) that a municipal advisor must, as applicable, consider when forming its advice or recommendation. The MSRB recognizes the diversity of the population of municipal advisors and the municipal advisory activities in which they engage in and believes the primarily principles-based approach taken by the proposed rule change will accommodate that diversity. The MSRB also believes this approach will clearly establish the minimum requirements and principles, which financial regulators could then consistently apply in their examination of municipal advisors.

Updating Recommendations. In response to the Second Request for Comment, SMA requested that the MSRB clarify that the suitability of a recommendation would be determined by the facts and circumstances at the time a client enters into the municipal securities transaction and that the municipal advisor should not have continuing responsibility to update its determination.

The MSRB believes that whether advice given or recommendations made by municipal advisors would need to be updated would depend on the facts and circumstances surrounding the

advice and recommendation, including, but not limited to, the scope of the services that the municipal advisor agreed to provide its client. The MSRB believes that the reasonableness of a municipal advisor's recommendation or advice would be determined by considering the information relied upon by, and available to, the municipal advisor at the time the recommendation is made or advice is given to its client. However, over the course of an ongoing municipal advisory relationship, it is possible that a municipal advisor would, as part of its duty of care, need to apprise its client of changes to the suitability of the advice or recommendation it had previously given. In such cases, a municipal advisor's responsibilities would depend upon the facts and circumstances and the parameters of its municipal advisory relationship. The MSRB believes that the proposed rule change will provide municipal advisors with the requisite guidance to comply with its requirements.

Third-Party Recommendations. Lamont and First Southwest, in response to the First Request for Comment, requested clarification regarding whether a municipal advisor must review any third-party recommendation related to the advice that the municipal advisor has agreed to provide.

Proposed Rule G-42 would require municipal advisors to review a third-party recommendation when such a review is within the scope of the engagement between it and its client or if such a review would be part of the reasonable diligence required to reasonably determine whether a recommendation or advice is suitable for its client. Therefore, a municipal advisor's obligation to review third-party recommendations would depend on the facts and circumstances of each particular instance. The MSRB believes that section (d) and the relevant portions of the supplementary material of the proposed rule change will provide sufficient guidance to municipal advisors presented with such scenarios.

Informing Client of Matters Related to Review of Recommendation. In response to the First Request for Comment, Northland commented that the Initial Draft Rule's requirement that municipal advisors must, under section (d), discuss matters such as the material risks of a recommendation and the basis upon which the municipal advisor reasonably believes its recommendation is suitable for its client would encourage written documentation of such discussions and create the potential for conflict between the information provided by the municipal advisor and the actions ultimately taken by the client. It appears that Northland's concern is that a municipal advisor could be exposed to liability in an ex post review of its suitability analysis.

The MSRB received other comments related to the Initial Draft Rule's requirement that municipal advisors must discuss these matters with their clients. In response, the Revised Draft Rule included a modification that required municipal advisors to inform their clients of the matters specified in proposed section (d). The modification was made to grant some flexibility to municipal advisors in the manner in which the matters are delivered to their clients. The MSRB understands that a municipal advisor's client could elect to engage in a course of action that deviates from the municipal advisor's recommendation. For purposes of compliance with section (d), however, a client's decision to disregard its municipal advisor's recommendation would alone have no bearing on whether the municipal advisor conducted an adequate analysis of the recommendation it provided. An examination for compliance with section (d) would focus on the adequacy of the suitability analysis provided by the municipal advisor, not whether the client ultimately pursued the municipal advisor's recommendation.

Limiting Duty to Review Recommendations of Others. In response to the First and Second Request for Comment, NAIPFA stated that, when a municipal entity or obligated person

has engaged an independent registered municipal advisor[65] and is also obtaining advice from a third party that is relying upon the independent registered municipal advisor exemption from the SEC registration requirement[66] to provide advice to the municipal entity or obligated person, the independent registered municipal advisor should not be permitted to limit the scope of the engagement with its client so as not to include the review of recommendations made by the third-party.

The MSRB has considered, yet disagrees with, NAIPFA's position. The MSRB believes that municipal advisor clients, with the agreement of the municipal advisor, should be able to define the scope of their municipal advisory relationships and thus determine what services the municipal advisor will provide. Furthermore, requiring municipal advisors to review all third-party recommendations could result in a costly burden to municipal entities and obligated persons that do not expect to derive sufficient value from such review. However, the MSRB acknowledges that limiting the scope of the engagement between a municipal entity or obligated person and its independent registered municipal advisor could affect a third party's ability to qualify and make use of exemptions discussed in the SEC Final Rule, including the exemption mentioned by NAIPFA.[67]

Request for Definition of "Independent" as Used in Paragraph .03 of the Supplementary Material

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65 See SEC Rule 15Ba1-1(d)(3)(vi) (17 CFR 240.15Ba1-1(d)(3)(vi)). "Independent registered municipal advisor" is defined in SEC Rule 15Ba1-1(d)(3)(vi)(A) (17 CFR 240.15Ba1-1(d)(3)(vi)(A)).

66 See SEC Rule 15Ba1-1(d)(3)(iv) (17 CFR 240.15Ba1-1(d)(3)(iv)).

67 17 CFR 240.15Ba1-1.

BDA, in response to the First Request for Comment, requested that the MSRB define the term "independent" for purposes of paragraph .03 of the Supplementary Material, action independent of or contrary to advice, to the Initial Draft Rule. Proposed paragraph .03 states that a municipal advisor would not be required to disengage from a municipal advisory relationship if its client were to elect a course of action that is "independent or contrary" to the advice provided by the municipal advisor. BDA asked if "independent" would mean that the municipal advisor's client is not relying on or considering the advice of the municipal advisor; that the client is not seeking advice from the municipal advisor; or, that the client is acting contrary to advice given by the municipal advisor.

Proposed paragraph .03 of the Supplementary Material was designed to address instances when a municipal advisor's client has decided either not to accept, rely on or consider the municipal advisor's advice or to take an approach or position that varies (completely or partially) from advice provided by the municipal advisor. In the event of such occurrences, paragraph .03 would allow a municipal advisor to continue in its advising capacity so long as doing so would not otherwise be precluded by MSRB rules or federal, state or other laws, as applicable.

Scope of the Recommendations Analysis. Proposed section (d) and paragraph .08 of the Supplementary Material address municipal advisors' recommendations of municipal securities transactions or municipal financial products. However, as part of the duty of care articulated under proposed paragraph .01 of the Supplementary Material, a municipal advisor would be required to have a reasonable basis for any advice provided to its client.

Northland requested clarification regarding whether section (d) of the Initial Draft Rule would be applicable to all recommendations provided by the municipal advisor or only when a recommendation is related to entering into a municipal securities transaction or municipal

financial product. NABL stated, in response to the First Request for Comment, that "suitability," as a general matter, is a regulatory concept that could not be appropriately applied to municipal advisors in all instances. NABL suggested that a municipal advisor should be permitted to make a recommendation as to a limited aspect of the transaction, even if the municipal advisor does not agree that the transaction is suitable.

Section (d) of Proposed Rule G-42 would provide that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product unless the municipal advisor has determined, based on the information obtained through the reasonable diligence of the municipal advisor, whether the transaction or product is suitable for the client. A municipal advisor could provide advice regarding an aspect of a municipal securities transaction or municipal financial product that the municipal advisor believes to be unsuitable for its client so long as the municipal advisor adhered to the duty of care, duty of loyalty, and all other laws, as applicable, and either did not recommend the unsuitable transaction or product or informed the client of the basis on which the municipal advisor reasonably believed the transaction or product to be unsuitable.

Documenting Recommendations. Lewis Young expressed concern that section (d) of the Initial Draft Rule would require excessive and "defensive" recordkeeping and documentation in order to evidence compliance with the section's requirement that municipal advisors inform their clients of certain matters pertaining to their recommendations. Lewis Young argued that such documentation would be a "waste of time and resources" because the client has already determined to pursue a particular municipal securities transaction or municipal financial product. Accordingly, Lewis Young believed documenting such discussions "so as to have a 'good answer' for the next regulatory audit" would be overly and unnecessarily burdensome.

The MSRB believes that the proposed rule change sufficiently articulates that municipal advisors and their clients would have the discretion to define the parameters of their municipal advisory relationship and, thus, decide between them what municipal advisory activities would be performed by the municipal advisor for its client, including what matters for which a municipal advisor would be providing advice. As such, regarding the scenario proffered by Lewis Young, a municipal advisor that has not been engaged to provide advice about a municipal securities transaction or municipal financial product that was previously selected by its client would not be under an implicit obligation to provide the client with the suitability analysis described in proposed section (d) and the supplementary material. The municipal advisor would remain subject to (among other provisions of the proposed rule change) a duty of care, duty of loyalty (as applicable) and relevant supplementary material such as paragraphs .04 (Limitations on the Scope of the Engagement) and .09 (Know Your Client). Further, the MSRB believes that the documentation required by proposed Rule G-8(h)(iv) is an appropriately tailored recordkeeping requirement that will assist regulatory examiners in assessing the compliance of municipal advisors with the proposed rule change. Also, the MSRB believes the recordkeeping requirements will not be overly burdensome because municipal advisors would only be required to maintain documents created by the municipal advisor that were material to its review of a recommendation by another party or that memorializes the basis for any conclusions as to suitability.

Recommendations of Investment Funds. NY State Bar requested the MSRB to clarify the obligations owed by a municipal advisor to its client when the recommendation is to invest in an investment fund that is managed by a third-party advisor. NY State Bar's concern was that, under the Initial Draft Rule, a municipal advisor would be obligated to provide a

recommendation, and therefore a suitability analysis, of the investment choices made by the manager of the investment fund.

Depending on the facts and circumstance of a particular scenario, such as described by NY State Bar, a municipal advisor could have a multitude of different obligations regarding its recommendation of an investment fund to a client. While the proposed rule change would allow municipal advisors and their clients to negotiate the municipal advisory activities to be performed, the standards of conduct articulated in section (a) and the relevant paragraphs of the supplementary material would not be subject to alteration. Therefore, a municipal advisor that has agreed to provide a recommendation regarding the investment in an investment fund would be required to exercise a duty of care that could, in turn, require the municipal advisor to conduct a suitability analysis that might, depending on the relevant facts and circumstance of a particular instance, require the municipal advisor to conduct a suitability analysis of the investment choices made by the manager of the investment funds. By establishing the applicable standards of conduct for municipal advisors, and providing additional guidance regarding those standards in the supplementary material to Proposed Rule G-42, the MSRB believes that municipal advisors will be able to make a determination regarding what actions they must undertake when making recommendations to clients.

Prescriptive Metrics for Suitability Analysis. In response to the First Request for Comment, MSA asked whether the MSRB would provide the "specific metrics (standard debt issuance options)" that should be used to determine the suitability of a recommendation. MSA also inquired into whether "there [will] be standards set for this quantitative review or will it be the responsibility of the individual [municipal advisor] to define the suitability metrics based on the unique circumstances of each client or project?"

In order to accommodate the diversity of the municipal securities and municipal advisory marketplace, the MSRB has taken a primarily principles-based approach regarding the required suitability analysis so that municipal entities and obligated persons would receive appropriately tailored and relevant advice and recommendations from their municipal advisors. For this reason, the MSRB does not intend to provide the specific metrics requested by MSA and instead will rely upon the principles and requirements provided by the proposed rule change.

Municipal Advisor Reliance on Information Provided by Client

A number of commenters voiced apprehension regarding what they believed to be the high standard set for providing recommendations to their clients or reviewing the recommendation of a third party. Specifically, commenters expressed concern with the portion of paragraph .01 (which would be applicable to recommendations contemplated under section (d)) that would require a municipal advisor to "undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information." Most commenters stated that a municipal advisor should be able to rely on the accuracy and veracity of the information provided by a client and not be required to validate such information.

Sutherland asked, in response to the First Request for Comment, in the context of 529 plans, what the Initial Draft Rule would require a municipal advisor to do in order to satisfy the proposed obligation to undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. Sutherland also asked whether a municipal advisor must obtain a representation from the issuer that the information it provides does not contain any material misstatements or omissions.

In response to the Second Request for Comment, ICI stated that municipal advisors to 529 plans should not be required to verify the veracity or completeness of the information

provided to them by persons who are authorized by the municipal entity client to act on behalf of a state's 529 plan.

NABL commented that a municipal advisor should be free to recommend a transaction based on facts given to it by its client, without exercising any diligence to check the facts, if consistent with the scope of the engagement with its client. Regarding the review of recommendations of others, MSA asked whether it would be necessary to obtain documentation or information used by a third-party to make a recommendation that the municipal advisor has been engaged to review. MSA believed that the Initial Draft Rule should require the third party, who provided the recommendation and that the municipal advisor has been engaged to review, to disclose any documentation relied upon for that recommendation.

The duty of care is a core principle underlying many of the obligations of the proposed rule and is included, among other reasons, to ensure municipal entities and obligated persons are shielded from the potential negative consequences that could result from not receiving well-informed advice and expertly-executed services from their municipal advisors. The MSRB believes that requiring municipal advisors to conduct a reasonable investigation about the accuracy and completeness of the information, including information pertaining to a 529 plan, on which they will be basing their advice is necessary to ensure that clients will be able to make an informed decision based on facts and choose a prudent course of action. As stated in section (d), the municipal advisor would only need to exercise reasonable diligence, thus obviating the need for a municipal advisor to go to impractical lengths to determine the accuracy and completeness of the information on which it will be basing its advice and/or recommendation. The MSRB believes that obtaining a representation from the municipal advisor's client that the information it has provided, with no or insufficient diligence conducted by the municipal advisor, would not

satisfy either section (d) or paragraph .01 of the Supplementary Material of Proposed Rule G-42 because such a representation would not sufficiently preclude the potential for the risks associated with providing advice or recommendations without a reasonable inquiry into the accuracy and completeness of the information upon which such advice or recommendations are based. While alone, such a representation would not satisfy the requirements of the proposed rule change, a municipal advisor would be free to seek and obtain such a representation as a prudent part of its process for conducting a reasonable investigation of the veracity and completeness of the information on which it is basing its recommendation.

Applicability of Suitability Analysis to 529 Plans

Several commenters raised concerns about how section (d) and the related supplementary material that address suitability analysis would generally apply to municipal advisors advising 529 plans.

ICI stated, in response to the Second Request for Comment, that the suitability standard set forth in paragraph .08 of the Supplementary Material should recognize what ICI believes to be differences between advice rendered in connection with municipal securities, generally, and that rendered in connection with 529 plans. Sutherland voiced concerns in its response to the First Request for Comment and stated that the suitability factors listed in paragraph .08 and section (d) are not workable with regard to 529 plans. ICI believed that some of the factors for determining suitability included in paragraph .08 would be “largely irrelevant in the context of rendering advice to a 529 plan” and the MSRB should modify the Revised Draft Rule to explicitly state that such factors would not apply to advice relating to 529 plans. In the absence of exempting 529 plans from needing to consider such factors, ICI asked the MSRB to clarify how it intends the listed factors to apply to 529 plans.

In consideration of these comments, the MSRB has modified proposed paragraph .08 (formerly paragraph .09) of the Supplementary Material to allow municipal advisors to base a suitability determination only on the listed factors that are applicable to the particular type of client being advised. The MSRB, accordingly, has inserted the phrase "as applicable to the particular type of client" as a qualifier to the list of factors in paragraph .08 that must be considered in a suitability analysis. The modifications proposed should address the commenters' concerns such as how factors such as "financial capacity to withstand changes in market conditions" would apply given that 529 plans are not dependent on external sources of revenue or funding to satisfy claims of investors. However, the listed factors in paragraph .08, consistent with the regulation of recommendations in other securities law contexts, are focused on the client and not the product involved.

Request for Clarification of Documentation and Procedural Requirements

In response to the Second Request for Comment, Piper Jaffray requested additional clarification on what a municipal advisor would need to do, and what documents would need to be created, to comply with the Revised Draft Rule's suitability requirements. Specifically, Piper Jaffray asked what the proposed rule change would require with regards to decisions that Piper Jaffray refers to as "smaller decisions" (e.g., call features and whether to utilize a premium bond structure that has a lower yield to call).

The proposed rule change would require, pursuant to the duty of care, a municipal advisor to have a reasonable basis for any advice it provides to or on behalf of its client. Also, municipal advisors would be required to conduct a suitability analysis of recommendations of municipal securities transactions and municipal financial products that would comport with the requirements of proposed paragraph .08 of the Supplementary Material. Whether or not a

suitability analysis would be required would depend, as previously discussed in Item II.A., on the facts and circumstances surrounding the communication made by the municipal advisor and whether the communication was a recommendation of a municipal securities transaction or municipal financial product. Advice as to the "smaller decisions" asked about by Piper Jaffray might, or might not, depending on the facts and circumstances of a particular instance, rise to the level of being a recommendation that would require a suitability analysis under the proposed rule change, even though such advice may relate to a municipal securities transaction or municipal financial product and therefore trigger other provisions of the proposed rule, because the advice might not reasonably be viewed as a "call to action" that would constitute a recommendation of a municipal securities transaction or municipal financial product. Note that even in the case of advice short of a recommendation, a subsequent communication that does constitute a recommendation requiring a suitability analysis might, depending on the particular facts and circumstances, require analysis at that time of a subject that was addressed in previous advice.

With regard to the recordkeeping requirements that would be required when providing a recommendation of a municipal securities transaction or municipal financial product, proposed MSRB Rule G-8(h)(iv) would require specifically that municipal advisors keep a copy of any document created by a municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any determination as to suitability for a period of not less than five years. The MSRB believes that the proposed recordkeeping requirements will allow regulatory examiners to efficiently assess a municipal advisor's compliance with the suitability obligations of Proposed Rule G-42. The MSRB also believes that the proposed recordkeeping requirements will not overly burden municipal advisors because the MSRB

understands that these documents are routinely made and retained by municipal advisors as a part of their normal business operations.

Suitability and Policy Related Considerations

In response to the First Request for Comment, BDA and Piper Jaffray stated that the factors to be considered by municipal advisors when determining whether a municipal securities transaction or municipal financial product is suitable for its municipal entity or obligated person client discussed in paragraph .08 (Suitability) of the Supplementary Material overlooks the effect that "policy and political considerations" could have on a suitability determination. Piper Jaffray requested that the MSRB clarify whether the determination of suitability should "incorporate the policy directives and decisions of the issuer at the time the issue is undertaken." BDA requested that the MSRB clarify that, if a municipal advisor's client states its objective, the municipal advisor, in making its recommendation, does not need to assess the appropriateness of the client's stated objective but could "generally accept the [objective]."

Section (a) and paragraph .01 of the Supplementary Material to Proposed Rule G-42 would require that municipal advisors exercise due care in performing their municipal advisory activities with respect to all of their clients. This duty would require, among other things, municipal advisors to provide their clients with informed advice. The MSRB believes that informed advice regarding the suitability of a municipal securities transaction or municipal financial product is the result of a municipal advisor making a reasonable inquiry into certain relevant information about the municipal advisor's client. For this reason, the MSRB has included in proposed paragraph .08 the requirement that a municipal advisor base its determination of suitability on any material information known by the municipal advisor after reasonable inquiry. Furthermore, proposed paragraph .09 of the Supplementary Material would

obligate a municipal advisor to know and retain the essential facts concerning its client to allow the municipal advisor to effectively service the client. The MSRB believes that policy considerations could be materially relevant information under all of the particular facts and circumstances that municipal advisors may consider when determining the suitability of a municipal securities transaction or municipal financial product. A stated objective of the client as BDA posits could be made most clear by reducing it to writing and including it in the relationship documentation on the scope of the engagement.

Evidencing Evaluations and Delivery of Required Information Regarding Recommendations

Several commenters, including BDA, MSA, Northland and Lewis Young, commented on records and documentation requirements of the proposed rule change that would be applicable to municipal advisors.

In response to the First Request for Comment, BDA requested clarification regarding what books and records a municipal advisor would need to maintain to evidence evaluations or recommendations made by the municipal advisor. BDA commented that some evaluations or recommendations could be delivered orally to a client and that requiring a municipal advisor to memorialize each recommendation or evaluation in writing could prove impractical and/or costly. MSA asked, in response to the First Request for Comment, whether the information regarding recommendations and evaluations of which a municipal advisor is required to "inform" its client could be "transmitted to the client orally or will each alternative require empirical evidence demonstrating the material risks, potential benefits, structure and characteristics?" If oral transmission is acceptable, MSA then asked whether it would need to be documented by both parties. Also in response to the First Request for Comment, Northland expressed concerns

regarding the Initial Draft Rule's requirement to discuss matters with the client, because it believed there is an implicit need to document these discussions therefore necessitating the use of written communications. However, Northland argued that written communications could result in a conflicting record that shows what the municipal advisor recommended as possibly in opposition to the course of action ultimately taken by its client. Northland was concerned that these potential conflicts could result in some exposure to liability in the event the justification of the decided upon course of action is challenged. Lewis Young contended that requiring municipal advisors, in section (d) of the Initial Draft Rule, to inform their clients of the risks and benefits of a particular structure or product when the client has already decided on a course of action (prior to engaging or seeking the advice of the municipal advisor) would yield little, if any, benefit. Lewis Young suggested only requiring the municipal advisor to inform its client of the matters discussed in section (d) when the client is considering, or presented with a recommendation of, a financial product, transaction or mechanism that is "novel to the client."

Proposed Rule G-8(h)(iv) would require a municipal advisor to maintain a copy of any document it created that was material to its review of a recommendation by another party or that memorializes the basis for any determination as to suitability. Section (d) of Proposed Rule G-42 would require a municipal advisor to inform its clients of the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is, or is not, suitable for the client; and whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively

serve the client's objectives. The MSRB notes that municipal advisors, under Proposed Rule G-42, would be required to "inform" their clients of such matters, rather than "discuss," as previously required under the Initial Draft Rule. Under Proposed Rule G-42, a municipal advisor would be allowed to choose the appropriate method in which to communicate its evaluation of the material risks and benefits attendant to the recommendation. The method selected and used by the municipal advisor must, however, comport with the duty of care and duty of loyalty (as applicable) that is owed to its client and should, therefore, result in the municipal advisor's client receiving timely, full and fair notification of the matters provided for in proposed subsections (d)(i)-(iii) and that adhere to the guidance provided in proposed paragraph .08 of the Supplementary Material.

Exemption from Suitability Standard, "Sophisticated" Issuers

In response to the First Request for Comment, First Southwest expressed general support for a suitability standard for recommendations by municipal advisors but stated that certain clients of municipal advisors are capable of independently evaluating recommendations of municipal advisors and these clients should be exempt from the suitability standard in a manner similar to the "sophisticated municipal market professional" under MSRB Rule G-48. Lamont voiced a similar concern stating that many of its "large sophisticated" issuer clients do not want, or need, a review of the transaction they have already decided to undertake. Lamont commented that these types of clients are "sufficiently capable of weighing the risks in a transaction and making their own decision about whether to proceed."

In response to the Second Request for Comment, SMA stated that when a municipal securities transaction or municipal financial product has been decided upon by a municipal advisor's client and: (a) is related to a project or event determined by the governing body of the

municipal entity or its citizens to be in its interest and consistent with its goals; (b) is permitted by state statute as determined by municipal or bond counsel; and (c) involves a transaction or product which the municipality has employed in the past, then it seems suitability has been determined and the advisor ought to be able to rely on these facts and the closing documents as establishing a reasonable basis for suitability. Southern MA suggested that a municipal advisor should not be put in the position of substituting its judgment as to the suitability of a municipal securities transaction or municipal financial product for that of the municipal policy makers, citizens or state lawmakers.

The MSRB has determined that the requirements of section (d), and the related paragraphs of the supplementary material, should be applicable regardless of the municipal advisor's perception of the sophistication of its client or the client's perception of its own degree of sophistication. The proposed rule change is aimed at protecting municipal entities, obligated persons and the public interest and, as a result, the MSRB believes that exemptions such as those described by these commenters would frustrate that objective. However, in designing Proposed Rule G-42, the MSRB did incorporate many of the concepts that commenters believed were indicia of the sophistication of an issuer into the factors to be considered when determining the suitability of a recommendation. Under those factors, the considerations proffered by SMA could be relevant to, and therefore be part of, a municipal advisor's suitability analysis depending on all of the particular circumstances, though they might not alone be sufficient to support a suitability determination under the proposed rule change.

Specified Prohibitions

Several commenters provided input on Proposed Rule G-42(e)(i), which sets forth certain activities in which municipal advisors would be prohibited from engaging.

General Comments

In response to the First Request for Comment, NAIPFA and GFOA expressed general support for the specified prohibitions, NAIPFA stated that the section includes prohibitions that are "important measures that are needed to eliminate certain practices that often carry unmanageable conflicts of interest inconsistent with Municipal Advisor fiduciary duties," and the prohibitions are appropriately tailored and would not impose undue regulatory burdens. Other commenters noted their general support for the prohibitions, but suggested some revisions or limitations, which are discussed in the section below.

Cooperman commented that the MSRB should determine, after a monitoring period since the passage of the Dodd-Frank Act, what, if any, abuses or inappropriate conduct remain that would require the regulation set forth in the proposed rule change. Alternatively, Cooperman suggested that the MSRB consider, at least initially, "limiting the [proposed rule] to an enumeration of prohibited forms of conduct and practices" rather than imposing extensive compliance, supervision and other requirements. In response to the Second Request for Comment, Lewis Young commented that the specified prohibitions subsections (e)(i) and (ii) (on the ban of certain principal transactions) are unnecessary because the matters addressed in those sections are adequately attended to in section (a) and should be intrinsic to a reputable municipal advisor's business practices. As such, Lewis Young recommended that these prohibitions be set forth in the supplementary material in order not to detract from the focus of the proposed rule. In response to such comments, the MSRB notes that, in many respects, Proposed Rule G-42 adopts a principles-based approach, enumerating prohibited forms of conduct and practice. However, regarding certain arrangements that the MSRB has identified as particularly prone to conflict

with, or risk of breach of, the fiduciary duty and duty of care, the MSRB believes that the proposed rule change appropriately incorporates more specific requirements and prohibitions.

Excessive Compensation

In response to the First Request for Comment, SIFMA, Lewis Young and MSA commented that the provision that would prohibit receiving compensation that is excessive in relation to the municipal advisory activities actually performed (now Proposed Rule G-42(e)(i)(A)), did not include a sufficiently clear standard for how excessive compensation would be determined and failed to provide adequate amount of guidance to facilitate compliance. SIFMA expressed concern that without a clear standard or more guidance, such determinations would be made in hindsight, presumably by financial regulatory examiners, and to the detriment of municipal advisors. Lewis Young called the prohibition unworkable, expressed concern that it would require advisors to document all of their work and requested that the paragraph be deleted. SIFMA and Lewis Young also commented that municipal advisor compensation is subject to market forces, and therefore its reasonableness should be determined by a negotiation between the client and the municipal advisor. PRAG stated that the proposed rule change fails to contemplate instances where transaction fees are included in a municipal advisor's compensation to compensate the municipal advisor for services that it has provided but that were unrelated to the issuance of municipal securities. SIFMA and Lewis Young asked whether the practice of including fees for services a municipal advisor provided, if not related to the issuance of municipal securities, would be permitted under the proposed rule change. Columbia Capital commented that the MSRB should strike the phrase "whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product," in paragraph .10 of the Supplementary Material of Proposed Rule G-42, and add, as an additional factor to be

considered when determining whether compensation is excessive, a comparison of the municipal advisor's compensation to other professionals providing services on the transaction in question.

After carefully considering the comments submitted in response to the First Request for Comment, the MSRB incorporated guidance regarding excessive compensation in paragraph .10 of the Supplementary Material of the Revised Draft Rule and solicited further comment. Paragraph .10 of Proposed Rule G-42 sets forth various factors that municipal advisors should consider when determining the reasonableness of their compensation. These factors include: the municipal advisor's expertise, the complexity of the municipal securities transaction or the financial product, whether the fee is contingent upon the closing of the transaction or financial product, the length of time spent on the engagement and whether the advisor is paying any other costs related to the transaction or financial product. Furthermore, Proposed Rule G-42 would prohibit receiving compensation that is excessive in relation to the municipal advisory activities actually performed. Depending on the facts and circumstances of a particular municipal advisory relationship, either or both of these provisions could apply to a scenario like that posited by PRAG. The proposed rule change, however, would not prescribe the source of funds that could be used to pay the municipal advisor for its services. Finally, the phrase regarding contingent fees is not deleted from paragraph .10 of the Supplementary Material as the MSRB believes it is a relevant factor and appropriately included in a non-exhaustive list of other relevant factors.

Inaccurate Invoicing

In response to the First Request for Comment, Wulff Hansen commented that the prohibition on the delivery of inaccurate invoices (now Proposed Rule G-42(e)(i)(B)) should be modified to clarify that it would apply only to any overstatements of fees, expenses or activities, and not to any fee discounting by a municipal advisor. SIFMA commented that the prohibition

should stand but should be modified to add materiality and knowledge qualifiers (i.e., a municipal advisor may not intentionally deliver a materially inaccurate invoice).

The MSRB believes that the proposed rule change clearly implies that offering a payment discount from the services actually performed is a permissible activity because a municipal advisor would be able to accurately describe such a discount on its invoice. In response to the SIFMA comment, the MSRB notes that the scope of inaccuracy targeted by the proposed provision is limited to the significant subjects of the services performed and personnel who performed those services, and the MSRB believes any inaccuracy in an invoice on those subjects should be proscribed. In addition, the MSRB believes that the addition to the proposed provision of the state-of-mind elements that SIFMA suggested would not sufficiently protect municipal entity and obligated person clients.

Prohibition on Fee-Splitting

The Initial Draft Rule included a prohibition on making or participating in any fee-splitting arrangement with underwriters, and any undisclosed fee-splitting arrangement with providers of investments or services to a municipal entity or obligated person client (now Proposed Rule G-42(e)(i)(D)). In response to the First Request for Comment, GFOA supported the fee-splitting prohibition in the Initial Draft Rule, noting that it "appears to be an inherent conflict, and should be avoided." NAIPFA supported the prohibition, but asked the MSRB to provide a definition of "fee-splitting arrangements," under which independent contractors and subcontractors would fall outside of the prohibition. Lewis Young and Winters LLC stated that fee-splitting arrangements should be disclosed but not prohibited. SIFMA commented that fee-splitting arrangements with affiliates, if fully and fairly disclosed, should be permissible. SIFMA stated that there could be legitimate reasons for such arrangements, including fee structures

requested by clients of an affiliate, and, with such disclosure, the parties should be free to engage in the fee arrangement believed to be most economical and efficient under the circumstances. NABL commented that the provision appears to apply to transactions even when the advice provided is exempted or excluded from that which would cause one to be a "municipal advisor" under the SEC Final Rule. Based on this assumption, NABL argued that the prohibition should apply only when a municipal advisor is giving "non-exempt" advice as part of the same transaction, not when it is giving advice that is exempt under the SEC Final Rule.

Several commenters provided examples of fee-splitting arrangements that they believed should not be prohibited. Cooperman stated that a municipal advisor should not be prohibited from outsourcing certain parts of its municipal advisory activities to independent contractors and subcontractors, including those that may have advisors on their staffs, when payment to those third parties is not dependent upon successful conclusion of the financing or payment to the municipal advisor of its fee. In addition, Cooperman stated the fee-splitting prohibition should not prevent two advisor firms from contracting with an issuer to perform services for a predetermined fee that is disclosed to the issuer. Lewis Young, who favored disclosure of fee-splitting in lieu of a complete prohibition, wrote that municipal advisors should be permitted to enter into a fee-splitting arrangement with a structuring agent that provides specific quantitative services on a transaction. Winters LLC asserted that a municipal entity or obligated person should be able to have its municipal advisor or other professionals (including underwriters, if after the underwriting period) receive compensation from investment providers or other service providers for providing oversight and performing other services so long as there is full and fair written disclosure of the fee-splitting or sharing arrangements. Lamont stated that allowing an investment provider to pay fees related to the solicitation of the investment by the municipal

advisor, and that are within the permitted limits of the Internal Revenue Service rules, should be acceptable as long as the payments are disclosed to the issuer and each investment provider on the bid list. Wulff Hansen asked whether it would be permissible under the provision for a municipal advisor to arrange for a routine purchase of services on behalf of the advised client in a transaction with an entity in which the advisor has an interest (e.g., a purchase of services from DTCC when the advisor is also a DTCC Participant and thus a part owner of DTCC). Finally, Piper Jaffray requested that the MSRB clarify that the fee-splitting prohibition, with regards to underwriters, applies to "any issue for which it is serving as municipal advisor" because the failure to link the prohibition to the actual advisory engagement could lead to unintended and adverse consequences.

The MSRB agrees with Piper Jaffray's comment and amended the provision in the Revised Draft Rule (now Proposed Rule G-42 (e)(i)(D)) to prohibit a municipal advisor from making or participating in any fee-splitting arrangement with underwriters on any municipal securities transaction as to which it has provided or is providing advice.

The MSRB believes that the proposed rule change would help prevent violations of fiduciary duties and the duty of care by clearly identifying and prohibiting specific fee-splitting arrangements that are particularly prone to conflict with such duties. Other fee-splitting arrangements would be permitted, provided they are fully and fairly disclosed.

Payments to Obtain/Retain an Engagement to Perform Municipal Advisory Activities

In response to the First Request for Comment, NABL commented that the Initial Draft Rule G-42 should not prohibit or require the disclosure of payments made to obtain or retain municipal advisory business, if those activities are engaged in by persons exempted from

registration as a municipal advisor under SEC Rule 15Ba1-1.[68] Similarly, the NY State Bar commented that the prohibition on making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities under subsection (g)(v) of the Initial Draft Rule (now proposed Rule G-42(e)(i)(E)) is unnecessarily restrictive with too narrow of an exemption. The NY State Bar stated that the provision should also permit payments to persons subject to comparable regulatory regimes (e.g., banks, trust companies, broker-dealers and investment advisors) as well as to affiliates of the municipal advisor so long as, in either case, the payments are disclosed to the client. SIFMA commented that the proposed rule should allow for reasonable fees to be paid to affiliates because soliciting on behalf of affiliates does not trigger a requirement for a person to register as a municipal advisor under the SEC Final Rule. In response to the Second Request for Comment, Sanchez made a similar comment. In addition, SIFMA commented that the prohibition should not cover expenditures for normal business entertainment expenses as well as marketing and sales activities.

In light of the comments received, the MSRB modified the provision (now Proposed Rule G-42(e)(i)(E)(1)) so that it would not specifically prohibit municipal advisors from making payments to an affiliate

> for a direct or indirect communication with a municipal entity or obligated person on behalf of the municipal advisor where such communication is made for the purpose of obtaining or retaining an engagement to perform municipal advisory activities….

The modification also would align the paragraph with Section 15B(e)(9) of the Exchange Act,[69] which allows affiliates of the municipal advisor to solicit on behalf of the municipal advisor

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68 17 CFR 240.15Ba1-1.

69 15 U.S.C. 78o-4(e)(9).

without triggering the municipal advisor registration requirement for the affiliate. The MSRB would clarify, in proposed subparagraph (e)(i)(E)(2), that a municipal advisor may pay reasonable fees to another municipal advisor registered as such with the Commission and the Board for making a similar communication on behalf of the municipal advisor making such payments. The MSRB would also clarify, in proposed subparagraph (e)(i)(E)(3), that payments that would qualify as permissible normal business dealings under current MSRB Rule G-20 also would not violate the prohibition. The revisions would harmonize the proposed rule change with relevant federal securities laws and rules.

Additional Comments on Specified Prohibitions

BDA and Piper Jaffray suggested adding two prohibitions to Proposed Rule G-42. In response to the First and Second Requests for Comment, Piper Jaffray suggested adding a specified prohibition that would prohibit a municipal advisor from taking into account whether it competes with other firms when the advisor makes a recommendation to its client (e.g., a recommendation to the client regarding which broker-dealer the client should hire as underwriter). In response to the First Request for Comment, BDA and Piper Jaffray suggested a second prohibition, which would prohibit a municipal advisor that is not also registered as, or affiliated with, a dealer, from using the term “independent,” if used in a manner intended to convey to potential clients that the municipal advisor is free from any potential conflicts of interest, and imply that, in contrast to advisors also registered as dealers, the municipal advisor would provide better advice. Piper Jaffray also stated that continued use of the term “independent” to connote an advisor free from conflicts should be specifically prohibited in light

of the issues its continued use could create if market participants confused such advisors with a person acting as an "independent registered municipal advisor" as used in the SEC Final Rule.[70]

The MSRB has not incorporated the prohibitions suggested by BDA and Piper Jaffray. To the extent the described conduct constitutes a material misrepresentation, the MSRB believes it is already appropriately addressed by Proposed Rule G-42 and existing MSRB Rule G-17, under which municipal advisors, in the conduct of their municipal advisory activities, must not engage in any deceptive, dishonest or unfair practice with any person.

Prohibition on Principal Transactions

The MSRB received extensive comments on the proposed provision to prohibit a municipal advisor (and its affiliates) from engaging in certain principal transactions (as defined in the proposed rule) with a municipal entity client of the municipal advisor ("prohibition on principal transactions" or "ban"). Specifically, Proposed Rule G-42(e)(ii) generally would prohibit a municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing, or has provided, advice.[71] Three related provisions of the proposed rule, subsection (f)(i) and paragraphs .07 and .11 of the Supplementary Material, would, respectively, define the phrase, "engaging in a principal transaction," clarify the relationship between the proposed ban and Rule G-23, and provide guidance regarding the term "other similar financial products" in connection

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70 See, e.g., SEC Final Rule, 78 FR at 67471.

71 In the Initial Draft Rule, the ban is set forth in section (f); in the Revised Draft Rule and the proposed rule change, the ban is set forth in subsection (e)(ii).

with principal transactions as defined in subsection (f)(i). Comments regarding the ban and the related provisions are discussed below.

General

In response to the First Request for Comment, many commenters raised concerns regarding: (1) the application of the ban to obligated person clients of municipal advisors; (2) the scope of the ban; (3) the meaning of "principal transaction" and "principal capacity;" (4) the ban's application to transactions by affiliates of municipal advisors; (5) the absence of an exception to the ban for an advisor or its affiliate based upon full and fair disclosure and the written consent of a client; and (6) the relationship between the ban and Rule G-23. In response to the Second Request for Comment, most of the comments focused on: (1) the scope of principal transactions that would be considered "directly related" to the advised transaction and come within the ban; (2) the ban's application to transactions by affiliates of municipal advisors; and (3) the relationship between the ban and Rule G-23.

Ban Does Not Apply to Obligated Person Clients

In the Initial Draft Rule, the ban prohibited a municipal advisor and its affiliates from engaging in principal transactions with municipal entity and obligated person clients. The ban in Proposed Rule G-42(e)(ii) no longer would apply to principal transactions with obligated person clients. As a result, the comments urging that the ban not apply to obligated persons are not incorporated in this discussion, except to note that such comments were considered and the MSRB modified the proposed ban such that it would not apply to principal transactions with such persons.

Scope and "Directly Related To"

In Initial Draft Rule G-42, the prohibition on principal transactions was significantly broader than the ban as modified in the Revised Draft Rule and as further narrowed in this proposed rule change. In the Initial Draft Rule, a municipal advisor (and its affiliates) generally were prohibited from engaging in any transaction in a principal capacity to which an obligated person client or a municipal entity client of the municipal advisor would be the counterparty. In response to the First Request for Comment, many commenters[72] interpreted the proposed prohibition quite broadly and expressed concerns regarding the scope of the proposed prohibition on principal transactions by municipal advisors (and their affiliates) with the clients of such municipal advisors.[73] Commenters, including ABA, BDA, NABL and Piper Jaffray, interpreted the ban as covering activities and transactions that were unrelated to the municipal advisory relationship. The ABA commented that "because banks almost always provide banking products and services in a principal capacity, the prohibition would prevent commercial banks and their affiliates from providing any other banking products, such as deposit accounts, loans, or cash

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72 Commenters that expressed such concerns include ABA, BDA, Cape Cod Savings, Coastal, Frost, GFOA, GKB, JP Morgan, Kutak, NABL, NY State Bar, Parsons, Piper Jaffray, SIFMA and Zion.

73 SIFMA suggested narrowing the proposed provision to:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the advice rendered by such municipal advisor (emphasis added).

BDA suggested the following alternative:

> A municipal advisor, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction with a municipal entity client if the structure, timing or terms of such principal transaction was [sic] established on the advice of the municipal advisor in connection with a municipal advisory relationship with such municipal entity client.

management services . . . despite the fact that these products and services are exempt from the municipal advisor regulatory regime." BDA, Frost, SIFMA and Zion, among others, raised similar concerns regarding the broad reach of the prohibition.

After carefully considering the comments, the prohibition on principal transactions was significantly narrowed and clarified, as set forth in Revised Draft Rule G-42(e)(ii). The MSRB limited the ban to "a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice" (emphasis added). The Revised Draft Rule would thus prohibit a municipal advisor (and its affiliates) to a municipal entity client from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice. The modification was designed to exclude many of the transactions that some commenters read as potentially covered by the Initial Draft Rule, including the taking of a cash deposit or the payment by a client solely for professional services.

In response to the Second Request for Comment, some commenters supported the changes to the proposed rule text. Several other commenters continued to raise concerns regarding what they believed to be the overly broad scope of the ban. Conversely, one commenter stated that the ban in Revised Draft Rule G-42(e)(ii) had become too narrow. GFOA approved of the modification narrowing the proposed ban to "a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice," and Wells Fargo noted that the modification mitigated the impact of the proposed ban. ABA also welcomed the revision, but suggested additional changes. In addition, BDA, NY State Bar, Piper Jaffray and SIFMA suggested that the ban be modified further to narrow or clarify the scope of the ban. ABA recommended that the

provision require the advice provided by the municipal advisor be provided pursuant to a municipal advisory relationship; NY State Bar recommended that the prohibition not apply where the municipal advisor does not make a recommendation to the municipal advisory client to enter into a transaction with the advisor or its affiliate; and SIFMA recommended that the provision ban only those principal transactions that are directly related to the advice the municipal advisor is providing, not merely the same municipal securities transaction or municipal financial product in connection with which the advice is provided. [74] BDA and Piper Jaffray commented that the term "directly related" was unclear, and recommended alternative language. In Piper Jaffray's view, the ban should be limited to a transaction or issuance where a firm served as a municipal advisor and about which advice was rendered. Alternatively, Piper Jaffray suggested that the ban should cover transactions "directly related to the advice given rather than directly related to the transaction itself." Applying the proposed "directly related to" standard to certain hypothetically paired transactions, BDA asked whether one of each pair of such transactions would be considered directly related to the second transaction and therefore

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[74] In response to the Second Request for Comment, ABA recommended the provision be modified to read:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice <u>pursuant to a municipal advisory relationship</u>.

SIFMA recommended the provision be modified to read:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from knowingly engaging in a [prohibited] principal transaction.

subject to the proposed prohibition, and also proposed a modification to the ban.[75] Conversely, Lewis Young argued that, with the changes set forth in the Revised Draft Rule, the scope of the prohibition on principal transactions has gone from "too broad to too narrow" because the definition of "engaging in a principal transaction" (discussed in greater detail below) does not extend fully to the variety of principal transactions in which a municipal advisor could engage, which would be in conflict with its municipal advisory role and fiduciary duty (e.g., a bank loan as a substitute for an issuance of municipal securities).

The principal transactions ban is incorporated in the proposed rule change as Proposed Rule G-42(e)(ii). The MSRB has determined not to narrow, broaden or otherwise modify the standard--"directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice"--in response to the comments received. The MSRB believes that the various alternative rule texts proposed by commenters would not be more effective or efficient means for achieving the stated objective of Proposed Rule G-42(e)(ii), which is to eliminate a category of particularly acute conflicts of interest that would arise in the fiduciary relationship between a municipal advisor and its municipal entity

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[75] In connection with interpreting the scope of the "directly related to" standard, BDA asked whether: (1) selling securities as a principal after winning a competitive bid for an open market refunding escrow on a refunding bond issue for which the firm was a municipal advisor would be a transaction "directly related to" the refunded bond issue and therefore a prohibited principal transaction; (2) acting as the underwriter on a series of variable rate bonds would be directly related to acting as the municipal advisor for a related swap, and be prohibited; and, (3) underwriting a refunding issue years after serving as a municipal advisor for the initial issue would be a transaction that would be considered directly related to the initial issue and prohibited.

BDA recommended the provision be modified to delete the "directly related to" standard and substitute: "if the structure, timing or terms of such principal transaction was established on the advice of the municipal advisor in connection with a municipal advisory relationship with such municipal entity client."

client. The alternatives offered by various commenters are similar in that they would seek to limit the scope of prohibited transactions to those pertaining to the advice rendered by the municipal advisor. If adopted, such a change could leave transactions that have a high risk of self-dealing insufficiently addressed. For example, a municipal advisor that provided advice to a municipal entity regarding the timing and structure of a new issuance arguably would not be prohibited from acting as principal in entering into an interest rate swap for the same issuance so long as the advisor refrained from advising on the swap. In addition, in response to the comments that the standard would continue to raise questions whether a transaction was prohibited under Proposed Rule G-42(e)(ii) and the suggestion that the MSRB further amend the provision to clarify the provision, the MSRB does not believe it would be feasible or desirable, given the principled nature of the provision, to specify in advance its application in all circumstances. As noted above, the proposed principal transactions ban is revised to clarify that the prohibition applies both to principal transactions that occur while the municipal advisor is providing advice with respect to a directly related municipal securities transaction or municipal financial product, and after the municipal advisor has provided such advice.

"Engaging in a Principal Transaction" and "Other Similar Financial Products"

In response to the First Request for Comment, certain commenters, including GFOA, NAIPFA, SIFMA and Wulff Hansen, commented that the MSRB should provide additional guidance regarding the meaning of various terms (e.g., "principal capacity" and "principal transaction") for purposes of interpreting the proposed prohibition on principal transactions. Several commenters, including GFOA, Wulff Hansen and First Southwest, sought clarification regarding the types of transactions that would constitute principal transactions. For example, the GFOA requested that the MSRB provide examples of prohibited and acceptable practices; Wulff

Hansen asked that the MSRB specify whether the sale of other additional municipal advisory or related services would constitute a prohibited principal transaction; and First Southwest asked whether a municipal advisor that also facilitates private placements would be engaged in a principal transaction.

In response to comments, the Revised Draft Rule G-42(f)(i) added, for purposes of the Revised Draft Rule, a defined term, "engaging in a principal transaction" to mean: "when acting as principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client."

In response to the Second Request for Comment, ABA and GFOA expressed support for the proposed defined term. Another commenter, Sanchez, asked the MSRB to include a non-exhaustive list of specific common roles (such as underwriter) in addition to the general description. NY State Bar recommended two significant changes intended to narrow the scope of the prohibition and the definition of principal transaction: (1) the "somewhat open-ended" phrase "other similar financial product" should be amended to refer exclusively to municipal financial products, as defined in the Exchange Act; and (2) the definition of "engaging in a principal transaction" should be amended to make clear that the term does not include any of the banking activities as to which a bank may provide advice without being registered as a municipal advisor pursuant to the exemption in the SEC Rule 15Ba1-1(d)(3)(iii),[76] including holding investments in a deposit or savings account, certificate of deposit or other deposit instrument issued by a bank; extensions of credit by a bank to a municipal entity or obligated person, including the issuance of a letter of credit; the making of a direct loan, or the purchase of a municipal security

[76] 17 CFR 240.15Ba1-1(d)(3)(iii).

by the bank for its own account; holding funds in a sweep account; or investments made by a bank acting in the capacity of an indenture trustee or similar capacity.

In response to comments filed regarding the Second Request for Comment, including Lewis Young's, the proposed rule would provide additional guidance regarding the term, "other similar financial products." Proposed Supplemental Material paragraph .11 would provide that, as used in Proposed Rule G-42(f)(i), "other similar financial products," "includes a bank loan, but only if it is in an aggregate principal amount of $1,000,000 or more and it is economically equivalent to the purchase of one or more municipal securities." The MSRB notes that the term "other similar financial products" is not limited to refer exclusively to municipal financial products, as defined in the Exchange Act, in that a fiduciary's obligation to its client -- not to engage in principal transactions in which the fiduciary's financial interests and concerns conflict with those of the client -- is not so limited. For the same reason, the MSRB has determined not to limit the scope of banned transactions, which are covered based generally on conflicts principles, to the category of transactions as to which advising triggers a registration requirement as a municipal advisor.

Exceptions to Ban

In the First Request for Comment, the MSRB specifically sought comments on whether a ban on principal transactions by municipal advisors was the appropriate regulatory approach, or whether a municipal advisor should be permitted to engage in certain types of principal transactions with its client, with full and fair disclosure and written client consent, and, if so, what types of principal transactions should be allowed.

In response to the First Request for Comment, several commenters, including ABA, First Southwest, Frost, GKB, Kutak, JP Morgan, NABL and SIFMA, expressed concerns regarding

what they viewed as the overly broad prohibition on principal transactions between municipal advisors and their clients. Several commenters, including the ABA, Cape Cod Savings, Frost, NABL, SIFMA and Zion, stated that the prohibition could do a disservice to municipal entities by unnecessarily and substantially restricting the choices available to municipal entities that engage their municipal advisors (or their affiliates) in other types of transactions that would be prohibited by the Initial Draft Rule. In addition, several commenters, including ABA, Kutak, NABL, Parsons, SIFMA, Sutherland and Wells Fargo, believed that a municipal advisor should be permitted to engage in certain types of principal transactions with its clients if the municipal advisor provides its client with full and fair disclosure and then receives informed consent from the client. NABL stated that the proposed ban would conflict with common law, under which an agent's fiduciary duties of loyalty and care could be waived or otherwise modified by the principal if the principal is not legally incompetent. Kutak commented that the Initial Draft Rule should not prohibit all principal transactions with municipal entities when the client is sufficiently sophisticated to adequately assess the risks of the transactions. Kutak believed transactions involving an investment in an instrument where an established market exists and a municipal entity client could readily ascertain the reasonableness and fairness of the price should be allowed under the Initial Draft Rule.

Also, multiple commenters, including ABA, Kutak, NABL and SIFMA (in response to the First Request for Comment) and FSR and Zion (in response to the Second Request for Comment), noted that under Section 206(3) of the Investment Advisers Act and other regulatory regimes, certain principal transactions are permitted based upon full and fair disclosure and client

consent.[77] The commenters suggested that a similar mechanism should be included in the ban that would allow municipal advisors to engage in principal transactions with their municipal entity clients, subject to similar disclosure and consent requirements. NABL also commented that, if the MSRB adopted a provision that was consistent with the SEC's guidance under the Investment Advisers Act regarding an exception to a ban based on disclosure and informed consent, the MSRB should provide clear guidance to market participants to avoid confusion.

In contrast, commenters Lewis Young and NAIPFA supported the proposed ban on principal transactions and did not recommend creating exceptions or narrowing its scope. Lewis Young commented that the ban was appropriate, stating that a party cannot be both a fiduciary and a principal party in a buyer/seller relationship if the sale is an asset, financial product or something other than services that are compatible with the fiduciary role.

The MSRB carefully considered the comments received that urged the MSRB to include one or more exceptions to the prohibition on principal transactions. After considering the fiduciary duty of the municipal advisor in its relationship to a municipal entity client and the possibilities for self-dealing, the MSRB believes that the proposed prohibition on principal transactions is sufficiently targeted and should be retained. In addition, the MSRB believes that

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77 See 15 U.S.C. 80b-6 and the rules adopted thereunder, which prohibit an adviser, acting as a principal for its own account, from knowingly selling any security to or purchasing any security from a client for its own account, without disclosing to the client in writing the capacity in which it (or an affiliate) is acting and obtaining the client's consent before the completion of the transaction.

SIFMA also referred to the regulation of swap dealers and security-based swap dealers that also serve as advisors to Special Entities (which includes municipal entities) under the CEA. See 7 U.S.C. 1 et seq. According to SIFMA, the CEA does not preclude such advisors from entering, in a principal capacity, into derivatives transactions with the Special Entities that they advise, including municipal entities, subject to the duty of the advisor to act in the best interests of the Special Entity.

exceptions to the prohibition based on disclosure and client consent, even if limited to sophisticated municipal entities, would not sufficiently protect municipal entity clients from potential self-dealing-related abuses. The prohibition has been narrowed to ban only those transactions that (1) are "directly related" to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice and (2) are purchases or sales of a security or involve entering into a derivative, guaranteed investment contract, or other similar financial product with the municipal entity client (as discussed, supra). In the MSRB's view, the prohibition on principal transactions should not at this juncture be modified or narrowed, given the acute conflicts of interest presented and the risk of self-dealing by a regulated entity (or its affiliate).[78]

Affiliates

In response to the First Request for Comment, a number of commenters commented on the ban's coverage of principal transactions by affiliates of a municipal advisor, including ABA, Frost, JP Morgan, Parsons, Piper Jaffray, SIFMA, Wells Fargo and Zion.

The ABA, SIFMA and other commenters commented generally that other fiduciary regimes do not prohibit all affiliates of a fiduciary from engaging in principal transactions with

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[78] Similar concerns regarding conflicts of interests arising when a regulated entity would provide financial advice to a municipal issuer and also serve as underwriter were raised by the MSRB and commenters in connection with SR-MSRB-2011-03, a proposed rule change to amend MSRB Rule G-23 relating to the activities of financial advisors, which was approved by the Commission. See Exchange Act Release No. 64564 (May 27, 2011), 76 FR 32248, 32249 (June 3, 2011) (order approving File No. SR-MSRB-2011-03) ("[T]he proposed rule change resulted from a concern that a dealer financial advisor's ability to underwrite the same issue of municipal securities, on which it acted as financial advisor, presented a conflict that is too significant for the existing disclosure and consent provisions of Rule G-23 to cure. Even in the case of a competitive underwriting, the perception on the part of issuers and investors that such a conflict might exist was sufficient to cause concern that permitting such role switching was not consistent with 'a free and open market in municipal securities'" (emphasis added)).

the party owed the fiduciary duty. Wells Fargo also sought to limit the coverage of the ban, commenting that the ban should not apply to certain affiliates. In Wells Fargo's view, affiliates of large financial institutions often offer substantially different services, operate with distinct governance structures and employ information barriers, and, in such instances, if a non-municipal advisor affiliate is not connected to the municipal advisor relationship, the risk of a conflict of interest in a principal transaction between a municipal advisor client and the non-municipal advisor affiliate is significantly diminished. Wells Fargo suggested that the MSRB not apply the ban to affiliates or, at a minimum, limit the ban to principal transactions of affiliates that are directly related to the municipal advisory relationship that the municipal advisor affiliate has with the client. ABA, NABL, SIFMA, Wells Fargo, Zion and other commenters generally expressed concerns related to regulating conduct of affiliates of municipal advisors, specifically the imposition of compliance burdens on the affiliates and possible unintended consequences to clients if certain products and services offered by affiliates of the municipal advisor were no longer available to clients. ABA and NABL commented that the MSRB does not have apparent authority to regulate the conduct of affiliates of municipal advisors that are not brokers, dealers or municipal securities dealers, and thus, any ban should be narrowly-tailored and addressed to the municipal advisor's right to advise, rather than its affiliates' rights to engage in unrelated transactions.

In response to the Second Request for Comment, ABA, FSR, SIFMA and Wells Fargo included significant comments that focused on the ban's application to transactions by affiliates. With respect to affiliates, among the concerns raised was the difficulty that municipal advisors and their affiliates might have in identifying transactions that are related to an advised transaction, particularly within large organizations, and the likely significant cost of compliance.

Commenters, such as SIFMA and Wells Fargo, also questioned the value of extending the prohibition to affiliates of a municipal advisor, stating that, in scenarios where the affiliate has no knowledge of the municipal advisory relationship, or where the municipal advisor has no knowledge of an affiliate's contemplated principal transaction, the parties would not be likely to engage in self–dealing or profit from the affiliation.

SIFMA suggested that the MSRB include the emphasized modifier in subsection (e)(ii) as follows: "A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from knowingly engaging in a principal transaction . . . ." (emphasis added), which is the same modifier contained in the provision on principal transactions in the Investment Advisers Act.[79] Wells Fargo suggested a modification to exempt municipal advisor affiliates operating with information barriers, stating that such entities are unlikely to engage in the self-dealing that the rule is aimed at preventing.

After considering the fiduciary duty of the municipal advisor in its relationship to a municipal entity client and the risk of self-dealing, the MSRB believes that the proposed prohibition on principal transactions, including its application to affiliates, is sufficiently targeted. In the MSRB's view, the proposed prohibition should be retained without exceptions, including one based on disclosure and consent, for the reasons set forth above, given the acute nature of the conflicts of interest presented and the risks of self-dealing by affiliates in transactions that are "directly related" to the same municipal securities transaction or municipal financial product as to which the affiliated municipal advisor is providing or has provided advice. Significantly, the prohibition is limited to certain types of transactions (i.e., purchases or sales of a security or those involving entering into a derivative, guaranteed investment contract,

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[79] See 15 U.S.C. 80b-6(3).

or other similar financial product). Finally, in connection with affiliates, if the prohibition on principal transactions were modified by "knowingly," the MSRB believes the standard would be overly stringent, which could hinder regulatory examinations and enforcement.

Relationship between the Ban and Rule G-23

In the First Request for Comment, the ban prohibiting municipal advisors (and their affiliates) from engaging in principal transactions with the municipal advisor's clients included the exception: "Except for an activity that is expressly permitted under [MSRB] Rule G-23" ("Rule G-23 exception"). The Rule G-23 exception was included to address the interrelationship between the proposed specific prohibition on principal transactions in Initial Draft Rule G-42 and principal transactions that are permitted by underwriters under Rule G-23.

Commenters sought clarity regarding the relationship between Rule G-23 and the prohibition on principal transactions in the Initial Draft Rule. In response to the First Request for Comment, commenters asked whether the prohibition on principal transactions was in conflict with principal transactions discussed in Rule G-23, under which a municipal advisor could acquire, as a principal, all or any portion of an issuance of municipal securities for which the municipal advisor had provided advice, as long as the municipal advisor complied with Rule G-23. BDA and GKB noted that, although the provision in the proposed ban referenced an exception for activities that are expressly permitted under Rule G-23, it was unclear what principal transactions would be permitted. Lamont commented that MSRB rules applicable to municipal advisors should not conflict with MSRB rules applicable to dealers regarding principal transactions, observing that, in its view, a fiduciary duty to the issuer will require additional steps to ensure that the pricing has been at least as favorable as having a third party in the transaction.

After careful consideration of the comments, the MSRB developed the Revised Draft Rule to clarify the relationship between the proposed ban on principal transactions and those principal transactions currently permitted under Rule G-23. Specifically, paragraph .07 to the Supplementary Material of the Revised Draft Rule described the Rule G-23 exception to the ban, providing that subsection (e)(ii) would not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities, provided that the municipal advisor complied with the requirements of Rule G-23. Thus, the Rule G-23 exception was more clearly described using the particular terminology in Rule G-23, rather than solely cross-referencing Rule G-23.

Several of the comments received in response to the Second Request for Comment continued to seek clarification regarding the Rule G-23 exception, desiring to avoid confusion regarding any express and direct conflict between the ban and Rule G-23. GFOA sought additional amendments to paragraph .07 of the Supplementary Material, seeking to "ensure that no component of a final Rule on G-42 removes the authority of issuers to decide for themselves how they utilize a [municipal advisor] or underwriter on a transaction so long as compliance with MSRB Rule G-23, MSRB Rule G-42 and the SEC's Municipal Advisor Rule are maintained." In BDA's view, the Revised Draft Rule language did not clarify the provision compared with the prior language regarding when a municipal advisor could act as a principal on the same transaction for which it is providing advice.

Sanchez appeared to interpret the provision to mean that a transaction permitted by Rule G-23 would be deemed in all cases to be lawful vis-a-vis other requirements under proposed Rule G-42 (such as the duty of loyalty) and under other laws (such as the statutory fiduciary

duty). Columbia Capital commented that the sentence regarding the Rule G-23 exception in paragraph .07 of the Supplementary Material should be deleted because it "contemplates a situation where an MA could serve as a principal in a transaction for which it provides MA services, creating a conflict" with the proposed prohibition on principal transactions. Finally, ABA commented that the clarification regarding the conflict between Rule G-23 and draft Rule G-42(e)(ii) is unnecessary, or, if the clarification is retained, the phrase, "provided that the municipal advisor complies with all of the provisions of Rule G-23," should be deleted and the phrase, "provided that such a transaction is not prohibited by the provisions of Rule G-23," should be incorporated.

The MSRB notes that the purpose of the sentence regarding the Rule G-23 exception in paragraph .07 of the Supplementary Material is to avoid a potential inconsistency in the MSRB's rules by providing specifically in Proposed Rule G-42, until such time as the MSRB may further review and potentially revise Rule G-23, that the specific ban on principal transactions in proposed subsection (e)(ii) does not prohibit a type of principal transaction that is already addressed and prohibited to a certain extent by Rule G-23. To further clarify this point, and respond to the comment by ABA, the MSRB has deleted the phrase "provided that the municipal advisor complies with all the provisions of Rule G-23" from the end of paragraph .07, and substituted the phrase "that is a type of transaction that is addressed by Rule G-23." Also, in response to the comments requesting additional clarification, the MSRB has included the phrase "on the basis that the municipal advisor provided advice as to the issuance." Proposed paragraph .07 of the Supplementary Material, as revised, would provide:

> In addition, the specific prohibition in subsection (e)(ii) . . . shall not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal

> securities on the basis that the municipal advisor provided advice as to the issuance because that is a type of transaction that is addressed and prohibited in certain circumstances by Rule G-23 (emphasis added).

The MSRB cautions that this provision is quite limited, providing an exception only to the specific prohibition in subsection G-42(e)(ii); and it would not mean, for example, that a transaction not prohibited by Rule G-23 is deemed in all cases to be lawful vis-a-vis all other requirements under Proposed Rule G-42 (such as the duty of loyalty) and under other laws (such as the statutory fiduciary duty).

Inadvertent Advice – Supplementary Material .06

In response to the Second Request for Comment, several commenters expressed concerns and suggested changes to the inadvertent advice exclusion in paragraph .06 of the Supplementary Material to the Revised Draft Rule. First, NAIPFA believed the paragraph impermissibly creates an additional exemption from the Commission's definition of the term "municipal advisor" and is inconsistent with Rule G-23, allowing broker-dealers to provide advice to municipal entities and obligated persons as municipal advisors without becoming subject to corresponding fiduciary responsibilities and ultimately allowing such municipal advisors to serve as underwriters of the securities being issued. Similarly, WM Financial believed paragraph .06 negated Rule G-23 and effectively allowed broker-dealers to serve as municipal advisors and then switch to serving as underwriters, undermining the definition of "municipal advisor" and the exemptions thereto provided by the SEC. Contrary to NAIPFA and WM Financial, Sanchez stated that "it appears reasonably clear at the moment that Supplementary Material .06 is only intended to provide relief from subsections (b) and (c) of Proposed Rule G-42;" however, he believed it would be useful for the MSRB to also include an affirmative statement that even inadvertent advice is subject to all other rules and requirements applicable to municipal advisory

activities and financial advisory relationships entered into by broker-dealers under Rule G-23, Commission rules, and the fiduciary duty set forth in the Exchange Act.

NAIPFA and WM Financial misinterpreted the safe harbor provided by paragraph .06 as broadly relieving a municipal advisor of other regulatory requirements. To address such confusion, the MSRB has revised paragraph .06 of the Supplementary Material to include a clarifying statement that the relief the paragraph provides "has no effect on the applicability of any provisions" of Proposed Rule G-42, other than sections (b) and (c) (relating to documentation of the municipal advisory relationship and the disclosure of conflicts of interest, respectively) or any other legal requirements applicable to municipal advisory activities, which would include, but are not limited to, SEC rules and Rule G-23.

Second, SIFMA suggested that the MSRB broaden the limited safe harbor provided by paragraph .06 to relieve municipal advisors that inadvertently engage in municipal advisory activities from compliance with section (d) and subsection (e)(ii) of the Revised Draft Rule. Section (d) would require a suitability analysis of recommendations made by the municipal advisor or by a third party while subsection (e)(ii) would prohibit principal transactions directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice. The MSRB believes that, despite inadvertently engaging in municipal securities activities, a municipal advisor should not be relieved of complying with the suitability analysis requirement to the extent the municipal advisor made or reviewed a recommendation as contemplated by Proposed Rule G-42(d). Further, the MSRB does not believe, as SIFMA suggested, that firms would be less likely to perform the disclaimer process under paragraph .06 because doing so would not permit them to engage in a principal transaction prohibited under Proposed Rule G-42(e)(ii). Specifically, use of

the exemption under paragraph .06 would only relieve a municipal advisor of compliance with the requirements of Proposed Rule G-42(b) and (c), and the prohibition on principal transactions would apply to the municipal advisor regardless. Therefore, the MSRB has not revised paragraph .06 in response to these comments.

Third, NAIPFA highlighted the importance of prompt use of the safe harbor provided by paragraph .06, suggesting that the proposed rule require utilization within ten days of discovery of the inadvertent advice. The MSRB has not prescribed a strict time frame for when the documentation must be provided by the municipal advisor beyond the general "promptly" standard, as doing so would create an arbitrary bright line that would be of limited benefit to municipal advisors or their clients. In response to the comment and to ensure that municipal advisors seeking to obtain the relief provided under paragraph .06 do so in a timely manner after having discovered that they inadvertently provided advice, the MSRB modified paragraph .06 to require municipal advisors to provide the documentation it prescribes "as promptly as possible after discovery" (emphasis added).

Fourth, SIFMA noted that there are circumstances in which a registered municipal advisor could be engaged in municipal advisory activities for some clients, but inadvertently provide advice to another client, and, therefore, could not state that it "has ceased engaging in municipal advisory activities" to comply with paragraph .06. In response to the comment, the MSRB has revised the disclaimer required by subparagraph (a) of paragraph .06 of the Supplementary Material to state that, effective immediately, the municipal advisor has ceased engaging in municipal advisory activities "with respect to that municipal entity or obligated person in regard to all transactions and municipal financial products as to which advice was inadvertently provided . . . ." (emphasis added). This revision would clarify that the municipal

advisor is not required to cease all municipal advisory activities to obtain the relief provided by paragraph .06.

Fifth, NAIPFA highlighted the importance of the identification of the inadvertent advice, suggesting requiring the identification of absolutely all of the inadvertent advice. In response to this comment, the MSRB revised subparagraph (c) of paragraph .06 to require that the municipal advisor identify all of the advice that was provided inadvertently, based on a reasonable investigation. This objective standard for the investigation would avoid requiring municipal advisors to go to impractical lengths to ensure that all inadvertent advice was identified, and the MSRB believes this would be sufficient to allow municipal advisor clients to assess risk exposure from any reliance on the advice and determine what potential mitigating actions need to be taken.

Finally, SIFMA suggested that the MSRB should carve out an exception for all advice that is incidental to brokerage/securities execution services. In the MSRB's view, SIFMA's request, as noted above, is a request that the MSRB interpret the SEC Final Rule and the definition of "municipal advisor," therein. The authority to interpret the Commission's rule lies with the Commission and the request should be directed to the Commission. As such, the MSRB declines to revise paragraph .06 of the Supplementary Material in this manner.

Trigger for Municipal Advisor Relationship

Subsection (f)(vi) would define "municipal advisory relationship" for purposes of Proposed Rule G-42 and states that a municipal advisory relationship will "be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person." In response to the Second Request for Comment, Columbia Capital objected to the deletion of "engages" from the definition of "municipal

advisory relationship" in subsection (f)(vi) of the Revised Draft Rule. Specifically, Columbia Capital stated that, "[i]f a person provides 'advice' he/she should trigger the [municipal advisor] duties at the time of providing that advice and should be considered [a municipal advisor] unless that person qualifies for an exemption or exclusion at the time such advice is provided." Under the proposed rule change, the municipal advisory relationship would begin at the time a municipal advisor enters into an agreement to engage in municipal advisory activities, which then triggers the documentation requirements of Proposed Rule G-42(c).

The MSRB believes Columbia Capital's concern is moot because the other duties required by Proposed Rule G-42, including, but not limited to, providing written disclosures to clients, would be triggered when a municipal advisor engages in municipal advisory activities. The MSRB also notes that engaging in municipal advisory activities would subject a firm to municipal advisor registration requirements and any other legal requirements applicable to municipal advisory activities. Accordingly, the MSRB has not revised subsection (f)(vi) of the Revised Draft Rule, as incorporated into the proposed rule, in response to this comment.

Economic Analysis of Comments on Economic Implications of Proposed Rule

Economic Analysis – Cost of Compliance

Several commenters stated that the cost of complying with the proposed rule would be "burdensome" or "significant." In some cases, commenters identified alternative approaches that they considered to be less costly. No commenter provided specific cost information or data that would support an improved estimate of the costs of compliance.

FSR and SIFMA both stated that the requirement on municipal advisors to provide disclosure of all material conflicts of interest including any of its affiliates that provides any advice, service, or product directly or indirectly related to performing municipal advisory

activities would be burdensome, particularly for municipal advisors that are part of large financial conglomerates. Sanchez commented that a "written statement" would be less burdensome than "written documentation" when municipal advisors conclude that material conflicts of interest exist. FSR, SIFMA, and Sanchez commented that the detailed disclosure of disciplinary events material to the client's evaluation of the municipal advisor could be accomplished at a lower cost by allowing municipal advisors to reference the documentation provided to the SEC on Forms MA and MA-I. Columbia Capital requested that the MSRB consider allowing municipal advisors to use more than one document to meet the requirement for documentation of the municipal advisory relationship.

The MSRB agrees that municipal entities and obligated persons can be made aware of relevant conflicts of interest at a lower cost by revising some of the requirements. To that end, the MSRB amended Proposed Rule G-42(b)(i)(A) to narrow the scope of potential conflicts that would need to be disclosed from those that "might" impair the advisor's ability to provide advice to those that "could reasonably be anticipated to impair" the advisor's ability and Proposed Rule G-42(b)(i)(B) to remove the requirement to disclose potential conflicts that might arise from advice, service, or products provided by affiliates and indirectly related to the performance of municipal advisory activities. The MSRB also amended Rule G-42(b)(i) to allow for a written statement instead of written documentation if a municipal advisor concludes that no known material conflicts of interest exist. The MSRB also agrees that information regarding disciplinary events may be disclosed by identification of the specific type of the event and specific reference to the relevant portions of Forms MA and MA-I and has amended Proposed Rule G-42(b)(ii) to reflect this. Finally, the MSRB has clarified that a municipal advisor may use

multiple documents to document the relationship by adding the plural "writings" to Proposed Rule G-42(c).

Economic Analysis – Transition Period

Lewis Young urged the MSRB to adopt a transitional period to permit advisors to honor their existing financial advisory agreements. They stated that many financial advisory agreements are longer-term arrangements and that advisors should be provided with a reasonable opportunity to conform existing arrangements to the requirements of the proposed rule when they are renewed or after a reasonable phase-in period after the rule is finalized. Zion also urges the MSRB to include a transitional provision to permit advisors to honor existing contracts, including many that are multi-year contracts. Zion notes the significant time, effort, and expense that would be involved to supplement or amend existing contracts with additional content and disclosure required by the proposed rule. Zion states that under particular state and/or local procurement laws, the alterations to existing agreements may reopen the request for proposal process for issuers to hire municipal advisors, requiring additional (and significant) time, effort, and expense.

The MSRB believes that the required disclosure can generally be accomplished without formal amendments and, therefore, that the costs imposed will be less significant than generally anticipated.

Economic Analysis – Burden on Small Municipal Advisors

MSRB did not receive any comments specific to the Dodd-Frank Act requirement that MSRB rules not impose a regulatory burden on small municipal advisors that is not necessary or

appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons provided that there is robust protection of investors against fraud.[80]

Nonetheless, the MSRB has been sensitive to the potential impact of the requirements contained in Proposed Rule G-42. To that end, the MSRB has made efforts to minimize costs, particularly those that might be expected to disproportionately impact smaller firms. In addition to the amendments discussed above that will reduce compliance costs, the MSRB has made changes to proposals included in prior Requests for Comment such as clarifying the obligations owed by municipal advisors to obligated persons, narrowing the circumstances under which disclosures related to the municipal advisory relationship and compensation arrangements need to be made, and removing disclosure requirements related to professional liability insurance.

The MSRB acknowledges that there will be costs associated with complying with this proposed rule and that some municipal advisors, including smaller firms, may exit the market as a result. However, the MSRB believes the costs and burdens are limited to those necessary to meet the objectives of the rule, consistent with its statutory basis.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period of up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

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[80] See 15 U.S.C. 78o-4(b)(2)(L)(iv).

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-MSRB-2015-03 on the subject line.

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File Number SR-MSRB-2015-03. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 am and 3:00 pm. Copies of the filing also will be available for inspection and copying at the principal office of the MSRB. All comments received will be posted without change; the Commission does not edit

personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-MSRB-2015-03 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[81]

Secretary

[81] 17 CFR § 200.30-3(a)(12).

MSRB
Municipal Securities Rulemaking Board

Regulatory Notice

2014-01

Publication Date
January 9, 2014

Stakeholders
Municipal Advisors, Issuers, General Public

Notice Type
Request for Comment

Comment Deadline
March 10, 2014

Category
Fair Practice

Affected Rules
Rule G-8; Rule G-9

Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Overview

The Municipal Securities Rulemaking Board ("MSRB") is seeking comment on draft Rule G-42 on standards of conduct and duties of municipal advisors when engaging in municipal advisory activities other than the undertaking of solicitations. The MSRB is also seeking comment on associated draft amendments to Rules G-8, on books and records, and G-9, on the preservation of records.

Comments should be submitted no later than March 10, 2014, and may be submitted in electronic or paper form. Comments may be submitted electronically by clicking here. Comments submitted in paper form should be sent to Ronald W. Smith, Corporate Secretary, Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314. All comments will be available for public inspection on the MSRB's website.[1]

Questions about this notice should be directed to Michael L. Post, Deputy General Counsel, or Kathleen Miles, Associate General Counsel, at 703-797-6600.

Background

In the aftermath of the financial crisis of 2008, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").[2] Congress, among other things, amended Section 15B of the Securities Exchange Act of 1934 ("Exchange Act") to provide for the

[1] Comments are posted on the MSRB website without change. Personal identifying information such as name, address, telephone number, or email address will not be edited from submissions. Therefore, commenters should only submit information that they wish to make available publicly.

[2] Pub. Law No. 111-203, 124 Stat. 1376 (2010).

regulation by the Securities and Exchange Commission ("SEC") and the MSRB of municipal advisors[3] and to grant the MSRB certain authority to protect municipal entities[4] and obligated persons.[5] The Dodd-Frank Act accordingly grants the MSRB broad rulemaking authority over municipal advisors and municipal advisory activities.[6] The Dodd-Frank Act's legislative history indicates Congress was concerned that the municipal securities market had

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[3] Section 15B(e)(4)(A) of the Exchange Act defines the term "municipal advisor" to mean, in relevant part and subject to certain exceptions,

> a person (who is not a municipal entity or an employee of a municipal entity) that (i) provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues; or (ii) undertakes a solicitation of a municipal entity.

As noted below, the SEC has adopted final rules on the registration of municipal advisors that set out the SEC's definition of "municipal advisor" to which the municipal advisor regulatory regime is to apply. The term "municipal advisor" is used in this notice, draft Rule G-42 and the associated amendments to Rules G-8 and G-9 with the same meaning as set forth in the SEC definition, but excluding solicitors.

[4] Section 15B(e)(8) of the Exchange Act defines the term "municipal entity" to mean:

> any State, political subdivision of a State, or municipal corporate instrumentality of a State, including ---- (A) any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (B) any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (C) any other issuer of municipal securities.

[5] Section 15B(e)(10) of the Exchange Act defines the term "obligated person" to mean:

> any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities.

[6] Section 15B(b)(2) of the Exchange Act provides that

> [t]he Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

been subject to less regulation than corporate securities markets, and particularly that "[d]uring the [financial] crisis, a number of municipalities suffered losses from complex derivatives products that were marketed by unregulated financial intermediaries."[7] The regulation of municipal advisors and their advisory activities is, as the SEC has recognized, generally intended to address problems observed with the conduct of some municipal advisors, "including 'pay to play' practices, undisclosed conflicts of interest, advice rendered by financial advisors without adequate training or qualifications, and failure to place the duty of loyalty to their clients ahead of their own interests."[8]

As discussed in more detail below, the Dodd-Frank Act itself specifically establishes that a fiduciary duty is owed by a municipal advisor to its municipal entity clients.[9] By contrast, the Dodd-Frank Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients.[10]

The SEC and MSRB have developed registration regimes for municipal advisors. In September 2010, the SEC adopted, and subsequently extended, a temporary registration program for municipal advisors.[11] In November 2010, the MSRB amended its rules to require municipal advisors to register with the MSRB.[12] Any municipal advisor engaging in municipal advisory activities

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[7] S. Rep. No. 111-176, at 38 (2010).

[8] Exchange Act Release No. 34-70462, (September 20, 2013), 78 FR 67468 (November 12, 2013) ("SEC Final Rule") at 67469; *see id.* at 67475 nn.104-6 and accompanying text (discussing relevant enforcement actions). *See also*, MSRB, Unregulated Municipal Market Participants—A Case for Reform, April 2009, http://www.msrb.org/Market-Disclosures-and-Data/Market-Statistics/~/media/Files/Special-Publications/MSRBReportonUnregulatedMarketParticipants_April09.ashx.

[9] Section 15B(c)(1) of the Exchange Act provides:

> A municipal advisor and any person associated with such municipal advisor shall be deemed to have a fiduciary duty to any municipal entity for whom such municipal advisor acts as a municipal advisor, and no municipal advisor may engage in any act, practice, or course of business which is not consistent with a municipal advisor's fiduciary duty or that is in contravention of any rule of the Board.

[10] *See* SEC Final Rule at 67475 n.100.

[11] *See* Exchange Act Release No. 34-62824 (September 1, 2010); 75 FR 54465 (September 8, 2010).

[12] *See* Exchange Act Release No. 34-63308 (November 12, 2010); 75 FR 70335 (November 17, 2010).

after December 31, 2010, without registering with the MSRB is in violation of MSRB rules.[13] In December 2010, the SEC proposed a permanent registration regime for municipal advisors.[14]

Recently, on September 18, 2013, the SEC acted on that proposal and adopted final rules to, among other things, define who is a municipal advisor, establish a permanent registration regime for that defined set of persons, and establish basic recordkeeping requirements for such advisors ("SEC Final Rule").[15] The SEC Final Rule, scheduled to take effect January 13, 2014, differs significantly from the original proposal in many respects. For example, the SEC Final Rule generally expands the scope of the exclusions and exemptions from the definition of municipal advisor, and provides additional guidance to market participants about what constitutes "advice."

With the adoption of the SEC Final Rule, the MSRB has formally re-engaged in its development of a regulatory framework for municipal advisors. A cornerstone of that regulatory framework is draft Rule G-42 establishing certain core standards of conduct and duties of municipal advisors,[16] other than when engaging in solicitation activities.[17]

The Exchange Act, as amended by the Dodd-Frank Act, contains several grants of rulemaking authority that form the statutory basis for this rulemaking initiative. Section 15B(b)(2) directs the MSRB to undertake certain rulemaking with respect to brokers, dealers, and municipal securities

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[13] *See* MSRB Notice 2010-50 (November 15, 2010).

[14] Exchange Act Release No. 34-63576 (December 20, 2010), 76 FR 824 (January 6, 2011).

[15] *See supra* note 10.

[16] SEC Final Rule at 67519 n.679 (recognizing that the regulation of municipal advisors includes the "application of standards of conduct . . . that may be required by the Commission or the MSRB, and other requirements unique to municipal advisors that may be imposed by the MSRB").

[17] Draft Rule G-42 does not address the duties of a municipal advisor when undertaking a solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Exchange Act and the rules and regulations thereunder. The MSRB intends to undertake separate rulemaking with regard to solicitation activities, which may raise issues particular to those activities, at a later date. Municipal advisors engaged in such activities are reminded that they currently are subject to the MSRB's basic fair practice rule, Rule G-17, which applies to all municipal advisors as well as to brokers, dealers and municipal securities dealers.

dealers ("dealers") and municipal advisors who provide advice to or on behalf of municipal entities and obligated persons with respect to municipal financial products and the issuance of municipal securities.[18] Such rulemaking includes, under Section 15B(b)(2)(L)(i), the establishment of rules with respect to municipal advisors to accomplish several ends, including "prescrib[ing] means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients." Section 15B(b)(2)(C) grants the MSRB authority to adopt rules to prevent fraud and in general to protect investors, municipal entities, obligated persons, and the public interest.

Previously, in the exercise of its rulemaking authority under the Dodd-Frank Act, the MSRB amended Rule G-17 on fair dealing to provide that municipal advisors, in the conduct of their municipal advisory activities, must deal fairly with all persons and not engage in any deceptive, dishonest, or unfair practice.[19]

Summary of Draft Rule G-42 and the Draft Amendments to Rules G-8 and G-9

Draft Rule G-42 (Duties of Non-Solicitor Municipal Advisors) sets forth the basic duties and responsibilities of a municipal advisor. The regulatory regime for municipal advisors includes a fiduciary duty and other standards of conduct.[20] As noted by the SEC, however, Section 975 of the Dodd-Frank Act did not define the contours of a municipal advisor's fiduciary duty. In addition, the SEC did not undertake to define the fiduciary duty or other standards of conduct of a municipal advisor as part of its Final Rule.[21]

Draft Rule G-42 elaborates on the duties of a municipal advisor, including the fiduciary duties of a municipal advisor towards its municipal entity clients. The approach towards fiduciary duties in draft Rule G-42 flows from the distinctions drawn in the Dodd-Frank Act between a municipal advisor's duties owed to clients that are municipal entities on the one hand, and obligated persons, on the other. In practice, under many circumstances, these distinctions may not be material insofar as municipal advisors have,

[18] *See* supra note 6.

[19] *See* Exchange Act Release No. 34-63599; File No. SR-MSRB-2010-16 (December 22, 2010).

[20] *See* SEC Final Rule at 67519 n.679.

[21] *See* SEC Final Rule at 67475 n.100.

with respect to all clients, a duty of care and a duty to deal fairly and to not engage in any deceptive, dishonest, or unfair practice.[22] Nevertheless, as discussed below, the MSRB invites comment on whether draft Rule G-42 appropriately limits the application of the fiduciary duty to municipal advisors' municipal entity clients, or should extend such fiduciary duty to all clients, including obligated persons, under the MSRB's issuer protection mandates.

Irrespective of any fiduciary duties, draft Rule G-42 subjects municipal advisors to a duty of care in the conduct of their municipal advisory activities. In addition, draft Rule G-42 requires municipal advisors to disclose conflicts of interest and certain other information to their clients and document their municipal advisory relationship. Draft Rule G-42 does not permit a municipal advisor to recommend that a client enter into any municipal securities transaction or municipal financial product unless the advisor has a reasonable basis for believing that the transaction or product is suitable for the client. If engaged to do so by its client, a municipal advisor also would be required to undertake a review of a recommendation made by a third party regarding a municipal securities transaction or municipal financial product. Draft Rule G-42 prohibits a municipal advisor (and any affiliate) from engaging in any transaction in a principal capacity to which the municipal entity or obligated person client of the municipal advisor is a counterparty, except for activity that is expressly permitted by underwriters under Rule G-23. The draft rule also enumerates certain other prohibited activities.

Draft Rule G-42 includes Supplementary Material that provides additional guidance on such topics as: aspects of the duty of care, aspects of the duty of loyalty, responsibilities if a client pursues an action independent of or contrary to advice provided by a municipal advisor, limitations of the scope of the municipal advisory engagement, and the requirements to provide certain disclosures to investors. The Supplementary Material also includes provisions specifically addressing the suitability of recommendations and the requirement to know one's client.

Draft Rule G-42 includes definitions, for purposes of the rule, of "advice," "affiliate of the municipal advisor," "municipal advisor, ""municipal advisory activities," "municipal advisory relationship," "municipal advisory business," "municipal entity," "obligated person," and "official statement." The terms "advice," "municipal advisor," "municipal advisory activities," "municipal entity," and "obligated person" are based upon the interpretations of statutory definitions given in the SEC Final Rule.

[22] *See* SEC Final Rule at 67511 n.574 and accompanying text.

The draft amendments to MSRB Rules G-8 (on books and records) and G-9 (on preservation of records) require, by reference, the keeping of all of the records required by the SEC Final Rule. In addition, the draft amendments to Rule G-8 would include specific recordkeeping requirements that would correspond to certain specific requirements of draft Rule G-42 that are not necessarily covered by the SEC Final Rule. The draft amendments to Rule G-9 require municipal advisors generally to preserve records for not less than five years.

The MSRB requests comment on draft Rule G-42 and the associated draft amendments to Rules G-8 and G-9.

Request for Comment

Standards of Conduct

Under draft Rule G-42(a), each municipal advisor in the conduct of its municipal advisory activities for an obligated person client is subject to a duty of care. Each municipal advisor in the conduct of its municipal advisory activities on behalf of a municipal entity client is subject to a fiduciary duty, which includes, without limitation, a duty of care and a duty of loyalty.

The Supplementary Material in the draft rule provides guidance on the meaning of the duty of care and the duty of loyalty. The duty of care, as described in Supplementary Material .01, means, without limitation, that a municipal advisor must: (a) exercise due care in performing its municipal advisory activities; (b) possess the degree of knowledge and expertise needed to provide the client with informed advice; (c) make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client; and (d) undertake a reasonable investigation to determine that the municipal advisor is not basing any recommendation on materially inaccurate or incomplete information. In addition, a municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities must also undertake a thorough review of the official statement for that issue unless otherwise directed by the client and so documented in writing.

The duty of loyalty, as described in Supplementary Material .02, requires, without limitation, a municipal advisor to deal honestly and with the utmost

good faith with a municipal entity client and act in the client's best interests without regard to the financial or other interests of the municipal advisor.

As a general matter, the duties created by the draft rule would be, as provided in Supplementary Material .06, in addition to any state law or other duties, including fiduciary duty laws.

Disclosure of Conflicts of Interest and Other Information

Draft Rule G-42(b) requires a municipal advisor to fully and fairly disclose to its client in writing all material conflicts of interest, and to do so at or prior to the inception of a municipal advisory relationship. These include any actual or potential conflict of interest that might impair the advisor's ability to render unbiased and competent advice to or on behalf of the client.

To aid municipal advisors in meeting these disclosure obligations, draft Rule G-42(b) includes a non-exhaustive list of specific items requiring disclosure. These items include the provision by any affiliate of certain advice, services, or products to or on behalf of the client; payments to obtain or retain the client's municipal advisory business; payments received from third parties to enlist the municipal advisor's recommendations; any fee-splitting arrangements with any provider of investments or services to the client; conflicts that may arise from the use of the form of compensation under consideration or selected by the client; and any other engagements or relationships of the municipal advisor or any affiliate that might impair the advisor's ability either to render unbiased and competent advice to or on behalf of the client or to fulfill its fiduciary duty to the client, as applicable. Draft Rule G-42(b) also requires disclosure of the amount and scope of coverage of professional liability insurance that the municipal advisor carries (*e.g.*, coverage for errors and omissions, improper judgments, or negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage. Finally, draft Rule G-42(b) requires disclosure of any legal or disciplinary event that is (a) material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel; (b) disclosed by the municipal advisor on the most recent Form MA filed with the SEC; or (c) disclosed by the municipal advisor on the most recent Form MA-I filed with the SEC regarding any individual actually engaging in or reasonably expected to engage in municipal advisory activities in the course of the engagement.

Paragraph .05 of the Supplementary Material provides that the conflicts disclosures must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict and must also

include an explanation of how the advisor addresses or intends to manage or mitigate each conflict.

Documentation of the Municipal Advisory Relationship

Under draft Rule G-42(c), municipal advisors must evidence each of their municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship. The documentation would be required to include, at a minimum, certain key terms and disclosures: (i) the form and basis of direct or indirect compensation, if any; (ii) the reasonably expected amount of any such compensation (stated in dollars to the extent it can be quantified); (iii) the scope of municipal advisory activities to be performed and any limitations on the scope of the engagement; (iv) in the case of municipal advisory activities relating to a new issue or reoffering of municipal securities, the specific undertakings, if any, requested by the client to be performed by the advisor relating to the preparation or finalization of the official statement or similar disclosure document; and (v) certain terms relating to the termination of the municipal advisory relationship or, if there are no such terms, then a statement to that effect. Section (c) also requires the relationship documentation to include the conflict and other information required to be disclosed by section (b).

Draft Rule G-42(c) requires that the municipal advisor amend or supplement the writing during the term of the municipal advisory relationship as necessary to reflect changes in or additions to the terms or information required to be disclosed by section (b) or (c). For example, if the basis of compensation or scope of services changed during the term of the relationship, the municipal advisor would be required to amend or supplement the writing. The same would be true in the case of material conflicts of interest discovered after the initial writing had been provided or entered into. To avoid the necessity for amendments or supplementation based on very minor changes in the amount of reasonably expected compensation, a revised writing would only be required on the basis of a change that is material. The amendment and supplementation requirement in draft Rule G-42(c) applies to any changes and additions that are discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor.

Draft Rule G-42(c) is modeled in part on MSRB Rule G-23, which requires that a dealer that enters into a financial advisory relationship with an issuer must evidence that relationship in writing prior to, upon, or promptly after the relationship has been entered into. The writing would not need to be a two-party agreement. For example, if state law provided for the procurement of

municipal advisory services in a manner that did not include a bilateral agreement, the municipal advisor could send a letter referencing the procurement document and containing the terms and disclosures that would be required by draft Rule G-42(b) and (c).

Because in some cases a client may have already reached a decision regarding a particular type of municipal securities transaction or financial product, and in other cases a client may have engaged another professional to undertake certain duties in connection with a municipal securities transaction, Supplementary Material .04 provides that a municipal advisor and its client may limit the scope of the municipal advisory relationship to certain specified activities or services. The municipal advisor, however, is not permitted to alter the standards of conduct or duties imposed by the draft rule with respect to that limited scope.

Review of the Official Statement

Except for the default requirement pursuant to the duty of care to review thoroughly the official statement, the draft rule does not prescribe specific responsibilities to be undertaken with regard to the official statement. Draft Rule G-42(c)(iv) reflects the MSRB's view that it is generally the prerogative of the client to determine the scope of the municipal advisory activities to be performed by the advisor and any limitations on the scope of the engagement. Draft Rule G-42(c)(v) would require that the specific undertakings, if any are requested by the client to be performed by the advisor with respect to the preparation and finalization of the official statement or similar document, be included in the documentation of the municipal advisory relationship. The provisions of draft Rule G-42(c)(v) may encourage the client to consider at the outset of the transaction whether and to what extent the client wants the municipal advisor to have responsibilities with regard to the official statement or similar disclosure document in light of the particular circumstances of the transaction, including the roles of any other parties involved (*e.g.*, disclosure counsel, bond counsel, swap counsel or counsel to the obligated person). If the municipal advisor and client so agree, they may exclude from the scope of the municipal advisory relationship the default requirement to thoroughly review the official statement.

Disclosure to Investors

Paragraph .07 of the Supplementary Material requires that the municipal advisor provide written disclosure to investors of any affiliation that meets the requirements of subsection (b)(ii) of the draft rule, if a document prepared by the municipal advisor or the affiliate is included in an official statement for an issue of municipal securities (*e.g.*, accountant's letter, bond

opinion, feasibility study). This requirement would be satisfied if the municipal advisor's affiliate were to provide written disclosure of the affiliation to investors. For example, if the advisor for a bond issue were affiliated with the accounting firm that would certify as to the issuer's financial statements, the disclosure of affiliation could be included in the accounting firm's letter to the issuer or disclosures concerning the accounting firm, which would be included in the official statement for the bonds. The purpose of these disclosures would be to alert investors to the affiliation.[23]

Recommendations

Section (d) provides that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product unless the advisor has a reasonable basis for believing that the transaction or product is suitable for the client. The advisor also is required to discuss with its client its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the advisor reasonably believes the recommended transaction or product is suitable for the client and whether the municipal advisor has investigated or considered other reasonably feasible alternatives. With respect to a municipal entity client, the advisor must only recommend a transaction or product that is in the municipal entity client's best interest.

Paragraph .08 of the Supplementary Material provides guidance related to an advisor's suitability obligations. Under that provision, a municipal advisor's determination of whether a municipal securities transaction or municipal financial product is suitable for the client must be based on numerous factors: the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products, financial capacity to withstand changes in market conditions and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry.

Paragraph .09 of the Supplementary Material includes a "Know Your Client" obligation which, drawing upon similar rules adopted by the Financial Industry Regulatory Authority ("FINRA") and the Commodity Futures Trading

[23] The draft amendments to Rule G-8 provide that, if the disclosure of the affiliation to investors is not provided in the official statement, the records of the municipal advisor must include a copy of the disclosure provided by the municipal advisor or its affiliate to such investors.

Commission ("CFTC"), requires the advisor to use reasonable diligence to know and maintain essential facts concerning the client and in support of the advisor's fulfillment of its suitability obligations.[24] The facts "essential" to "knowing your client" include those required to effectively service the municipal advisory relationship with the client; act in accordance with any special directions from the client; understand the authority of each person acting on behalf of the client; and comply with applicable laws, regulations and rules.

As a practical matter, a client may at times elect a course of action either independent of or contrary to the advice of its municipal advisor. Paragraph .03 of the Supplementary Material would provide that the advisor is not required *on that basis* to disengage from the municipal advisory relationship.

Review of Recommendations of Other Parties

Section (e) addresses situations when a municipal advisor may be asked to evaluate a recommendation made to its client by another party, such as a recommendation by an underwriter to an obligated party of a new financial product or financing structure. Draft Rule G-42(e) requires that a municipal advisor, if requested to do so and if the review of others' recommendations is within the scope of the engagement, discuss with its client its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product. The advisor would also be required to discuss with the client whether the advisor reasonably believes that the recommended transaction or product is, or is not, suitable for the client and the basis for such belief, as well as whether the municipal advisor has investigated or considered other reasonably feasible alternatives.

Principal Transactions

Section (f) prohibits a municipal advisor, and any affiliate of a municipal advisor, from engaging in any transaction in a principal capacity to which the municipal entity or obligated person client of the municipal advisor is a counterparty. To avoid a conflict with another MSRB rule, an exception is

[24] *See, e.g.,* FINRA Rule 2090 (Know Your Customer), Exchange Act Release No. 34-63325; SR-FINRA-2010-039 (November 17, 2010), 75 FR 71479 (November 23, 2010) and the CTFC's Subpart H-Business Conduct Standards for Swap Dealers and Major Swap Participants Dealing with Counterparties, including Special Entities, 17 CFR § 23.402(b), 77 FR 9823 (February 17, 2012). Notably, the CFTC's rule applies to dealings with special entity clients, defined to include states, state agencies, cities, counties, municipalities, other political subdivisions of a State, or any instrumentality, department, or a corporation of or established by a State or political subdivision of a State. *See* the definition of special entity in 17 CFR § 23.401(c).

allowed for activity that is expressly permitted by underwriters under Rule G-23. The MSRB notes that principal transactions by municipal advisors is an area of particular concern and has proposed to prohibit such transactions rather than allow them with the client's consent. It is questionable whether, given the high potential for self-dealing in such situations, a client consent following any amount of disclosure should be considered to be valid. Comment on whether this is the appropriate regulatory approach to principal transactions is requested below.

Specified Prohibitions

Draft Rule G-42(g) specifically prohibits certain types of activities by a municipal advisor, including: receiving excessive compensation; delivering an invoice for fees or expenses that does not accurately reflect the municipal advisory activities actually performed or the personnel that actually performed those services; misrepresenting its capacity, resources and knowledge in response to requests for proposals or qualifications or in oral presentations to a client or prospective client; making or participating in any fee-splitting arrangements with underwriters; and making or participating in any undisclosed fee-splitting arrangements with providers of investments or services to a client of the municipal advisor. In addition, a municipal advisor would be prohibited from making payments for the purpose of obtaining or retaining municipal advisory business, other than reasonable fees paid to another municipal advisor (registered as such with both the SEC and MSRB) for a solicitation of a municipal entity or obligated person as described in Section 15B(e)(9) of the Exchange Act.

Applicability to Municipal Fund Securities

The regulation of municipal advisors, as the SEC has recognized,[25] is relevant to municipal fund securities.[26] Paragraph .10 of the Supplementary Material highlights the draft rule's application to municipal advisors whose municipal advisory clients are sponsors or trustees of municipal fund securities.

[25] SEC Final Rule at 67472-67473.

[26] The term "municipal fund security" refers to, among other things, interests in governmentally sponsored 529 college savings plans and local government investment pools and is defined in MSRB Rule D-12 to mean "a municipal security issued by an issuer that, but for the application of Section 2(b) of the Investment Company Act of 1940, would constitute an investment company within the meaning of Section 3 of the Investment Company Act of 1940."

Books and Records

The draft provisions on record-keeping would be the first revisions to Rules G-8 and G-9 to address the books and records that must be made and preserved by municipal advisors registered or required to be registered with the MSRB. The SEC Final Rule already establishes a comprehensive record-keeping and preservation regime for municipal advisors that requires records, related to municipal advisory activities, of:

- all written communications received and sent by such municipal advisor;
- each version of all policies and procedures of the municipal advisor;
- any document created by the municipal advisor that was material to the making of a recommendation to a client or that memorializes the basis for that recommendation;
- all written agreements entered into by the municipal advisor with any municipal entity, employee of a municipal entity, or an obligated person or otherwise relating to the business of such municipal advisor; and
- the names of associated persons.

The draft amendments to Rules G-8 and G-9 incorporate by reference all of these record-keeping provisions of the SEC Final Rule. The draft amendments, in addition, include requirements that correspond to certain specific requirements of draft Rule G-42 that are not necessarily covered by the SEC Final Rule. This includes keeping a copy of any document created by a municipal advisor that was material to its review of a recommendation made by another party. This also includes the keeping of any document that memorializes the basis for any conclusions of the municipal advisor as to suitability. Finally, this includes, unless it is included in the official statement for an issue of municipal securities, a copy of any disclosure provided by the municipal advisor, or any affiliate, to investors as required by Supplementary Material .07.

The draft amendments to Rule G-9 require records to be preserved for not less than five years—the same period required by the SEC Final Rule. In addition, the draft amendments to Rule G-9(e) expressly provide that municipal advisors may retain records using electronic storage media or by other similar medium of record retention, subject to the retrieval and reproduction requirements of the rule. The provision for this means of compliance is made generally applicable, so as to expressly accommodate the use of electronic storage media by dealers as well as municipal advisors. Draft section (k) of Rule G-9 provides that whenever a record is preserved by a municipal advisor on electronic storage media, if the manner of storage

complies with SEC Rule 15a1-8(d) under the Exchange Act, it will be deemed to be preserved in a manner that is in compliance with the requirements of Rule G-9. This provision gives municipal advisors the choice to comply with either the SEC's or the MSRB's preservation requirements.

General Matters

In addition to any other subject which commenters may wish to address related to draft Rule G-42 and the draft amendments to Rules G-8 and G-9, the MSRB seeks public comment on the specific questions below. 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 contained in this request for comment.

1) Draft Rule G-42 follows the Dodd-Frank Act in deeming a municipal advisor to owe a fiduciary duty, for purposes of the draft Rule G-42, only to its municipal entity clients. Is carrying forward that distinction in the draft rule appropriate in light of the services a municipal advisor provides to its obligated person clients? Would having a uniform fiduciary standard applied to *all* of a municipal advisor's clients facilitate compliance with the draft rule or provide better protection for issuers? If so, are there any legal impediments to the MSRB extending a fiduciary duty in the draft rule to all clients of a municipal advisor?

2) Do commenters agree that a municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities should have an obligation, unless agreed to otherwise by the advisor and client, to review thoroughly the entire official statement? Should a municipal advisor be permitted to limit the scope of the engagement such that the advisor is not required to review the official statement? If so, under what circumstances should this limitation be allowed? Should any duty to review the official statement be limited to any portions of the official statement directly related to the scope of municipal advisory services?

3) Would draft Rule G-42(c)(vi) have benefits in terms of encouraging municipal entity and obligated person clients to carefully consider at the outset of a transaction any obligations it may have in connection with the preparation and distribution of the official statement and the extent to which it has engaged professionals, as necessary, to assist it in fulfilling its responsibilities?

4) Do commenters agree or disagree that there is a need to specifically require disclosure of conflicts of interest that may arise from the form of

compensation under consideration by the client and/or selected by the client?

5) Draft Rule G-42 allows fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client, but requires written full and fair disclosure of the arrangement. Should such fee-splitting arrangements be prohibited, regardless of whether they are fully and fairly disclosed?

6) Is draft Rule G-42(b)'s requirement that the disclosure of conflicts of interest and other information be provided at or prior to the inception of the municipal advisory relationship the appropriate timeframe?

7) Should a municipal advisor be required to obtain a written acknowledgment from the client of receipt of the conflicts disclosure and consent to any conflicts disclosed before proceeding with a municipal advisory engagement?

8) Should a municipal advisor be required to disclose legal and disciplinary events that relate to an individual that is employed by the municipal advisor even if the individual is not a part of (or reasonably expected to be part of) the advisor's team working for the client?

9) Should the MSRB, in furtherance of its mandate under the Dodd-Frank Act to protect municipal entities and obligated persons, require professional liability insurance by municipal advisors, and, if so, should the MSRB specify the minimum amount and terms of such coverage?

10) Would the cost of professional liability insurance be an undue barrier to entry for a potential municipal advisor?

11) Should an advisor be required to review any feasibility study as a part of the information considered in its evaluation of whether a transaction it recommends is suitable for the client?

12) Should a municipal advisor (or its affiliate) be permitted to engage in certain types of principal transactions with its client, with full and fair disclosure and written client consent? If so, what types of principal transactions should be allowed?

13) Should the treatment of principal transactions differ based upon whether a municipal advisor has a fiduciary duty to the client?

Economic Analysis

In proposing draft Rule G-42 and the draft amendments to Rules G-8 and G-9, the MSRB has been guided by its policy on the use of economic analysis in rulemaking. The MSRB is sensitive to the costs imposed by its rules and has sought to tailor the draft rule and amendments so as not to impose unnecessary or inappropriate costs and burdens on municipal advisors. In accordance with this policy, the Board considered the following factors with respect to draft Rule G-42 and the draft amendments to Rules G-8 and G-9: 1) the need for the draft rule and how the draft rule will meet that need; 2) relevant baselines against which the likely economic impact of elements of the draft rule can be considered; 3) reasonable alternative regulatory approaches; and 4) the potential benefits and costs of the draft rule and the main alternative regulatory approaches. Each of these factors is discussed in detail below.

1. **The need for the draft rule and how the draft rule will meet that need.**

Prior to the enactment of the Dodd-Frank Act, municipal advisors were largely unregulated as to their municipal advisory activities.[27] As noted, the Dodd-Frank Act amends the Exchange Act to provide new protections for municipal entities and obligated persons in connection with the issuance of, or the investment of the proceeds of, municipal securities, and to grant the MSRB a role in the protection of municipal entities and obligated persons. The Dodd-Frank Act establishes a federal regulatory regime that requires municipal advisors to register with the SEC, grants the MSRB certain regulatory authority over municipal advisors, and imposes, among other things, a federal statutory fiduciary duty on municipal advisors when advising municipal entity clients. Municipal advisors advising municipal entities are prohibited from engaging in any act, practice, or course of business which is not consistent with that fiduciary duty. In addition, Congress directed that the MSRB develop rules reasonably designed to prevent acts, practices, or courses of business by municipal advisors that are inconsistent with their fiduciary duty, as applicable. Neither the Dodd-Frank Act nor the recently adopted SEC Final Rule prescribe the duties and obligations of municipal advisors beyond a general statement that municipal advisors shall be deemed to have a fiduciary duty to any municipal entity for whom the municipal advisor acts as a municipal advisor. Therefore, there is a need for regulatory guidance with respect to the duties of municipal advisors and the

[27] Prior to the Dodd-Frank Act, certain MSRB rules applied to a subset of municipal advisors consisting of dealers acting as financial advisors in connection with new issues of municipal securities.

prevention of breaches of a municipal advisor's fiduciary duty to its municipal entity clients.

Draft Rule G-42 also establishes standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for obligated persons and provides guidance to these advisors as to what conduct would satisfy these duties and obligations.

The MSRB believes that by articulating specific standards of conduct and duties for municipal advisors, draft Rule G-42 will assist municipal advisors in complying with the statutorily-imposed requirements of the Dodd-Frank Act, and help prevent failures to meet those requirements. The draft rule is expected to aid municipal entities and obligated persons that choose to engage municipal advisors in connection with their issuances of municipal securities as well as transactions in municipal financial products by promoting higher ethical and professional standards of such advisors. The MSRB also believes that articulating standards of conduct and duties of municipal advisors will enhance the ability of the MSRB and other regulators to oversee the conduct of municipal advisors, as contemplated by the Dodd-Frank Act.

2. Relevant baselines against which the likely economic impact of elements of the draft rule can be measured.

In considering the economic consequences of draft Rule G-42 and the draft amendments to Rules G-8 and G-9, the MSRB has defined and analyzed several baselines to serve as points of reference. Given that the draft rule contains many different elements, the MSRB has considered a separate baseline for one or more different elements. The purpose of the baselines is to compare, on the one hand, the expected state with draft Rule G-42 in effect to, on the other hand, the baseline state prior to the rule taking effect. The economic impact of the draft rule is considered to be the difference between these two states.

For draft Rule G-42, one relevant baseline for analysis is the Dodd-Frank Act, which subjected municipal advisors to a statutory fiduciary duty with respect to municipal entity clients. The MSRB considers the obligations imposed by this duty to be a baseline, such that the costs and benefits of draft Rule G-42 should be measured by any change from this existing state. Although the statute imposed this fiduciary duty, it does not describe or clarify its elements. Draft Rule G-42 can be viewed as establishing guidance and clarification with respect to this fiduciary duty and potentially prescribing means designed to prevent breaches of this duty.

The MSRB considers MSRB Rule G-17 to be a relevant baseline for the standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for obligated persons. This rule, as amended in 2010, requires municipal advisors to deal fairly with all persons and not engage in any deceptive, dishonest, or unfair practice. Although Rule G-17 applies to all municipal advisors, the MSRB does not regard it as the baseline for municipal advisors with municipal entity clients because the fiduciary duty imposed by the Dodd-Frank Act represents a higher baseline state for these municipal advisors. Draft Rule G-42 can be viewed, to a certain extent, as articulating guidance on the conduct required for municipal advisors to meet their existing duty to deal fairly with all persons (including obligated persons).

The Dodd-Frank Act prohibits municipal advisors from engaging in any fraudulent, deceptive, or manipulative act or practice, as pertinent here, in connection with providing advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities. The MSRB considers this prohibition also to serve as a baseline for standards of conduct for municipal advisors.

A subset of municipal advisors who are also dealers are subject to MSRB Rule G-23 which establishes requirements with respect to the conflict of interest that can arise in the context of dealers who may seek to switch roles between financial advisor and underwriter to issuers with respect to the issuance of municipal securities. In particular, Rule G-23(c) provides that a dealer that enters into a financial advisory relationship must evidence that relationship in writing prior to, upon, or promptly after the relationship has been entered into. Rule G-23 also prohibits a dealer that has a financial advisory relationship with the issuer in connection with a new issue from acting as an underwriter or placement agent for such new issue. For this subset of municipal advisors, the applicable set of standards and requirements of Rule G-23 is considered by the Board to be a baseline.

In addition to the Dodd-Frank Act and the MSRB's existing rules, the SEC Final Rule on registration of municipal advisors provides baselines for particular elements of draft Rule G-42. The SEC Final Rule requires disclosure in registration forms of certain disciplinary history and conflicts of interest. Draft Rule G-42 requires disclosure of at least some similar information. Although draft Rule G-42 would require disclosure directly to clients rather than through submissions to a regulator, the MSRB considers the SEC Final Rule to serve as a relevant baseline.

Another relevant consideration when analyzing the duties under draft Rule G-42 is current state law. For example, to the extent that municipal advisors owe a fiduciary duty to their clients under the laws of at least some states,[28] the MSRB regards these laws as a baseline.

Finally, the MSRB considers existing requirements in the SEC Final Rule on recordkeeping and record preservation to serve as a baseline. These requirements are the existing state against which additional requirements by the MSRB can be compared. In addition, municipal advisors who are also registered as dealers or investment advisors are subject to recordkeeping requirements under those regulatory regimes that can serve as baseline requirements for that subset of the municipal advisor population.

3. Identifying and evaluating reasonable alternative regulatory approaches.

The MSRB policy on economic analysis in rulemaking addresses the identification and evaluation of reasonable regulatory alternatives.

One alternative to the draft rule would be for the MSRB not to engage in additional rulemaking, and thus, not establish guidance with respect to the duties and obligations of municipal advisors. Under this alternative, the needs of municipal advisors for guidance on avoiding and potentially preventing breaches of the broad statutorily-imposed requirements of the Dodd-Frank Act would go unmet.

Another alternative is for the MSRB to use a solely principles-based approach to its rulemaking on this subject. Under this approach, the regulatory objectives would be specified but individual firms would be free to select the means used to meet these objectives. Employing a solely principles-based approach, however, may provide insufficient guidance on meeting the standards of conduct for municipal advisors required under the Dodd-Frank Act and on establishing means for preventing breaches of applicable fiduciary duties. The MSRB believes that the duties and obligations articulated in the draft rule, although some are relatively more prescriptive, provide balanced and useful guidance. In addition, this balanced approach serves to minimize the risks attendant to the framework of municipal securities regulation involving multiple enforcement organizations.

[28] *See, e.g.*, *In re O'Brien Partners, Inc.*, Securities Act Release No. 7594, Investment Advisors Act Rel. No. 1772, A.P. File No. 3-9761 (Oct. 27, 1998), 1998 SEC LEXIS 2318, at 31 n.20 (citing *Production Credit Ass'n of Lancaster* v. *Croft*, 423 N.W. 2d 544, 547 (Wis. App. 1988); *Recorded Picture Co.* v. *Nelson Entertainment, Inc.*, 61 Cal. Rptr. 2d 742, 754 (Ct. App. 2 Dist. 1977)).

The MSRB invites public comment to suggest alternative regimes as well as comments on the potential costs and benefits of alternative regimes.

4. Assessing the benefits and costs, both quantitative and qualitative, of the draft rule and the main alternative regulatory approaches.

Below, the MSRB preliminarily addresses the likely costs and benefits of the draft rule against the context of the economic baselines discussed above, primarily in terms of the specific changes from the baseline and, to some degree, in terms of the potential overall impact on the market for municipal advisory services. In considering these costs, benefits and impacts, the MSRB addresses reasonable alternatives, where applicable.

At the outset, the MSRB notes it is currently unable to quantify the economic effects of draft Rule G-42 and the amendments to Rules G-8 and G-9 because the information necessary to provide reasonable estimates is not available. The MSRB observes, as the SEC also observed in its Final Rule, that there is little publicly available information about the municipal advisory industry. In addition, estimating the costs for municipal advisory firms to comply with the draft rule is hampered by the fact that these costs depend on the business activities and size of these municipal advisory firms, which can vary greatly. Given the limitations on the MSRB's ability to conduct a quantitative assessment of the costs and benefits associated with the draft rule, the MSRB has thus far considered these costs and benefits primarily in qualitative terms.

Benefits

The MSRB believes that the draft rule would result in a number of benefits by enhancing protections to municipal entities, obligated persons and investors and by providing guidance to municipal advisors for complying with the requirements of the Dodd-Frank Act.

The MSRB believes that one benefit of the draft rule is that it enhances protections to municipal entities and obligated persons by ensuring that these entities have available to them sufficient information to make meaningful choices about engaging a municipal advisor. These protections would also be enhanced as a result of the draft rule's guidance for municipal advisors that may assist these advisors in complying with, or help prevent breaches of, their fiduciary and fair-dealing duties. To the extent that this guidance increases the likelihood of compliance by municipal advisors, municipal entities and obligated persons will benefit. Investors in municipal bond offerings may benefit from the draft rule to the extent that a municipal

entity issuing bonds that uses a municipal advisor is more likely to receive services that reflect a higher ethical and professional standard than otherwise would be the case. Municipal entities, obligated persons and investors also may benefit to the extent that making explicit the core restrictions on certain activities in which the municipal advisor has a self-interest would reduce the incidence of self-dealing or other similar activities that can directly or indirectly raise costs of a financing that ultimately would be borne by municipal entities, obligated persons or investors.

The MSRB believes that the draft rule provides needed guidance and clarification with respect to the standards of conduct and duties of a municipal advisor that would meet the purposes of the Dodd-Frank Act. The draft rule also prescribes for municipal advisors means that may prevent breaches of these duties. Therefore, this guidance provides a benefit to municipal advisors who could otherwise face greater uncertainty about the standards of conduct and duties required to meet certain of the requirements of the Dodd-Frank Act, particularly, as noted, given the regulatory framework for municipal securities regulation involving multiple enforcement organizations.

The MSRB believes that one benefit of the draft rule may follow from the increased level of information disclosed to clients by municipal advisors relative to the baseline, which may lead to an improvement in the selection of municipal advisors. As a result of the information disclosed through the draft rule, municipal entities and obligated persons may be able to more easily establish objective criteria to use in selecting municipal advisors and may increase the likelihood that municipal advisors are hired because of their qualifications as opposed to other reasons.

The draft rule should also result in improved quality-based competition among municipal advisors to the extent that the clients of municipal advisors rely on the information that would be required to be disclosed by the rule in the municipal advisor selection process.

Costs

In this section we preliminarily analyze the potential costs of the draft rule relative to the appropriate baseline. Our analysis does not consider all the costs associated with the draft rule, but instead focuses on the incremental costs attributable to the draft rule's requirements that exceed the baseline case. The costs associated with the baseline case are in effect subtracted from the costs associated with the draft rule in order to isolate the costs attributable to the incremental requirements of the draft rule.

The MSRB recognizes that municipal advisors would incur costs to meet the standards of conduct and duties contained in draft Rule G-42 and the amendments to Rules G-8 and G-9. These costs may include additional compliance costs and additional recordkeeping costs. To ensure compliance with the disclosure obligations of the draft rule, municipal advisors may incur costs by seeking advice from legal and compliance professionals when preparing disclosures to clients. However, the MSRB believes that some of these costs are accounted for in the baseline requirements of the SEC Final Rule which requires disclosure of at least some similar information, such as the disclosure of disciplinary history. Draft Rule G-42 may impose additional costs on municipal advisors as it requires disclosure of additional information and requires that information be disclosed directly to clients rather than through submissions to a regulator. The magnitude of these additional costs is not quantifiable using available data and the MSRB seeks public comment on this cost component.

Municipal advisors may incur additional recordkeeping costs as a result of the draft rule. The MSRB considers existing requirements in the SEC Final Rule on record-keeping and record preservation to serve as a baseline. As the SEC recognized in its economic analysis of its recordkeeping requirements, municipal advisors should already be maintaining books and records as part of their day-to-day operations. In addition, municipal advisors who are also registered as broker-dealers or investment advisors are currently subject to the recordkeeping requirements of those regulatory frameworks. Against these baselines, the MSRB believes that the costs associated with the few additional recordkeeping requirements associated with draft Rule G-42 will not be very significant, but seeks public comment on the magnitude of these costs.

The MSRB believes that any increase in municipal advisory fees attributable to the additional costs of the draft rule compared with the baseline state will be, in the aggregate, minimal and that the cost per municipal advisory firm will be spread across the number of advisory engagements for each firm. The MSRB recognizes, however, that for smaller municipal advisors with fewer clients, the cost of compliance with the draft rule's standards of conduct and duties may represent a greater percentage of annual revenues, and thus, such advisors may be more likely to pass those costs along to their advisory clients.

The MSRB recognizes that, as a result of these costs, some municipal advisors may decide to exit the market, curtail their activities, consolidate with other firms, or pass the costs on to municipal entities and obligated persons in the form of higher fees. The MSRB believes, however, that municipal advisors

may exit the market for a number of reasons, including business reasons separate from reasons involving the costs associated with the draft rule. The MSRB believes that municipal advisors that have been subject to past disciplinary actions may decide to exit the market rather than disclose that information directly to clients, which could improve the quality of the market for municipal advisory services and, therefore, benefit municipal entities and obligated persons. The Board recognizes that some of the municipal advisors that may exit the market for financial reasons could be small municipal advisors and that such exit from the market may lead to a reduced pool of municipal advisors.

The MSRB has also considered the possibility that some compliance costs could be greater in the absence of the draft rule. By articulating the duties and obligations of municipal advisors and by prescribing means that will prevent breaches of these duties, the draft rule may reduce possible confusion and uncertainty about what is required in order to comply with the Dodd-Frank Act. Therefore, the draft rule may reduce certain costs of compliance that might have otherwise been incurred by allowing municipal advisors to more quickly and accurately determine compliance requirements.

Effect on Competition, Efficiency and Capital Formation

The MSRB considered that the costs associated with the draft rule relative to the baseline may lead some municipal advisors to consolidate with other municipal advisors. For example, some municipal advisors may determine to consolidate with other municipal advisors in order to benefit from economies of scale (*e.g.*, by leveraging existing compliance resources of a larger firm) rather than to incur separately the costs associated with the draft rule. The MSRB believes that the market for municipal advisory services is likely to remain competitive despite the potential exit of some municipal advisors, including small municipal advisors, consolidation of municipal advisors, or lack of new entrants into the market.

As noted above, the increased level of information disclosed by municipal advisors relative to the baseline may lead to an improved municipal advisor selection process which may increase the willingness of municipal entities and obligated persons to use municipal advisors. This, in turn, may contribute to a more efficient capital formation process as municipal entities and obligated persons may make different decisions about issuance relative to other financing options.

Request for Comment on Economic Analysis

In furtherance of the MSRB's policy on economic analysis, the MSRB requests public comment on the potential economic consequences which may result from the adoption of draft Rule G-42 and the draft amendments to Rules G-8 and G-9. Commenters are encouraged to provide supporting data, studies, or other information related to their views of the economic effects of the draft rule. In particular, the MSRB welcomes any information regarding the potential to quantify likely benefits and costs. In addition to comments on the potential economic consequences associated with the draft rule, the MSRB also requests comment to help identify the potential benefits and costs of the regulatory alternatives suggested by commenters. The MSRB also requests comment on the competitive or anticompetitive effects, as well as efficiency and capital formation effects, of the draft rule and draft amendments on any market participants.

The Dodd-Frank Act provides that MSRB rules may not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons provided that there is robust protection of investors against fraud. The MSRB is sensitive to the potential impact of the requirements contained in draft Rule G-42 on small municipal advisors. The MSRB understands that some small municipal advisors and solo practitioners, unlike larger municipal advisory firms, may not employ full-time compliance staff and that the cost of ensuring compliance with the requirements of the draft rule may be proportionally higher for these smaller firms. The MSRB, preliminarily, believes that the draft rule is consistent with the Dodd-Frank Act's provision with respect to burdens imposed on small municipal advisors. In order to minimize any significant burdens on small municipal advisors, however, the MSRB is particularly interested in receiving meaningful feedback regarding the potential economic impact of the draft rule and draft amendments on small municipal advisors. The MSRB will consider such feedback in light of the Dodd-Frank Act provision.

In addition to any issues raised by this analysis about which interested persons may wish to comment, the MSRB specifically requests that commenters address the following questions:

1) Do commenters agree or disagree that a need exists for the MSRB to articulate the duties of municipal advisors or to prescribe means of preventing breaches of a municipal advisor's fiduciary duty to its municipal entity clients? If so, do commenters agree or disagree that the draft rule addresses those needs?

2) The MSRB proposes to use the fiduciary duty already imposed on municipal advisors by the Dodd-Frank Act to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for municipal entity clients. Is this an appropriate baseline?

3) The MSRB proposes to use the fair-dealing requirements under MSRB Rule G-17 to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for obligated persons. Is this an appropriate baseline?

4) The MSRB proposes to use the Dodd-Frank Act's prohibition on municipal advisors from engaging in any fraudulent, deceptive, or manipulative act or practice in connection with advising a client to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct for municipal advisors (regardless of whether the client is a municipal entity or obligated person). Is this an appropriate baseline?

5) The MSRB proposes to use the existing requirements for dealers who act as financial advisors to issuers with respect to the issuance of municipal securities to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct and duties for this subset of municipal advisors. Is this an appropriate baseline?

6) The MSRB proposes to use the required disclosures in registration forms of certain disciplinary history and legal events contained in the SEC Final Rule to serve as a baseline for evaluating the economic impact of the draft rule's disclosure requirements. Is this an appropriate baseline?

7) The MSRB proposes to use the recordkeeping and record preservation requirements contained in the SEC Final Rule to serve as a baseline for evaluating the economic impact of the draft rule's recordkeeping and record preservation requirements. Is this an appropriate baseline?

8) In addition to the baselines proposed above, are there other relevant baselines that the MSRB should consider?

9) Please compare the costs and benefits of having disciplinary histories and legal events disclosed through registration forms versus disclosure directly to the client.

10) Are there lower-cost alternatives to requiring disclosure of the amount of professional liability coverage carried by the municipal advisor that would provide comparable benefits to clients of municipal advisors?

11) Would additional benefits accrue if the MSRB were to impose different or additional recordkeeping requirements and, if so, what would these requirements entail?

12) To the extent that draft Rule G-42 establishes new, or clarifies existing, standards of conduct and duties for municipal advisors, will this cause a change in the quality of advice offered by municipal advisors?

13) To the extent that draft Rule G-42 and the draft amendments to Rules G-8 and G-9 impose costs on municipal advisors, will these costs be passed on to municipal entities or obligated persons in the form of higher fees?

14) To the extent that the requirements of draft Rule G-42 enhance the oversight of municipal advisors, will this affect the willingness of market participants to use municipal advisors?

15) To the extent that the requirements of draft Rule G-42 enhance the oversight of municipal advisors, will this lead to different issuance costs and financing terms for issuers?

16) To the extent that the requirements of draft Rule G-42 lead to reduced issuance costs and better financing terms for issuers, will this improve capital formation?

17) Would the requirements of draft Rule G-42 assist municipal entities or obligated persons in making hiring decisions with respect to municipal advisors?

18) What are the initial and ongoing costs associated with making and preserving the additional records required by the draft amendments to Rules G-8 and G-9?

19) Are there additional costs or benefits to recordkeeping that the MSRB should consider? If so, please explain.

20) If the draft rule is adopted, what are the likely effects on competition, efficiency and capital formation?

21) How will the requirements of draft Rule G-42 affect potential municipal advisors' decisions with respect to entry into the market?

22) What training costs would the requirements of draft Rule G-42 cause at municipal advisory firms to ensure compliance?

23) Will draft Rule G-42 have benefits in terms of protecting municipal entities, obligated persons and investors?

24) Will the requirements of draft Rule G-42 impose any burden on small municipal advisors that is not necessary or appropriate?

25) Will the requirements of draft Rule G-42 create advantages for large municipal advisor firms relative to smaller municipal advisor firms?

January 9, 2014

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Text of Proposed Amendments[29]

Rule G-42: Duties of Non-Solicitor Municipal Advisors

(a) *Standards of Conduct.*

(i) A municipal advisor to an obligated person client shall, in the conduct of all municipal advisory activities for that client, be subject to a duty of care.

(ii) A municipal advisor to a municipal entity client shall, in the conduct of all municipal advisory activities for that client, be subject to a fiduciary duty that includes a duty of loyalty and a duty of care.

(b) *Disclosure of Conflicts of Interest and Other Information*. A municipal advisor must, at or prior to the inception of a municipal advisory relationship, provide the client with a document making full and fair disclosure of all material conflicts of interest, including disclosure of:

(i) any actual or potential conflicts of interest of which it is aware after reasonable inquiry that might impair its ability either to render unbiased and competent advice to or on behalf of the client or to fulfill its fiduciary duty to the client, as applicable;

(ii) any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor;

[29] Underlining indicates new language; strikethrough denotes deletions.

(iii) any payments made by the municipal advisor directly or indirectly to obtain or retain the client's municipal advisory business;

(iv) any payments received by the municipal advisor from third parties to enlist the municipal advisor's recommendation to the client of its services, any municipal securities transaction or any municipal financial product;

(v) any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client;

(vi) any conflicts of interest that may arise from the use of the form of compensation under consideration or selected by the client for the municipal advisory activities to be performed;

(vii) any other engagements or relationships of the municipal advisor or any affiliate of the municipal advisor that might impair the advisor's ability either to render unbiased and competent advice to or on behalf of the client or to fulfill its fiduciary duty to the client, as applicable;

(viii) the amount and scope of coverage of professional liability insurance that the municipal advisor carries (*e.g.*, coverage for errors and omissions, improper judgments, or negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage; and

(ix) any legal or disciplinary event that is (a) material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel; (b) disclosed by the municipal advisor on the most recent Form MA filed with the Commission; or (c) disclosed by the municipal advisor on the most recent Form MA-I filed with the Commission regarding any individual actually engaging in or reasonably expected to engage in municipal advisory activities in the course of the engagement. If a municipal advisor has disclosed a legal or disciplinary event on any form referenced in section (b) or (c) of this rule, the advisor must provide the client with a copy of the relevant sections of the form or forms.

If a municipal advisor concludes that it has no material conflicts of interest, the municipal advisor must provide written documentation to the client to that effect.

(c) *Documentation of Municipal Advisory Relationship*. A municipal advisor must evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship. The writing must be dated and include, at a minimum,

(i) the form and basis of direct or indirect compensation, if any, for the municipal advisory activities to be performed;

(ii) the reasonably expected amount of any such compensation (stated in dollars to the extent it can be quantified);

(iii) the information regarding conflicts of interest and other matters that is required to be disclosed by section (b) of this rule;

(iv) the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement;

(v) in the case of municipal advisory activities relating to a new issue or reoffering of municipal securities, the specific undertakings, if any, requested by the client to be performed by the municipal advisor with respect to the preparation and finalization of an official statement or similar disclosure document; and

(vi) the date, triggering event, or means for the termination of the municipal advisory relationship, or, if none, a statement that there is none.

During the term of the municipal advisory relationship, the writing must be promptly amended or supplemented to reflect any changes in or additions to the terms or information required by section (b) or this section (c), and the revised writing must be promptly delivered to the client, provided that this requirement applies with respect to subsection(c)(ii) of this rule only if the change in the amount of reasonably expected compensation is material. This amendment and supplementation requirement applies to any changes and additions that are discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor.

(d) *Recommendations*. A municipal advisor must not recommend that its municipal entity or obligated person client enter into any municipal securities transaction or municipal financial product unless the advisor has a reasonable basis for believing, based on the information obtained through the reasonable diligence of the advisor, that the transaction or product is suitable for the client. In addition, the municipal advisor must discuss with its client:

(i) the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product;

(ii) the basis upon which the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is suitable for the client; and

(iii) whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives.

With respect to a client that is a municipal entity, a municipal advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest.

(e) *Review of Recommendations of Other Parties.* When requested to do so by its municipal entity or obligated person client and within the scope of its engagement, a municipal advisor must undertake a thorough review of any recommendation made by any third party regarding a municipal securities transaction or municipal financial product. In addition, the municipal advisor must discuss with its client:

(i) the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product;

(ii) whether the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is suitable for the client, and the basis for such belief; and

(iii) whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives.

(f) *Principal Transactions.* Except for an activity that is expressly permitted under Rule G-23, a municipal advisor, and any affiliate of a municipal advisor, is prohibited from engaging in any transaction, in a principal capacity, to which a municipal entity or obligated person client of the municipal advisor is a counterparty.

(g) *Specified Prohibitions.* A municipal advisor is prohibited from:

(i) receiving compensation that is excessive in relation to the municipal advisory activities actually performed;

(ii) delivering an invoice for fees or expenses for municipal advisory activities that do not accurately reflect the activities actually performed or the personnel that actually performed those services;

(iii) making any representation or the submission of any information about the capacity, resources or knowledge of the municipal advisor, in response to requests for proposals or qualifications or in oral presentations to a client or prospective client, for the purpose of obtaining or retaining municipal advisory business that the advisor knows or should know is materially false or misleading;

(iv) making, or participating in, any fee-splitting arrangements with underwriters, and any undisclosed fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client of the municipal advisor; and

(v) making payments for the purpose of obtaining or retaining municipal advisory business other than reasonable fees paid to another municipal advisor registered as such with the Commission and the Board for a solicitation of a municipal entity or obligated person as described in Section 15B(e)(9) of the Act.

(h) *Definitions*.

(i) "Advice" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(4)(A)(i) of the Act and the rules and regulations thereunder.

(ii) "Affiliate of the municipal advisor" shall mean, for purposes of this rule, any person directly or indirectly controlling, controlled by, or under common control with such municipal advisor.

(iii) "Municipal advisor" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(4) of the Act and the rules and regulations thereunder; provided that it shall exclude a person that is otherwise a municipal advisor solely with respect to either activities within the meaning of Section 15B(e)(4)(A)(ii) or any solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Act.

(iv) "Municipal advisory activities" shall, for purposes of this rule, have the same meaning as the activities specified in Section 15B(e)(4)(A) of the Act and the rules and regulations thereunder, provided that they shall exclude the activities within the meaning of Section 15B(e)(4)(A)(ii) of the Act and the rules and regulations thereunder and any solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Act and the rules and regulations thereunder.

(v) A "municipal advisory relationship" shall, for purposes of this rule, be deemed to exist when a municipal advisor engages in or enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person client.

(vi) "Municipal advisory business" shall mean, for purposes of this rule, the provision of advice to or on behalf of a municipal entity or an obligated person with respect to the issuance of municipal securities or municipal financial products by a municipal advisor whether for compensation or otherwise.

(vii) "Municipal entity" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(8) of the Act and the rules and regulations thereunder.

(viii) "Obligated person" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(10) of the Act and the rules and regulations thereunder.

(ix) "Official statement" shall, for purposes of this rule, have the same meaning as in Rule G-32(d)(vii).

---Supplementary Material:

.01 Duty of Care. Municipal advisors must exercise due care in performing their municipal advisory activities. The duty of care includes, but is not limited to, the obligations discussed in this section. A municipal advisor must possess the degree of knowledge and expertise needed to provide the municipal entity or obligated person client with informed advice. A municipal advisor also must make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client. A municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities must also undertake a thorough review of the official statement for that issue, unless otherwise directed by the client and documented under subsection (c)(iv) of this rule. A municipal advisor must undertake a reasonable investigation to determine that it is not

basing any recommendation on materially inaccurate or incomplete information. Among other matters, a municipal advisor must have a reasonable basis for:

(a) any advice provided to or on behalf of a client;

(b) any representations made in a certificate that it signs that will be reasonably foreseeably relied upon by the client, any other party involved in the municipal securities transaction or municipal financial product, or investors in the municipal entity client's securities or securities secured by payments from an obligated person client; and

(c) any information provided to the client or other parties involved in the municipal securities transaction when participating in the preparation of an official statement for any issue of municipal securities with respect to which the advisor is advising.

.02 Duty of Loyalty. Municipal advisors must fulfill a duty of loyalty in performing their municipal advisory activities for municipal entity clients. The duty of loyalty includes, but is not limited to, the obligations discussed in this section. A municipal advisor must deal honestly and with the utmost good faith with a municipal entity client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. A municipal advisor to a municipal entity client must either eliminate or provide full and fair disclosure to the client about each of its material conflicts of interest. A municipal advisor must investigate or consider other reasonably feasible alternatives to any recommended municipal securities transaction or municipal financial product that might also or alternatively serve the municipal entity client's objectives.

.03 Action Independent of or Contrary to Advice. If a municipal entity or obligated person client of a municipal advisor elects a course of action that is independent of or contrary to advice provided by the advisor, the advisor is not required on that basis to disengage from the municipal advisory relationship.

.04 Limitations on the Scope of the Engagement. Nothing contained in this rule shall be construed to permit the municipal advisor to alter the standards of conduct or impose limitations on any of the duties prescribed herein. If requested or consented to by the municipal entity or obligated person client, however, a municipal advisor may limit the scope of the municipal advisory relationship to certain specified activities or services. If the municipal advisor engages in a course of conduct that is inconsistent with any such agreed upon limitations, it may result in negating the effectiveness of such limitations.

.05 Conflicts of Interest. Disclosures of conflicts of interest by a municipal advisor to its municipal entity or obligated person client must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict. Such disclosures also must include an explanation of how the advisor addresses or intends to manage or mitigate each conflict.

.06 Applicability of State or Other Laws. Municipal advisors may be subject to fiduciary or other duties under state or other laws. Nothing contained in this rule shall be deemed to supersede any more restrictive provision of state or other laws applicable to the activities of municipal advisors.

.07 Disclosure to Investors. If all or a portion of a document prepared by a municipal advisor or any of its affiliates is included in an official statement for any issue of municipal securities by or on behalf of its municipal entity or obligated person client, the municipal advisor must provide written disclosure to investors, which disclosure may be provided in the official statement, of any affiliation that meets the criteria of subsection (b)(ii) of this rule. This disclosure requirement shall be deemed satisfied if the relevant affiliate provides the required written disclosure to investors.

.08 Suitability. A determination of whether a municipal securities transaction or municipal financial product is suitable must be based on the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued in the municipal securities transaction are reasonably expected to be outstanding and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry.

.09 Know Your Client. A municipal advisor must use reasonable diligence, in regard to the maintenance of the municipal advisory relationship, to know and retain the essential facts concerning the client and concerning the authority of each person acting on behalf of such client. The facts "essential" to "knowing a client" include those required to:

(a) effectively service the municipal advisory relationship with the client;

(b) act in accordance with any special directions from the client;

(c) understand the authority of each person acting on behalf of the client; and

(d) comply with applicable laws, regulations and rules.

.10 529 College Savings Plans and Other Municipal Fund Securities. This rule applies equally to municipal advisors to sponsors or trustees of 529 college savings plans and other municipal fund securities. All references in this rule to an "official statement" include the plan disclosure document for a 529 college savings plan and the investment circular or information statement for a local government investment pool.

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Rule G-8: Books and Records to be Made by Brokers, Dealers, ~~and~~ Municipal Securities Dealers, and Municipal Advisors

(a) - (g) No change.

(h) *Municipal Advisor Records*. Every municipal advisor that is registered or required to be registered under section 15B of the Act and the rules and regulations thereunder shall make and keep current the following books and records:

(i) *General Business Records.* All books and records described in Rule 15Ba1-8(a)(1)-(8) under the Act.

(ii) *Records Concerning Duties of Non-Solicitor Municipal Advisors pursuant to Rule G-42.*

(A) A copy of any document created by a municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any conclusions as to suitability; and

(B) Unless included in the official statement for an issue of municipal securities, a copy of any disclosure provided by the municipal advisor or any affiliate of the municipal advisor to investors, as required by the provisions of Rule G-42 Supplementary Material .07.

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Rule G-9: Preservation of Records

(a) - (d) No change.

(e) *Method of Record Retention.* Whenever a record is required to be preserved by this rule, such record may be retained either as an original or as a copy or other reproduction thereof, or on microfilm, ~~electronic or~~ magnetic tape, electronic storage media, or by the other similar medium of record retention, provided that such broker, dealer, ~~or~~ municipal securities dealer, or municipal advisor shall have available adequate facilities for ready retrieval and inspection of any such record and for production of easily readable facsimile copies thereof and, in the case of records retained on microfilm, ~~electronic or~~ magnetic tape, electronic storage media, or other similar medium of record retention, duplicates of such records shall be stored separately from each other for the periods of time required by this rule.

(f) *Effect of Lapse of Registration.* The requirements of this rule shall continue to apply, for the periods of time specified, to any broker, dealer, ~~or~~ municipal securities dealer, or municipal advisor which ceases to be registered with the Commission, except in the event a successor registrant shall undertake to maintain and preserve the books and records described herein for the required periods of time.

(g) No change.

(h) *Municipal Advisor Records*. Every municipal advisor shall preserve the books and records described in Rule G-8(h) for a period of not less than five years.

(i) *Municipal Advisor Records Related to Formation and Cessation of its Business*. Every municipal advisor shall comply with the provisions of Rule 15Ba1-8(b)(2) and (c) under the Act.

(j) *Records of Non-Resident Municipal Advisors.* Every non-resident municipal advisor shall comply with the provisions of Rule 15Ba1-8(f) under the Act.

(k) *Electronic Storage of Municipal Advisor Records Permitted.* Whenever a record is required to be preserved by this rule by a municipal advisor, such record may be preserved on electronic storage media in accordance with section (e). Electronic preservation of any record in a manner that complies with Rule 15a1-8(d) under the Act will be deemed to be in compliance with the requirements of this rule.

Alphabetical List of Comment Letters on Notice 2014-01 (January 9, 2014)

1. Acacia Financial Group, Inc.: Letter from Kim M. Whelan, Co-President, dated March 10, 2014

2. American Bankers Association: Letter from Cristeena G. Naser, Vice President and Senior Counsel, dated March 4, 2014

3. American Council of Engineering Companies: Letter from David A. Raymond, President and CEO, dated March 7, 2014

4. American Public Transportation Association: Letter from Michael P. Melaniphy, President and CEO, dated March 10, 2014

5. Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated March 10, 2014

6. Cape Cod Five Cents Savings Bank: Letter from Dorothy A. Savarese, President and Chief Executive Officer

7. Chancellor Financial Associates: E-mail from William J. Caraway, President, dated January 14, 2014

8. Coastal Securities: Letter from Chris Melton, Executive Vice President, dated March 10, 2014

9. College Savings Foundation: Letter from Mary G. Morris, Chair, dated March 10, 2014

10. College Savings Plans Network: Letter from Betty Everitt Lochner, Director, Guaranteed Education Tuition Program, dated March 10, 2014

11. Cooperman Associates: Letter from Joshua G. Cooperman dated March 10, 2014

12. Erika Miller: E-mail dated February 4, 2015

13. FCS Group: Letter from Taree Bollinger, Vice President, dated March 17, 2014

14. First River Advisory L.L.C.: Letter from Shelley J. Aronson, President, dated January 16, 2014

15. First Southwest Company: Letter from Hill A. Feinberg, Chairman and Chief Executive Officer, and Michael G. Bartolotta, Vice Chairman, dated March 7, 2014

16. Frost Bank: Letter from William H. Sirakos, Senior Executive Vice President, dated March 10, 2014

17. George K. Baum & Company: Letter from Guy E. Yandel, EVP and Head of Public Finance, Dana L. Bjornson, EVP, CFO and Chief Compliance Officer, and Andrew F. Sears, SVP and General Counsel, dated March 10, 2014

18. Government Finance Officers Association: Letter from Dustin McDonald, Director, Federal Liasion Center, dated March 13, 2014

19. Government Investment Officers Association: Letter from Laura Glenn, President, et. al., dated March 7, 2014

20. Investment Company Institute: Letter from Tamara K. Salmon, Senior Associate Counsel, dated March 4, 2014

21. J.P. Morgan: Letter from Paul N. Palmeri, Managing Director, dated March 10, 2014

22. Kutak Rock LLP: Letter from John J. Wagner dated March 10, 2014

23. Lamont Financial Services Corporation: Letter from Robert A. Lamb, President, dated March 10, 2014

24. Lewis Young Robertson & Burningham, Inc.: Letter from Laura D. Lewis, Principal, dated March 3, 2014

25. MSA Professional Services, Inc.: Letter from Gilbert A. Hantzsch, CEO, dated March 10, 2014

26. National Association of Bond Lawyers: Letter from Allen K. Robertson, President, dated March 18, 2014

27. National Association of Health and Educational Facilities Finance Authorities: Letter from Pamela Lenane, President, David J. Kates, Chapman and Cutler LLP, and Charles A. Samuels, Mintz Levin, dated March 10, 2014

28. National Association of Independent Public Finance Advisors: Letter from Jeanine Rodgers Caruso, President, dated March 10, 2014

29. National Healthcare Capital LLC: Letter from Richard Plumstead

30. New York State Bar Association, Business Law Section, Securities Regulation Committee: Letter from Peter W. LaVigne, Chair of the Committee, dated March 12, 2014

31. Northland Securities, Inc.: Letter from John R. Fifield, Jr., Director of Public Finance/Senior Vice President, dated March 7, 2014

32. Oppenheimer & Co. Inc.: E-mail from John Rodstrom dated March 10, 2014

33. Parsons Brinckerhoff Advisory Services, Inc.: Letter from Mark E. Briggs, President, dated March 10, 2014

34. Piper Jaffray: Letter from Frank Fairman, Managing Director, Head of Public Finance Services, dated March 10, 2014

35. Public Financial Management, Inc.: Letter from John H. Bonow, Chief Executive Officer, dated March 10, 2014

36. Public Resources Advisory Group: Letter from Thomas Huestis dated March 10, 2014

37. Raftelis Financial Consultants, Inc.: Letter from Lex Warmath dated March 10, 2014

38. Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated March 10, 2014

39. Sutherland Asbill & Brennan LLP: Letter from Michael B. Koffler dated March 10, 2014

40. Wells Fargo Advisors, LLC: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated March 10, 2014

41. Winters & Co. Advisors, LLC: Letter from Christopher J. Winters dated March 10, 2014

42. WM Financial Strategies: Letter from Joy A. Howard, Principal, dated March 10, 2014

43. Woodcock & Associates, Inc.: E-mail from Christopher Woodcock dated January 14, 2014

44. Wulff, Hansen & Co.: Letter from Chris Charles, President, dated March 17, 2014

45. Yuba Group: Letter from Linda Fan, Managing Partner, dated March 7, 2014

46. Zions First National Bank: Letter from W. David Hemingway, Executive Vice President, dated March 10, 2014

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ACACIA
FINANCIAL GROUP, INC.

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March 10, 2014

Mr. Ronal W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Dear Mr. Smith:

On behalf of my firm, Acacia Financial Group, Inc., I appreciate the opportunity to provide the following comments on Draft MSRB Rule G-42, on Duties of the Non-Solicitor Municipal Advisors, released on January 9, 2014.

Pertaining to the draft text of Rule G-42, we would propose the addition of the following underlined, bolded language to Draft Rule G-42(c)(ii) as follows:

"(c) *Documentation of Municipal Advisory Relationship.* A municipal advisor must evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship. The writing must be dated and include, at a minimum, … (ii) the reasonably expected amount of any such compensation (stated in dollars to the extent it can be quantified) **only if such reasonably estimated amount can be estimated at the time of such written documentation**."

Rationale: Many times a municipal advisory may be engaged, pursuant to an RFQ/RFP or otherwise, to become the municipal advisory to a client with little, if any, known or defined anticipated transaction plans provided by the municipal entity or obligated person at such time (e.g. a municipal entity or obligated person who issues an annual RFQ or RFP for municipal advisor services that may arise during the year, but without specifying what those transactions may be).

Pertaining to the draft text of Draft Rule G-42(d), as follows:

"(d) Recommendations. A municipal advisor must not recommend that its municipal entity or obligated person client enter into any municipal securities transaction or municipal financial product unless the advisor has a reasonable basis for believing, based on the information obtained through the reasonable diligence of the advisor, that the transaction or product is suitable for the client. In addition, the municipal advisor must discuss with its client:

(i) the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product;
(ii) the basis upon which the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is suitable for the client; and
(iii) whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives.

With respect to a client that is a municipal entity, a municipal advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest."

Question/Concern: How is a municipal advisor to address a situation wherein the municipal entity or obligated person either (a) has decided upon a pre-determined transaction (plan of finance) prior to the engagement of said municipal advisor to which the municipal would not recommend or (b) irrespective of the advice of the municipal advisor upon engagement, chooses to pursue a transaction (plan of finance) to which the municipal would not recommend. How is the municipal advisor to proceed in consideration of the above language?

Regarding Question 2 under General Matters as follows:

"2) Do commenters agree that a municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities should have an obligation, unless agreed to otherwise by the advisor and client, to review thoroughly the entire official statement? Should a municipal advisor be permitted to limit the scope of the engagement such that the advisor is not required to review the official statement? If so, under what circumstances should this limitation be allowed? Should any duty to review the official statement be limited to any portions of the official statement directly related to the scope of municipal advisory services?"

Response: We believe that municipal advisors level of duty regarding the review of the official statement should be limited to those sections directly related to the scope of the municipal advisory services. Further, we believe that in circumstances wherein the municipal advisor has been engaged to provide services in a capacity that does not include the participation in the preparation of the official statement (e.g. pricing services only), then the municipal advisor should not bear a level of duty to the review of the official statement. In both cases, the level of duty and scope of review could be articulated to the disclosure described in Draft Rule G-42(c)(iv) & (v).

Regarding Question 6 under General Matters as follows:

"7) Should a municipal advisor be required to obtain a written acknowledgment from the client of receipt of the conflicts disclosure and consent to any conflicts disclosed before proceeding with a municipal advisory engagement?"

Response: We believe that municipal advisors should <u>not</u> be required to obtain a written acknowledgement from the client of receipt of the conflicts disclosure and consent to any conflicts disclosed before proceeding with a municipal advisory engagement, but should be required to (i) provide such information (and record such provision), (ii) request receipt and consent, but (iii) be permitted to proceed with a municipal advisory engagement in the absence of such receipt and consent if the municipal advisor has a reasonable belief that such information has been received. This is analogous to

INTERPRETIVE NOTICE CONCERNING THE APPLICATION OF MSRB RULE G-17 TO UNDERWRITERS OF MUNICIPAL SECURITIES

Sincerely,

Kim M. Whelan
Co-President

American Bankers Association
Building Success. Together.

Cristeena G. Naser
Vice President and Senior Counsel
Center for Securities, Trust & Investment
202-663-5332
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BY ELECTRONIC MAIL

March 4, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314

Re: MSRB Notice 2014-01 – Draft MSRB Rule G-42 Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

The American Bankers Association (ABA)[1] appreciates this opportunity to comment on draft Rule G-42 proposed by the Municipal Securities Rulemaking Board (MSRB). The draft rule would establish standards of conduct and duties of municipal advisors, including the fiduciary duty required under Section 975 of the Dodd-Frank Wall Street and Consumer Protection Act (Dodd-Frank Act).[2] Our members and their affiliates provide a broad range of products and services to municipal entities and obligated persons in various capacities, including as municipal advisors.

Among other things, draft Rule G-42 would impose on municipal advisors a fiduciary duty to municipal entity clients, and the proposal seeks comment on whether that duty should be extended to clients that are obligated persons. In addition, with respect to both municipal entity and obligated person clients, municipal advisors would be subject to (1) a duty of care, (2) a prohibition on principal transactions by the municipal advisor and any of its affiliates with any advised municipal entity or obligated person, and (3) a requirement to disclose fully conflicts of interest and certain other information. As discussed more fully below, ABA has significant concerns about the proposal.

[1] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $14 trillion banking industry and its 2 million employees. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities. Learn more at www.aba.com.

[2] *Pub. L*. 111-203.

- First, a municipal advisor owes no fiduciary duty to obligated persons in the statute. As a result, the MSRB does not have the requisite authority to extend that duty to obligated persons.

- Second, draft Rule G-42 should be amended to state clearly that it does not apply to activities that have been excluded or exempted under the final municipal advisor rule of the Securities and Exchange Commission (SEC).

- Third, the complete prohibition on any principal transactions with advised municipal entities or obligated persons by the municipal advisor or *any of its affiliates* must be significantly narrowed, and should not apply in any event to affiliates. As drafted, it would disproportionately impact banking organizations[3] which are required by law to compartmentalize a variety of activities in affiliates that are separate from the commercial bank. In addition, the prohibition would effectively deprive a commercial bank of the opportunity provided by the SEC in its final rule[4] from organizing its municipal advisory activities in a separately identifiable department or division (SIDD), the whole purpose of which is to avoid subjecting the entire bank to the municipal advisory regulatory regime. Because banks almost always provide banking products and services in a principal capacity, the prohibition would prevent commercial banks and their affiliates from providing any other banking products, such as deposit accounts, loans, or cash management services to advised municipal entities or obligated persons despite the fact that these products and services are exempt from the municipal advisor regulatory regime. Principal transactions should be treated in the same manner as they are in other regulatory regimes, i.e., they are permissible with appropriate disclosure and client consent. In any event, no prohibition on principal transactions should extend beyond the advisory transaction or relationship.

DISCUSSION

1. **The MSRB has no authority to impose a fiduciary duty on municipal advisors with respect to obligated persons**.

In draft Rule G-42, the MSRB asks whether it should extend to obligated persons (who are private sector entities) the fiduciary duty imposed on municipal advisors with respect to municipal entities. Under a plain reading of Section 975, the MSRB has no authority to do so. In considering Section 975, Congress, had it wanted to do so, could easily have extended to obligated persons that fiduciary duty. Because Congress chose not to do so, neither can the MSRB.

Even if the MSRB had the requisite authority, such treatment would be completely unworkable in the real world. Obligated persons can include non-profit firms such as colleges and

[3] As used in this letter, the term "banking organizations" includes bank holding companies or any other group of companies that includes as an affiliate a commercial bank.
[4] *See* Registration of Municipal Advisors, Release No. 34-70462.

universities, and for profit firms become obligated persons when they become "conduit borrowers," *i.e.*, they work with municipal entities on the issuance of tax-exempt bonds for which the conduit borrower becomes the obligor. Such obligated persons can be multi-national corporations, such as Georgia-Pacific with far-flung operations and multiple needs for a broad range of financial services.[5] Identifying obligated persons is a huge challenge for the financial services industry under the SEC's final rule. Banks have hundreds, and in many cases thousands of customers, any one of which could become an obligated person without the bank's knowledge. Such customers have no independent obligation to inform the bank that they are an obligated person, and, although banks and their affiliates could ask private-sector firms to provide notification when they become obligated persons, such firms are under no obligation to do so. As a result, there is a significant risk to banks of an inadvertent regulatory violation by becoming an unwitting municipal advisor with respect to a person they do not know is an obligated person. That risk of violating registration requirements would be unfairly exacerbated by the risk of violating any attendant fiduciary duty.

2. Draft Rule G-42 should not apply to the provision of products or services that are either excluded or exempted under the SEC's final rule on municipal advisor registration.

In enacting Section 975, Congress specifically excluded certain activities from the municipal advisor regulatory regime. Likewise, in its final rule implementing Section 975, the SEC specifically exempted certain activities from that regulatory regime. However, draft Rule G-42 could be read to reach such activities, particularly with respect to the ban on principal transactions. Therefore, we urge the MSRB to confirm that any activities excluded and exempted by Congress or the SEC are outside the scope of the proposed rule.

3. The prohibition on principal transactions must be narrowed substantially.

Draft Rule G-42 would prohibit a municipal advisor and any of its affiliates from acting as principal in *any* transaction with entities or obligated persons. We believe that the proposed complete prohibition is far too blunt an instrument to address any concerns the MSRB may have regarding principal transactions. Nor has the MSRB provided support for its position that municipal entities and obligated persons, regardless of sophistication, are incontrovertibly unable to provide informed consent to principal transactions. ABA strongly disagrees with that position. Such a ban would also force banking organizations' municipal entity customers and

[5] See the detailed discussion of this issue under Section 3B.

obligated persons to decide to choose between receiving covered municipal advice or banking products and services from their banks, because banks would not be permitted to provide both.[6]

Indeed, as discussed below, there are other long-established fiduciary regimes in which principal transactions are permitted with disclosure of the conflict and informed consent by the client. Moreover, the imposition of a complete ban would place banking organizations at a significant competitive disadvantage to entities, such as registered investment advisers, that are excluded from municipal advisor registration and thus may engage in principal transactions subject to appropriate disclosure and consent by the advisory client. Accordingly, ABA believes that principal transactions must be permitted with appropriate disclosure and consent.

In addition, the extension of the prohibition to all transactions by affiliates of a municipal advisor is unwarranted and will ultimately restrict the ability of municipal entities and obligated persons to obtain financial products and services.

A. Other fiduciary regulatory regimes do not completely prohibit principal transactions.

Other fiduciary regulation regimes, including common trust law, state fiduciary law (including the Uniform Trust Code),[7] the Employee Retirement Income Security Act of 1974 (ERISA) and national and state banking regulations – all of which incorporate the highest, strictest form of "fiduciary duty" – do not completely prohibit principal transactions. Rather, such transactions may be permitted, depending on whether the advisor has investment discretion as well as on the provisions of the governing documents or applicable state law. ERISA provides for certain prohibited transaction exemptions that permit principal transactions by an ERISA fiduciary with the advised account.[8]

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[6] *See* ABA's letter to the MSRB on Draft Rule G-36 (April 11, 2011).

[7] Under the Uniform Trust Code, Section 802(f), Duty of Loyalty, "An investment by a trustee in securities of an investment company or investment trust to which the trustee, or its affiliate, provides services in a capacity other than as trustee, is not presumed to be affected by a conflict between personal and fiduciary interests if the investment otherwise complies with the prudent investor rule of [Article] 9. In addition to its compensation for acting as trustee, the trustee may be compensated by the investment company or investment trust for providing those services out of fees charged to the trust. If the trustee receives compensation from the investment company or investment trust for providing investment advisory or investment management services, the trustee must at least annually notify the persons entitled under Section 813 to receive a copy of the trustee's annual report of the rate and method by which that compensation was determined". Section 802(h)(4) provides that, "This section does not preclude the following transactions if fair to the beneficiaries: a deposit of trust money in a regulated financial-service institution operated by the trustee."

[8] ERISA Section 408(b)(4) provides an exemption from prohibited transactions for "The investment of all or part of a plan's assets in deposits which bear a reasonable interest rate in a bank or similar financial institution supervised by the United States or a State, if such bank or other institution is a fiduciary of such plan and if (A) the plan covers only

State and national banks and trust companies (hereinafter, bank fiduciaries) are subject to the requirements of many decades of fiduciary common law, federal fiduciary regulations for national banks and trust companies, and comparable fiduciary regulations under state law for state banks and trust companies. Banks must apply to the appropriate regulator to receive trust powers, providing evidence of personnel competent to provide investment management services and of capital to support the services in a safe and sound manner. They are examined regularly by state and federal bank regulators for compliance with trust law and trust principles.[9] In particular, the Office of the Comptroller of the Currency (OCC), which regulates national banks, has promulgated regulations at 12 CFR Part 9, Fiduciary Activities of National Banks, that have become the model for fiduciary regulations throughout the country. Importantly, those regulations govern conflicts of interest only with respect to the "fiduciary account," and do not attempt to restrict more broadly conflicts in all transactions with the fiduciary client.

Similarly, registered investment advisers (RIAs) are permitted, consistent with their fiduciary duty, to act as principal in transactions with advisory clients so long as the adviser obtains the client's consent after disclosure of (1) the adviser's capacity, (2) any compensation to be received by the adviser, and (3) any other relevant facts.[10] It is not insignificant that Congress excluded RIAs from the registration requirement under Section 975, because it believed that the existing regulatory scheme provided appropriate protection for municipal entities and obligated persons.[11]

B. The ban on principal transactions should not apply to affiliates of a municipal advisor.

Although a complete ban on principal transactions by affiliates might be feasible in the case of stand-alone advisors, it is entirely unreasonable and impractical in the context of the structure of the banking industry. Such a prohibition would necessarily force a banking organization to assess the value of providing advisory services to municipal entities and obligated persons as compared to the value of providing all other products and services to municipal entities and obligated persons. Whatever the determination, the clear result would be to curtail significantly

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employees of such bank or other institution and employees of affiliates of such bank or other institution, or (B) such investment is expressly authorized by a provision of the plan or by a fiduciary (other than such bank or institution or affiliate thereof) who is expressly empowered by the plan to so instruct the trustee with respect to such investment."

[9] OCC has published numerous handbooks on various aspects of fiduciary activities.

[10] *See*, Investment Advisers Act of 1940 § 206(3).

[11] National and state banks are exempt from registration as an investment adviser under federal and state law, because Congress and state legislators recognize the comprehensive regulatory requirements and robust supervisory oversight of banks offering investment advice.

the provision of services by banking organizations to municipal entities and obligated persons, without any offsetting policy benefits. Moreover, it would likely lead to less competition and reduced availability of services in the municipal advisory market.

Because of statutory restrictions on the activities of banks under federal banking law,[12] banking organizations are formed with numerous affiliates both in the U.S. and abroad that perform specific activities pursuant to differing national and international regulatory regimes. Domestically, a typical banking organization may include a commercial bank regulated under banking laws, a registered broker-dealer regulated under the Securities Exchange Act of 1934, and possibly a registered investment adviser regulated under the Investment Advisers Act of 1940. The bank may provide deposit, lending, cash management, and custody services to municipal entities and obligated persons, while the broker-dealer may provide underwriting services to them. Banking organizations may provide advice to these clients through an RIA or a bank trust department. Moreover, unlike the securities industry, commercial banking services (i.e., deposits, loans, and cash management services) are almost always provided in a principal capacity.

A complete prohibition on *any* principal transactions with entities or obligated persons by the municipal advisor or any of its affiliates would, in essence, prohibit a bank using a SIDD for its municipal advisory activities from providing any other banking products such as deposit accounts, loans, or cash management services to those clients. This would entirely defeat the purpose of a SIDD, which is to confine the applicability of municipal advisor rules to a specific department or division of the bank without extending the municipal advisor regulatory regime to the entire bank. A similar situation for the bank would arise should any bank affiliate, such as a broker-dealer, provide covered advice to a municipal entity or obligated person.

Moreover, it is unclear that banks would be able simply to cease providing services to municipal entities or, in particular, obligated persons, and thus banks would be in jeopardy of incurring a regulatory violation. For example, municipal entities, non-profit organizations, and private corporations that are deposit, lending, or investment clients of a bank could make an offering of municipal securities with which neither the bank nor any of its affiliates was involved or had knowledge of. Further, if a bank learns that such a private corporation to which it has made a loan has become an obligated person, the bank would not necessarily be able to accelerate the

[12] *See, e.g.,* The National Bank Act, 12 U.S.C. § 21 *et seq.* and The Bank Holding Company Act, 12 U.S.C. § 1841 *et seq.*

repayment of a loan. Nor could it immediately cease providing deposit and cash management services to the corporation. Indeed, if the bank was the primary or sole provider of such services, immediate cessation could cause significant disruption to the corporation's business operations. Similarly, if a bank's trust department is providing advice to a private company's pension plan, it may not immediately be able to end its fiduciary relationship because it learns that an affiliate has provided advice on the company's conduit bonds.

Such a ban would ultimately disserve municipal entities and obligated persons. Both groups, like other bank and brokerage clients, seek a variety of services from financial institutions, many of which are unrelated to the issuance of municipal securities or municipal financial products. Examples would include custodial services for funds other than bond proceeds, cash management services, the investment of cash balances (i.e., "sweeping" cash balances) in money market mutual funds (assuming that such investments constitute principal transactions under draft Rule G-42), currency exchange services, loans for specific purposes, lockbox services for tax and fee collection, payroll deposit/payment accounts for their employees, and bond trustee services.

Obligated persons in a municipal financing are even more diversified in the range of services they seek from banking organizations. Many of these private sector firms are national or even multi-national in scope. For example, Georgia Pacific uses tax-exempt municipal financing to build pulp processing plants in economically depressed areas; for-profit health care corporations operate hospitals and clinics in a number of states; and airlines finance gate construction at different airports through tax-exempt bonds issued by a local municipal entity that are backed by the gate lease revenues collected by the airport. These last transactions, for example, are almost always without recourse to the municipal entity except with respect to the rights to the gate lease revenues that are pledged as security for the municipal entity's conduit loan to the obligated person. These types of organizations seek numerous services from banking organizations that are wholly unrelated to the issuance of municipal securities or municipal financial products, such as deposits and cash management services, letters of credit, revolving financing facilities, mortgages, or other types of loans.[13]

However, under draft Rule G-42, the provision of municipal advisory services to an obligated person on a single transaction, would trigger a complete ban on principal transactions by the

[13] We note that banks are prohibited by anti-tying laws from tying lending approval to the purchase of other banking or bank-affiliated products or services. *See,* Section 106 of the Bank Holding Company Act Amendments of 1970, 12 U.S.C. § 1972.

municipal advisor and all of its affiliates with the entire obligated person firm, whether or not those transactions are related to the advisory transaction. Thus, if a bank-affiliated broker-dealer were to advise an airline company on a tax-exempt financing in California, the bank itself could not make a loan to buy planes or permit the airline company to make deposits into the bank for any purpose. Nor could that broker-dealer sell investments to the airline's self-managed deferred executive compensation fund. If that broker-dealer were to advise a healthcare corporation about hedging a tax-exempt new hospital financing in Ohio through the use of a derivative, the bank could not offer a revolving facility to replace MRI equipment for clinics in Oregon. Moreover, custody clients of banks often use bank-affiliated broker-dealers to effect securities transactions on their behalf. Such transactions for equity securities are effected on an agency basis and are permitted with appropriate disclosures. However, such transactions in debt securities (such as for government securities) are effected on a principal basis and so would be prohibited.

This is but a sampling of the types of ordinary banking transactions that would be prohibited under draft Rule G-42. It should be clear from these examples that there is, in fact, no inherent conflict of interest in a banking organization acting as municipal advisor to an obligated person for a tax-exempt financing on one transaction and then its affiliate or even the bank itself, acting as a principal in a wholly unrelated arm's-length transaction. Congress surely did not intend to disrupt both municipal and private sector markets so significantly.

As noted above, draft Rule G-42 as a practical matter will not work for a municipal advisor firm that has affiliates. For banking organizations that typically have asset management, advisory, banking, wealth management, and other subsidiaries, merely tracking the multiple relationships with advised counterparties is already difficult. Such firms typically have internal conflict checks that make sure they do not inadvertently find themselves providing advice to two parties to the same transaction. But to comply with the rule as proposed, a banking organization, before seeking an engagement with a municipal entity or obligated person, would need to be sure that none of its affiliates was engaged in any kind of ongoing principal transactions anywhere in the world with that client. This is a nightmarishly complex task, and one in which predictable inadvertent oversights could lead to unintended regulatory violations.

The following example is illustrative. Assume that a bank-affiliated broker-dealer has been engaged by an airline as a municipal advisor on a tax-exempt gate-lease revenue-backed transaction, which would make the airline an obligated person. At the same time, the broker-

dealer's commercial bank affiliate is also negotiating an ordinary commercial loan with the airline for a cargo facility in another state. For reasons of negotiating strategy, the parties have signed non-disclosure agreements. Therefore, neither affiliate will know that the other may be providing services to the same entity. If both transactions are completed, there would be a violation of the rule, yet neither party would be aware of the violation. On the other hand, if there was no confidentiality agreement in place and the affiliates learned of the negotiations, what should be done? Should the bank be allowed to complete the loan or must it back out? What if the bank has already signed a contingent commitment letter months before that only surfaces after the broker-dealer accepted a municipal advisory role? In this and similar cases, the result for the airline is that its funding processes may be disrupted with no observable benefit. For all of the above reasons, we urge the MSRB *not* to extend any restrictions on principal transactions to affiliates of a municipal advisor.

C. Any prohibition on principal transactions should apply only to the municipal advisor with respect to matters directly related to the municipal advisory transaction or relationship.

Any consideration of restrictions on principal transactions should be limited only to municipal advisors and to matters concerning the advisory transaction or relationship. We note that this formulation is the same one proposed in the MSRB's 2011 draft Rule G-36 in which the prohibition on principal transactions applied only to matters concerning the "municipal advisory engagement."[14] We believe that this scope would appropriately address concerns about conflicts of interest, while preserving the current range of services to municipal entities and obligated persons.

We note that those entities providing advice to advised municipal entities or obligated persons that enjoy an exclusion from municipal advisor registration requirements are free to engage in principal transactions. As discussed above, RIAs may, consistent with their fiduciary duty under the Investment Advisers Act of 1940, engage in principal transactions with their advisory clients with disclosure and consent. The differing regulatory regime would create a significant competitive disadvantage for banking organizations, particularly with respect to the provision of investment management and advisory services, because a banking organization would be subject to Rule G-42's prohibition on principal transactions while an RIA providing exactly the same services would not. We believe that when Congress exempted RIAs from municipal

[14]MSRB Notice 2011-48 (August 23, 2011). *See also,* SEC Municipal Advisor Frequently Asked Questions at 5.2, (January 16, 2014).

advisor registration, it was mindful of the fiduciary duty of investment advisers, believing that an RIA's advisory clients were protected under that regulatory regime, including with respect to principal transactions. No policy reason supports the proposed disparate treatment.

4. Compliance with bank fiduciary regulations should satisfy the draft Rule G-42's requirements for municipal advisors.

Banks provide a range of investment management and advisory services in their fiduciary capacity through trust departments and trust companies (hereinafter, bank fiduciaries), and may be required to register as municipal advisors, because they provide advice with respect to proceeds from an offering of municipal securities. Their municipal advisory activities arise generally in the context of providing advice either to separately managed accounts in which pension plans offered by municipal entities invest, or to collective investment vehicles in which advised municipal entities or obligated persons invest.

Bank fiduciaries are subject to the strictest fiduciary duty under state and federal banking, trust, and common law.[15] A bank fiduciary is required by a long history of case law to put the interests of account beneficiaries before the interests of the bank. The bank fiduciary owes its beneficiaries undivided loyalty and must administer each trust for the exclusive benefit of account beneficiaries and the purposes for which the account was created.[16] For all fiduciary clients, including retirement plans, national banks must comply with 12 CFR Part 9, while state-chartered banks must comply with applicable state fiduciary and trust law and regulation, which often defers to the requirements under 12 CFR Part 9. To the extent a bank fiduciary obtains investment discretion with respect to, or control of, ERISA retirement plan assets, the bank becomes a fiduciary to the plan under ERISA.[17] In addition, bank fiduciaries are examined regularly by state and federal bank examiners for compliance with state and federal fiduciary laws and regulations.

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[15]Judge Cardoza's famous quote in *Meinhard v. Salmon*, 249 N.Y. 458 at 464 (1928) exemplifies the standards to which bank fiduciaries are held: "Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior."

[16]*See*, OCC Handbook on Collective Investment Funds at 12 ("It is a bank's fundamental duty to administer its [collective funds] solely in the interest of the bank's fiduciary customers whose assets are invested in the funds. When a bank makes a determination that a CIF serves as a prudent alternative to an individualized investment strategy for a fiduciary account, it must ensure that the CIF used is appropriate for each account. The duty of loyalty is critical and underlies the administration of a CIF.). *See also,* OCC Handbook on Conflicts of Interest.

[17] Although municipal entities' pension plans are not covered by ERISA, they often invest in collective funds that are subject to ERISA (because other clients in the funds are). As a result, ERISA and its requirements for fiduciaries often apply to collective investment funds.

Pursuant to this regulatory regime, bank fiduciaries are already required to provide to clients disclosures of conflicts of interest, and fee and compensation arrangements. Bank fiduciaries typically enter into investment management agreements (or equivalent agreements) that document the client relationship, fees, conflicts of interest, duties and obligations, term, and termination arrangements. Banks are also required to undertake initial and periodic account reviews pursuant to 12 CFR Part 9, which are comparable to the suitability determinations described in draft Rule G-42.[18] Further, bank fiduciaries are required to maintain detailed records of fiduciary accounts and to "know their customer" under federal banking law and regulation.

Draft Rule G-42 would impose significant regulatory requirements that overlap but are not coextensive with the robust regulatory regime with which bank fiduciaries must currently comply. We are very concerned that applying the rule's requirement to bank fiduciaries would impose on bank fiduciaries a duplicative and conflicting regulatory regime with no observable benefit to fiduciary clients, who ultimately would bear the costs of such redundant regulation. In addition, bank fiduciaries would also be at a competitive disadvantage with RIAs who would not be subject to such duplicative regulation.

Accordingly, we strongly urge the MSRB to recognize that the existing regime of bank fiduciary regulation, under which bank fiduciaries are regularly examined for compliance by knowledgeable examiners, constitutes effective compliance with draft Rule G-42. We would be happy to provide additional detailed information on the bank fiduciary regulatory regime.

[18] Draft Rule G-42 would impose a suitability requirement to "only recommend a transaction or product that is in the [client's] best interest." However, the suitability considerations identified in the rule appear to be targeted at municipal securities transactions and products rather than the types of products provided by bank collective funds and separately management accounts that operate under investment guidelines. For example, it is unclear whether and how suitability requirements would be imposed on investment management recommendations or decisions by a trust bank (acting as trustee to a collective investment vehicle or as manager of a client's separate account). Clients typically retain a trust bank to perform discretionary investment management where the investment decisions are subject to investment guidelines applicable to a fund authorized by the client, or guidelines specifically agreed to by the client.

5. Other Issues

Draft Rule G-42 would require municipal advisors to disclose information concerning their professional liability insurance coverage. We believe that given the capital requirements and risk management programs at banks, as well as robust supervision by the banking regulators, disclosure of the amount of professional insurance is unnecessary. Moreover, we are concerned that the proposal might require banks to disclose proprietary information.

With respect to the economic analysis in draft Rule G-42, ABA is concerned that the MSRB has failed to take into account the costs to banking organizations of compliance as well as the impact on municipal entities and obligated persons from the consequent inability to access financial services and products. As just one example, should the MSRB apply the prohibition on principal transactions to all affiliates of a municipal advisor, banking organizations would incur enormous costs simply to try to track potential transactions with a municipal entity or obligated person across all affiliates. These increased costs would clearly be passed through to customers. We are happy to discuss these concerns further with the MSRB.

CONCLUSION

ABA has considerable concerns with draft Rule G-42. The complete prohibition on principal transactions must be substantially narrowed to exclude affiliates and to permit principal transactions with disclosure and consent. If not significantly modified, the rule would force banking organizations to choose whether to provide advisory services to municipal advisors and obligated persons, or provide the full range of loans, deposits and other banking products and services they offer to such clients; banks would be unable to offer both to their customers.

Any resulting reduction in the availability of services would disserve those clients for no public benefit. ABA believes that extending a municipal advisor's fiduciary duty to cover obligated persons is not authorized by Section 975 and is contrary to Congressional intent. We urge the MSRB to confirm that draft Rule G-42 does not apply to activities that have been excluded or exempted under the SEC's final municipal advisor rule. Moreover, no prohibition on principal transactions should extend beyond the advisory transaction or relationship.

We stand ready to provide additional information that may be useful to the MSRB, particularly with respect to bank fiduciary activities, as you move forward with this proposed rule. Please do not hesitate to contact me with any questions.

Sincerely,

Cristeena G. Naser

cc: Lynette Kelly, Executive Director
Municipal Securities Rulemaking Board

Ernesto Lanza, Deputy Executive Director
Municipal Securities Rulemaking Board

Gary Goldsholle, General Counsel
Municipal Securities Rulemaking Board

Michael Post, Deputy General Counsel.
Municipal Securities Rulemaking Board

Kathleen Miles, Associate General Counsel
Municipal Securities Rulemaking Board

John Cross, Director of Municipal Securities Office
Securities & Exchange Commission

ACEC
AMERICAN COUNCIL OF ENGINEERING COMPANIES
100 Years of Excellence

DAVID A. RAYMOND
PRESIDENT & CEO

March 7, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314

Re: MSRB Draft Rule G-42

Dear Mr. Smith:

On behalf of the American Council of Engineering Companies (ACEC) – the national voice of America's engineering industry – I appreciate the opportunity to comment on the Municipal Securities Rulemaking Board's (MSRB) draft rule G-42, regarding the duties of non-solicitor municipal advisors.

ACEC members – numbering more than 5,000 firms representing hundreds of thousands of engineers and other specialists throughout the country – are engaged in a wide range of engineering works that propel the nation's economy, and enhance and safeguard America's quality of life. Many of our member firms work with municipal clients and could potentially be affected by the municipal advisor registration rule and related regulations.

As you know, Section 975 of the Dodd-Frank financial services reform law requires "municipal advisors" to register with the Securities and Exchange Commission (SEC) and the MSRB. The statute contains an exemption from registration for "engineers providing engineering advice." The final municipal advisor registration rule approved by the SEC on September 18, 2013 includes additional exemptions, such as the general information exemption and the independent registered municipal advisor exemption, which may be utilized by engineering firms. However, the SEC's definitions of municipal advisor and advice in the final rule may not fully shield all engineers from registration.

There is a potential conflict for engineers that register as municipal advisors and must therefore assume the fiduciary duties outlined in MSRB draft rule G-42. The draft rule states: "A municipal advisor to a municipal entity client shall, in the conduct of all municipal advisory activities for that client, be subject to a fiduciary duty that includes a duty of loyalty and a duty of care." A duty of loyalty requires a municipal advisor to deal

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honestly and in good faith with the municipal entity and to act in the municipal entity's best interests without regard to financial or other interests of the municipal advisor. While this duty may not, in the normal course of events, cause any conflicts for the engineer, there are circumstances when such duties could come into direct conflict with the engineer's professional and ethical responsibilities.

Engineering is a profession that is heavily regulated by state boards of engineering, and is founded on professional credentials and personal integrity as a condition of licensure. The regulations of the various state licensing boards for professional engineers delineate the ethical duty of the engineer to uphold the safety, health, and welfare of the public. For example, the Commonwealth of Virginia's Board for Architects, Professional Engineers, Land Surveyors, Certified Interior Designers, and Landscape Architects' current regulations, which have the force and effect of law, provide as follows:

> *The primary obligation of the professional is to the public. The professional shall recognize that the health, safety, and welfare of the public are dependent upon professional judgments, decisions, and practices. If the professional judgment of the professional is overruled under circumstances when the health, safety, and welfare, or any combination thereof, of the public are endangered, the professional shall inform the employer and client of the possible consequences and notify appropriate authorities.*

The same obligation is reflected in the codes of ethics of private professional associations such as ACEC and the National Society of Professional Engineers (NSPE), as well as related professional associations such as the American Institute of Architects (AIA).

In the course of providing professional engineering services to a client, circumstances could arise in which the engineer would find himself or herself facing a conflict between breaching the fiduciary obligations of a municipal advisor and violating the ethical obligations imposed upon the engineer under applicable state licensing board regulations and/or one or more professional associations. In such a circumstance, it would be detrimental to the health, safety, and welfare of the public to prioritize the engineer's fiduciary duty to his or her client. By failing to address such a conflict, MSRB draft rule G-42 does not serve the interests of the public.

Based on these concerns, we respectfully request that the MSRB address how the conflict between an engineer's duty to public health and safety and fiduciary duty to a municipal client can be managed.

In addition to conflicts related to engineering codes of ethics, the same fiduciary and duty of loyalty provisions can be in conflict with normal expectations when engineering firms are involved in demand and revenue forecasting. An example would be traffic and revenue forecasts for a toll facility. In that role, the engineer is expected to operate independently of the client as he or she prepares estimates of revenue. These forecasts may be at odds with client expectations, yet this "arm's length" relationship is essential to the credibility of the study product. In this role, engineers are not actually serving as

'advisors' to the client, but rather as independent forecasters providing a critical component to the design process. Once again, we ask the MSRB to address how the engineer can manage the conflict between these requirements.

In its notice, the MSRB specifically requested comment on whether the municipal advisor's fiduciary duty should be limited to a municipal advisor's municipal entity clients. This question is pertinent to engineering firms that register as municipal advisors, in terms of the professional services they provide to different municipalities. It is likely that an engineering firm that registers as a municipal advisor will have municipal clients for which it does purely technical engineering work. It would be inappropriate to impose fiduciary duty on the engineering firm in such circumstances. Requiring engineering firms that register as municipal advisors to assume a fiduciary duty toward all municipal entity clients would, as noted above, provide fertile ground for a conflict between the engineer's primary ethical duty to protect public health, safety and welfare, and the fiduciary's duty to protect the interests of his or her client.

The MSRB also requested comment on whether to require disclosure of the amount of professional liability insurance (PLI) carried by a municipal advisor. We question whether this information would provide a benefit to municipalities seeking to hire municipal advisors. The amount of PLI coverage would not appear to correlate with the experience and qualifications of the municipal advisor, or the quality of their services.

In addition, there is significant uncertainty whether PLI carried by engineers would cover fiduciary duty that goes beyond the standard of care, such as design flaws, to a duty of loyalty. If claims arising out of an alleged breach of a fiduciary duty are not be covered by the engineering firm's current PLI policy, the firm would face two choices. The firm could elect to acquire additional insurance coverage, the cost of which would be passed along to all of the firm's clients through the firm's general and administrative overhead rate regardless of the nature of the firm's services on behalf of any given client. Alternatively, as the MSRB's current regulations do not require a municipal advisor to maintain professional liability insurance covering fiduciary duties, the firm could elect not to procure such additional insurance coverage so as to avoid having to increase the cost of its services to all of its clients in a very competitive environment.

Finally, the MSRB asked whether the compliance costs associated with registration as a municipal advisor would be passed on to municipal entity clients in the form of higher fees. It seems reasonable to assume that at least some portion of these costs will be reflected in higher contract prices. The filing, record-keeping, and employee training costs are too substantial for most engineering firms to absorb. We expect that the municipal entity client would pay for some part of the additional services, such as fiduciary duty and associated insurance costs, which they will be receiving from registered municipal advisors. As an example, the Federal Acquisition Regulation, which regulates the work of engineering firms and other federal contractors, generally allows the legal and regulatory costs of doing business to be charged to the client.

We respectfully request that the MSRB consider the issues we have raised. Thank you for your consideration of our comments, and we look forward to working with the MSRB as the rulemaking process moves forward.

Sincerely,

David A. Raymond
President & CEO

AMERICAN PUBLIC TRANSPORTATION ASSOCIATION

March 10, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314

RE: MSRB Draft Rule G-42

Dear Mr. Smith:

On behalf of the more than 1,500 member organizations of the American Public Transportation Association (APTA), I write to provide comments on the Municipal Securities Rulemaking Board's (MSRB) draft rule G-42 concerning the duties of non-solicitor municipal advisors, which was published on January 9, 2014.

About APTA

APTA is a non-profit international trade association of more than 1,500 public and private member organizations, including public transit systems; high-speed intercity passenger rail agencies; planning, design, construction and finance firms; product and service providers; academic institutions; and state associations and departments of transportation. More than ninety percent of Americans who use public transportation are served by APTA member transit systems.

APTA speaks for its members. Its Board of Directors reiterated that fact on March 9, 2013, when it adopted the following statement: "While APTA encourages its members to provide specific examples or impacts in support of the association's positions, APTA crafts its comments to represent those of all APTA members. The association goes to great lengths to ensure its regulatory comments represent the consensus views of our members. Every APTA member has the opportunity to review drafts, participate in discussions, and assist in crafting those consensus comments. In short, we speak with a single voice and, when the rare instance occurs that we cannot reach consensus, we do not speak at all. APTA's comments are those of our more than 1,500 members. This consensus-based method of crafting regulatory comments is a factor underlying APTA's selection as one of Washington's most trusted brands in a broad survey conducted by the National Journal and we encourage all federal agencies to recognize the representative nature of the association's regulatory comments."

Summary Comments

As drafted, rule G-42 could effectively halt public transportation projects, most funded with assistance from the US Department of Transportation through the Federal Transit Administration (FTA). Specifically, we are concerned that the Federally-mandated planning process that supports decision making leading to the issuance of securities (the work that engineering firms do) is being viewed by MSRB in the same context as the marketing of specific securities (the work that underwriters, investment bankers, and independent financial advisors do). For that reason, we request activities conducted by engineering and consulting firms pursuant to public transportation planning and oversight under the provisions of Title 49, United States Code, Chapter 53, be deemed "engineers providing engineering advice" and specifically exempted from coverage under the rule.

Financial Planning Associated with Public Transportation Investments

It has long been a practice of FTA to rely upon transportation planning professionals – and not municipal advisors – for financial analysis in the planning process leading up to (but not including) the issuance of debt.

FTA's expectations regarding the level of detail and integration between engineering, transportation planning, and financial planning is well-documented and long standing. FTA's involvement, through its Office of Planning, began in the mid-1970s on the Washington Metrorail Alternatives Analysis and the early 1980s in several other Alternatives Analyses (e.g., Houston, Miami) and other major investment projects. FTA was particularly concerned with the ability of project sponsors to develop realistic, well-documented financial projections that demonstrated their capacity to not only construct and operate the proposed projects but also to continue – over the long-term – to operate the underlying existing transit services and renew and replace the assets that supported those services. Among its concerns was the internal consistency among the various inputs to the financial plans (e.g., that the same demographic projections were applied to project ridership and fare revenue as well as dedicated tax revenue; that the same level of service projections were applied to project ridership and fare revenue as well as operating and maintenance cost; that the average fare paid per passenger – and future increases – applied in the projection of fare revenue were applied to project ridership). Understanding these internal consistencies and the integration of the highly technical results of the planning and engineering disciplines demanded that this work be executed by transportation planning professionals.

From the late 1980s through the early 2000s, FTA developed its New Starts planning process and specific requirements for the development of financial plans. These requirements emphasized the integration of engineering, travel demand modeling, urban planning, environmental planning, and financial planning.

By the late 1980s, FTA engaged engineering and consulting firms subject to the municipal advisor rule to develop and teach courses on financial planning for major transit investments. Subsequently, under contract to FTA's grantee, the National Transit Institute (NTI), firms now subject to the rule have developed and delivered the NTI course on "Financial Planning in

Transportation." The audience for that course includes transit agencies, metropolitan planning organizations, and state departments of transportation.

Specific FTA Requirements for the Development of Financial Plans

The following documents establish the professional standards that FTA expects of its project sponsors for the development of financial plans:

- Alternatives Analysis (Corridor Planning) Financial Plans - Procedures and Technical Methods for Transit Project Planning. http://www.fta.dot.gov/planning/newstarts/planning_environment_2396.html See Part II, Chapter 8 Financial Planning for Transit.
- New Starts Financial Plans - Guidance for Transit Financial Plans. http://www.fta.dot.gov/publications/reports/other_reports/publications_1336.html See attachment "gftfp.pdf"
- New and Small Starts Evaluation and Rating Process Final Policy Guidance, August 2013, http://www.fta.dot.gov/documents/NS-SS_Final_PolicyGuidance_August_2013.pdf
- Full-Funding Grant Agreements Guidance Circular 5200.1A http://www.fta.dot.gov/laws/circulars/leg_reg_4119.html. This includes several references to the depth analysis of the financial plan (e.g., Chapter II, Section 8; references to "Local Financial Commitment").

Extent and Limits to the Scope of Work of Firms Developing New Starts Financial Plans

Engineering and consulting firms supporting project sponsors develop financial plans subject to the above noted regulations and guidance. FTA relies on those financial plans in its determination of which of many competing projects are recommended to Congress for funding. Fifty percent of the evaluation score FTA assigns to projects during its review is based on "financial commitment," which is evidenced by the financial plans.

It should be noted that FTA does not intend the financial plans developed to satisfy its evaluation and oversight functions to be applied to support the actual issuance of a particular security, nor are they suited for that purpose. FTA's intent is solely to support the planning process leading to the federal commitment to proceed with a project. Once that commitment is reached, engineering and consulting firms step back and independent financing advisors step forward to prepare the financial plan that is actually presented to investors. An example of this kind of "hand-off" was the development of the financial plan for the New Starts submission of the San Francisco Municipal Transportation Agency (SFMTA). The financial plan was initially developed by an engineering firm and SFMTA used the results of that financial plan in its New Starts submissions to FTA. Once SFMTA committed to the plan, they engaged their independent financial advisor to prepare the financial plan that was the basis for the actual issuance of debt.

Long-Term Perspective of New Starts Financial Plans

The financial planning work examines specific funding sources, typically dedicated taxes and the timing and rates of taxation necessary to support the issuance of debt to fund the projects examined. These analyses include cash flow analyses (with a 20- to 30-year planning horizon), including consideration of alternative forms of short- and long-term debt financing. These cash flow analyses typically address alternative project implementation schedules within the context of uncertainty with respect to project cost, inflation and interest rates, ridership and market response to fare increases, dedicated non-federal funding, and the level and timing of federal grant funding. FTA expects that financial plans submitted that include debt financing be able to demonstrate that the financial tests applied by the project sponsor (e.g., debt service coverage) be consistent with issuance of prior debt or meet conventional expectations of the capital market.

In most cases, the financial plans submitted to FTA address the entirety of the financial obligations of the project sponsor. The capital needs addressed include not only the proposed New Starts project, but also the continuing infrastructure renewal and replacements needs of the project sponsor, the cumulative cost of which – over the analysis period – typically exceeds the construction cost of the New Starts project. As a result, these financial plans project the need for multiple (possibly annual) debt issuances throughout 20- to 30-year planning horizon. This long-range perspective greatly surpasses the relatively narrow intent of the rule which appear to focus solely on a specific near-term financing.

FTA Does Not Expect Third Parties to Rely on New Starts Financial Plans

Some of the firms previously engaged in preparing financial plans responding to FTA regulation and guidance are or were associated with Certified Public Accounting firms. Such firms followed the professional Prospective Financial Reporting Guidelines of the American Institute of Certified Public Accountants (AICPA) and these guidelines have implicitly become integrated within FTA expectations for standards of practice. In particular, the AICPA Guidelines fundamentally distinguish between prospective financial reports which are for internal use only (that is, financial planning studies) and prospective financial reports which are relied on by third parties (that is reports which are included in the Offering Statements or Official Statements (OSs) associated with the issuance of securities). The standards and disclosure requirements with regard to prospective financial reports which are relied upon by third parties (that is, investors) are and should be far more stringent that the corresponding requirements for internal use only reports. FTA did not and does not expect that the financial plans developed to support its regulations and guidance rise to the standards of financial plans to be relied upon by third parties.

FTA Expects Consideration of Alternative Forms of Financing in New Starts Financial Plans

FTA has advocated specific alternative forms of financing (e.g., TIFIA loans) and alternative forms of project delivery. FTA and its sister agency, the Federal Highway Administration (FHWA) funded the development of state-of-the-practice reports regarding financing, including:

- "Financing Capital Investment: A Primer for the Transit Practitioner Public-Private Partnerships." Transit Cooperative Research Program, Report 89, 2003, *http://onlinepubs.trb.org/Onlinepubs/tcrp/tcrp_rpt_89a.pdf*
- National Cooperative Highway Research Program. "Future Financing Options to Meet Highway and Transit Needs." Web-only Document 102. December 2006. http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_w102.pdf

These reports were intended to provide project sponsors with financing options. While FTA makes no demands that such financing structures be implemented, it encourages project sponsors to consider such options. FTA has been satisfied that the engineering and consulting firms that the project sponsors engaged to prepare financial plans have adequately addressed such options.

FTA specifically does not consider the financing structure applied in the New Starts financial plan submitted to FTA as a "recommendation." It recognizes that the ultimate decision about the structuring of the debt will depend upon the future financial condition of the project sponsor and capital market conditions, which may change subsequent to the development of financial plans submitted to FTA.

Failure to Exempt These Services from Coverage Under Rule G-42 Would Create a Conflict of Interest for Engineering Firms

The draft rule states: "A municipal advisor to a municipal entity client shall, in the conduct of all municipal advisory activities for that client, be subject to a fiduciary duty that includes a duty of loyalty and a duty of care." A duty of loyalty requires a municipal advisor to deal honestly and in good faith with the municipal entity and to act in the municipal entity's best interests without regard to financial or other interests of the municipal advisor. While this duty may not, in the normal course of events, cause any conflicts for engineers, there are circumstances when such duties could come into direct conflict with the engineer's professional and ethical responsibilities.

As extensively explained by our colleagues from the American Council of Engineering Companies (ACEC), engineering is heavily regulated by state boards of engineering, and is founded on the assessment of professional credentials and personal integrity as a condition of licensure. The regulations of the various state licensing boards for professional engineers delineate the ethical duty of the engineer to uphold the safety, health, and welfare of the public. For example, the Commonwealth of Virginia's Board for Architects, Professional Engineers, Land Surveyors, Certified Interior Designers, and Landscape Architects' current regulations, which have the force and effect of law, provide as follows:

The primary obligation of the professional is to the public. The professional shall recognize that the health, safety, and welfare of the public are dependent upon professional judgments, decisions, and practices. If the professional judgment of the professional is overruled under circumstances when the health, safety, and welfare, or any combination thereof, of the public are endangered, the professional shall inform the employer and client of the possible consequences and notify appropriate authorities.

The same obligation is reflected in the codes of ethics of private professional associations such as ACEC and the National Society of Professional Engineers (NSPE), as well as related professional associations such as the American Institute of Architects (AIA) and the American Society of Civil Engineers.

In the course of providing the services described above to public transportation project sponsors, it is conceivable that circumstances could arise in which the engineer would find himself or herself facing a conflict between breaching the fiduciary obligations of a municipal advisor and violating the ethical obligations imposed upon the engineer under applicable state licensing board regulations and/or one or more professional associations. These conflicting ethical obligations would create a Hobson's choice for these professionals and their firms.

Faced with Impossible Choices, Engineering Firms Could Elect to Withdraw from the Public Transportation Market Altogether

The number of engineering firms with the necessary skill set to undertake public transportation project planning under the FTA's extensive New Starts program framework is quite limited and the universe of transit projects relatively small. Financial analysis, as described above, is an integral part of that planning process and cannot reasonably be separated from the myriad other tasks. With the threat of conflicting professional obligations, draft rule G-42 could effectively force those firms from our limited market.

We appreciate the opportunity to assist in this important rulemaking. For additional information, please contact James LaRusch, APTA's chief counsel and vice president corporate affairs, at (202) 496-4808 or jlarusch@apta.com.

Sincerely yours,

Michael P. Melaniphy
President & CEO

MPM/jpl

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March 10, 2014

VIA ELECTRONIC MAIL

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Regulatory Notice 2014-01 (January 9, 2014): Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

On behalf of the Bond Dealers of America ("BDA"), I am pleased to submit this letter in response to Municipal Securities Rulemaking Board ("MSRB") Regulatory Notice 2014-01, regarding draft Rule G-42 ("Draft Rule G-42") on the standards of conduct and duties of municipal advisors when engaging in municipal advisory activities other than the undertaking of solicitations. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")[1], Congress, among other things, amended Section 15B of the Securities Exchange Act of 1934 ("Exchange Act") to provide for the regulation by the Securities and Exchange Commission ("SEC") and the MSRB of municipal advisors and to grant the MSRB certain authority to protect municipal entities and obligated persons. The Dodd-Frank Act accordingly grants the MSRB broad rulemaking authority over municipal advisors and municipal advisory activities. We recognize that Draft Rule G-42 is one step in the establishment of a regulatory framework for municipal advisors and we welcome this opportunity to state our position and provide these comments.

[1] *See* Pub. Law No. 111-203, 124 Stat. 1376 (2010).

General

The BDA has supported and welcomes the regulation of municipal advisors through the municipal advisor rule of the SEC (the "Municipal Advisor Rule")[2] and the rules of the MSRB which will help to establish and govern the conduct standards for municipal advisors. We have concerns, however, about Draft Rule G-42 in its current form. In particular, we are concerned about the interaction between the SEC's approach to defining a municipal advisor using an activities-based approach and the MSRB's approach to defining a financial advisor which has been traditionally transaction-based. How the concept of a financial advisor relates to the concept of a municipal advisor is very important. The SEC Municipal Advisor Rule and the MSRB rules, including Draft Rule G-42, cannot function independently of each other. We would like to warn the MSRB to strongly consider how it exercises its broad rulemaking authority over municipal advisors and municipal advisory activities and examine how the rules created pursuant to this authority will interact with the SEC's Municipal Advisor Rule in governing and proscribing the duties of a municipal advisor. There is a tremendous opportunity for the MSRB to add clarity for municipal advisors and help them work within the framework put forth by the SEC Municipal Advisor Rule. We hope these comments will help the MSRB avoid negative consequences for the municipal marketplace and potentially unnecessary burdens that substantially change the conduct of business without realizing intended policy benefits.

Principal Transactions

We are concerned with the provisions of Draft Rule G-42 that prohibit principal transactions for a municipal advisor for two reasons. First, the use of the phrase "[e]xcept for an activity that is expressly permitted under Rule G-23…" is unclear and creates confusion as to exactly what activities are permitted under Draft Rule G-42. The MSRB should more clearly indicate which activities are intended to be permitted under Draft Rule G-42 following the framework set forth by the SEC's Office of Municipal Securities in its FAQs.[3] Second, Draft Rule G-42, as written, places a complete

[2] *See* Registration of Municipal Advisors, Exchange Act Release No. 34-70462, *available at* https://www.sec.gov/rules/final/2013/34-70462.pdf.

[3] *See* Registration of Municipal Advisors, Frequently Asked Questions ("FAQs") at

prohibition on all principal transactions by a municipal advisor, thereby casting a large net around many activities and transactions that are unrelated to the actual advice being given by the municipal advisor. For example, the provision could be interpreted to prohibit commercial banks from being able to hold the deposits of an entity just because another business segment of the bank is working on a transaction involving the issuance of securities with that entity. While certain principal transactions may indeed result in a conflict of interest, a ban on all principal transactions for a municipal advisor whether or not the principal transaction relates to the municipal advisor relationship does not harmonize with SEC interpretative guidance in its recently issued FAQs. The SEC's guidance limits the prohibition to conducting business as the result of a conflict to the particular transaction on which the conflict arose. The Office of Municipal Securities in its FAQs relating to the Municipal Advisor Rule clearly limits the scope of such prohibition to the transaction at hand. The ban on engaging in principal transactions under Draft Rule G-42 should be limited to the specific transaction or transactions for which the municipal advisor was engaged to provide advice and should not apply broadly to all activities of the municipal entity.

Fiduciary Standards

The SEC did not undertake to define the fiduciary duty or other standards of conduct of a municipal advisor in its Municipal Advisor Rule and so Draft Rule G-42 seeks to define the fiduciary duty and the applicable standards of conduct by subjecting municipal advisors to a duty of care and a duty of loyalty in the conduct of their municipal advisory activities. Draft Rule G-42 also requires municipal advisors to disclose conflicts of interest and certain other information to their clients and to document their municipal advisory relationship. The fiduciary standards set forth in Draft Rule G-42, however, do not operate like other well-established fiduciary standards, such as those for attorneys, which means a large portion of the municipal securities industry will now have to design unique compliance regimes. The MSRB does not provide justification as to why this fiduciary standard deviates from accepted and established fiduciary duty standards or provide a detailed discussion of the benefits being obtained by veering away from

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http://www.sec.gov/info/municipal/mun-advisors-faqs.pdf.

commonly used standards when there is significant precedent in this area that could be drawn from – in particular the ABA Model Rules of Professional Conduct ("Model Rules").[4] Moreover, there is no discussion in the cost-benefit analysis section of the proposed rule regarding such a significant deviation from the typical legal framework for fiduciary standards.

The BDA proposes that the fiduciary duty standard should not be different for municipal advisors than it is for other professionals with fiduciary duties and that, in particular, the provisions concerning conflicts of interest should be structured like the requirements for conflicts of interest for attorneys. For example, the Model Rules applicable to attorneys provide for a definition of conflicts that generally (1) involves the representation of one client while being adverse to another client, or (2) involves a significant risk that the representation of one or more clients will be materially limited by the attorney's responsibilities to another client, a former client, a third person or a personal interest of the lawyer. In the event a conflict of interest arises, if the lawyer reasonably believes that he or she will be able to competently and diligently represent each affected client, the attorney may proceed by disclosing the conflict of interest and each affected client must give its informed consent, confirmed in writing. There are then specific types of conflicts, such as an engagement involving the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding, that cannot be waived by a client under any circumstances. This is a more workable regulatory structure than a blanket prohibition for all principal transactions in which a conflict of interest may arise for a municipal advisor.

The BDA supports the requirement that a municipal advisor disclose any material conflicts of interests and believes appropriate disclosures and waivers should be the basis for the MSRB fiduciary standard. Paragraph (b) of the Draft Rule G-42 sets forth the requirements for municipal advisors to disclose conflicts of interests. In addition, the BDA would like to see the MSRB incorporate into Draft Rule G-42 a further standard

[4] *See* American Bar Association Model Rules of Professional Conduct *available at* http://www.americanbar.org/groups/professional_responsibility/publications/model_rules_of_professional_conduct/model_rules_of_professional_conduct_table_of_contents.html.

establishing conflicts that cannot be waived. The Model Rules describe this type of conflict as a conflict that will cause the attorney to be unable to provide competent and diligent representation to each affected client.[5] Draft Rule G-42 could include a provision that a municipal advisor should disclose any actual or potential conflicts of interest of which it is aware after reasonable inquiry that might impair its ability either to render unbiased and competent advice to or on behalf of the client or to fulfill its fiduciary duty to the municipal entity client. If a municipal advisor concludes that a conflict of interest calls into question its ability to render unbiased and competent advice, as a fiduciary to a municipal entity, the municipal advisor may be in the position of being unable to serve as a municipal advisor on that transaction.

The BDA believes that Draft Rule G-42 should contain a provision dealing with when and how municipal advisors withdraw from or terminate a municipal advisor relationship with a municipal entity. As with other fiduciary standards, MSRB Draft Rule G-42 needs to provide for the effective withdrawal and termination of municipal advisory relationships. Under the Model Rule of Professional Conduct (the "Model Rules"), a representation in a matter generally is completed when the agreed-upon assistance has been concluded.[6] Similarly, an advisor's fiduciary duty should end at the completion of the transaction for which advice was given or in accordance with the terms of the written agreement. Also, municipal advisors need to be sure that their affirmative withdrawal as a municipal advisor in advance of the completion of a transaction complies with the MSRB's fiduciary duty standards and these standards should be included in any final rule.

Furthermore, it is critical that the MSRB clarify when a municipal advisory relationship is no longer in existence or deemed to be no longer in existence and the municipal advisor is no longer held to a fiduciary duty standard. Draft Rule G-42 should apply on a transaction by transaction basis and clarify the beginning and end of a municipal advisor relationship to avoid confusion and the unintended consequence of broker-dealers being constrained from pursuing legitimate business opportunities in a market in which issuers

[5] *See* Model Rules 1.7.
[6] *See* Model Rules 1.2(c) and 6.5.

can choose from a variety of professionals for advice and underwriting services.

Obligated Persons

The BDA agrees that it is appropriate to limit the extension of the fiduciary duty of a municipal advisor only to its municipal entity clients and not extend it to obligated persons. The Dodd-Frank Act clearly provides that a statutory fiduciary duty is owed by a municipal advisors to its municipal entity clients only and not to its obligated person clients. Congress was clearly intending to protect municipal entities in this regard and created separate legal duties for a municipal advisor when it advises its municipal entity clients and its obligated person clients. While the Dodd-Frank Act authorizes the MSRB to prescribe means that are reasonably designed to prevent acts, practices, and business conduct that are not consistent with a municipal advisor's fiduciary duty to its clients, the fiduciary duty does not extend to obligated persons because Congress only extended the fiduciary duty to an advisor's municipal entity clients. Further, the BDA believes that the MSRB amendment to Rule G-17, which requires that municipal advisors must deal fairly with all persons and not engage in deceptive, dishonest, or unfair practices, provides sufficient protection for obligated persons. The concept of an "obligated person" includes a wide spectrum of different kinds of entities, from universities to hospitals to corporate borrowers to developers, with different financial capabilities, levels of sophistication and regulatory requirements. It would include, for example, Goldman Sachs Headquarters LLC and The Goldman Sachs Group, Inc., who are obligated persons in connection with bonds issued by the New York Liberty Development Corporation to finance Goldman's new headquarters in New York City. Applying a fiduciary duty to each and every one of those relationships could lead to unintended consequences for the obligated persons and afford protections to entities that do not need, do not want, and were not intended, to be protected by Congress under the Dodd-Frank Act.

We are also concerned about the inconsistencies in the application of Draft Rule G-42 with respect to obligated persons. Draft Rule G-42(f) provides that "a municipal advisor, and any affiliate of a municipal advisor, is prohibited from engaging in any transaction, in a principal capacity, to which a municipal entity or *obligated person* client of the

municipal advisor is a counterparty" (*emphasis added*). In the absence of the municipal advisor having a fiduciary obligation to its obligated person clients, this prohibition on principal transactions is overreaching and provides unnecessary protections for obligated persons. Any restrictions on engaging in principal transactions should be limited only to municipal entities.

As discussed above, we believe Draft Rule G-42(a) expressly and correctly provides that a municipal advisor is subject to different legal duties when advising a municipal entity and when advising an obligated person. A municipal advisor, when advising a municipal entity, is subject to a fiduciary duty. A municipal advisor when advising an obligated person is subject to a duty of care and a duty of fair dealing. Despite the clear intention to establish distinct standards in Draft Rule G-42 for a municipal advisor when advising a municipal entity and when advising an obligated person, Draft Rule G-42 then imposes the exact same obligations and restrictions on the actions of a municipal advisor without regard to the type of client it is advising rendering any distinction in the standards meaningless. By imposing the same obligations and restrictions equally to both relationships, the result is that Draft Rule G-42 would, in practice, effectively extend a fiduciary duty to a municipal advisor's advisory activities with an obligated person. We believe that this result is both inconsistent with the MSRB's intent and the clear distinctions drawn in the Dodd-Frank Act between a municipal advisor's duties owed to clients that are municipal entities on the one hand, and obligated persons, on the other. We would request the MSRB to review and revise Draft Rule G-42 as needed to ensure that the final rule is internally consistent and also consistent with respect to the very different duties and obligations imposed upon municipal advisors depending on whether they are advising municipal entities or obligated persons.

Review of the Official Statement

The BDA believes that the default requirement in Draft Rule G-42 that a municipal advisor engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities must, under its duty of care, undertake a "thorough review" of an official statement is

appropriate. Including a default requirement will help to ensure that an issuer and a municipal advisor discuss and specify in the documentation evidencing the engagement the precise scope of the municipal advisor's responsibility with respect to the official statement. However, we would like the MSRB to provide additional clarification regarding what constitutes a "thorough review" of an offering document and how a "thorough review" is distinguished from a due diligence review of an offering document in order to guide municipal advisors as to the breadth and scope of their required review of the official statement in light of this default requirement.

We believe that it is generally the prerogative of the client to determine the scope of municipal advisory activities to be performed by the advisor, including whether or not the municipal advisor will review or prepare the official statement. Very often, an issuer will have engaged bond counsel or disclosure counsel to prepare or review the official statement and it should be decided by the issuer and the municipal advisor if the municipal advisor's role will be limited. Draft Rule G-42 in its final form should make it very clear that a municipal advisor's review of the offering document should be qualified to the scope of services the issuer chooses, as there are typically other professional service providers who are also engaged by the issuer in preparation of the official statement such as public accountants and engineering firms. In those instances, however, where the municipal advisor is specifically engaged to prepare or assist the issuer in preparing the official statement, the municipal advisor should not be able to contractually limit its obligation to do a thorough review of the official statement. Draft Rule G-42 seems to allow such a scenario. If the municipal advisor is engaged to prepare the official statement, the advisor should be held under its duty of care to be sure that the issuer understands its obligations with respect to the information in the official statement and to make sure that that official statement contains the information necessary, and at a minimum accurate and complete, for the type of transaction or security being offered. Any definition or guidance regarding what constitutes a "thorough review" of an official statement would therefore need to give due weight to a number of facts and circumstances, including, without limitation, the municipal advisor's contractual responsibility and role in preparing the official statement, the municipal advisor's

experience in the municipal market segment in which the deal falls, the municipal advisor's role in the overall transaction, and the role of other parties such as bond counsel, disclosure counsel, other consultants to the issuer, underwriters and their counsel in the preparation of the official statement.

Documentation of the Municipal Advisory Relationship

Under Draft Rule G-42(c), municipal advisors must evidence each of their municipal advisory relationships by a writing entered into "prior to, upon or promptly after the inception of the municipal advisory relationship." Draft Rule G-42 regarding documentation works well in the situation where a municipal advisor is hired for a period of time to provide advice regarding a number of transactions. However, with respect to more limited engagements, Draft Rule G-42 should mirror the transaction-based framework established by the Municipal Advisor Rule. The disclosures required by Draft Rule G-42, by MSRB Rule G-17 and by the Municipal Advisor Rule would provide the issuer with critical information it needs before engaging a party to provide advice in its designated role in connection with a specific transaction. Under the SEC's Municipal Advisor Rule, a person generally can become a municipal advisor in one of three ways: (1) providing advice with respect to the issuance of municipal securities; (2) providing advice with respect to municipal financial products or (3) undertaking to solicit a municipal entity. We believe each one of these circumstances should be addressed separately and we will not at this time address the solicitation of a municipal entity since it is outside the scope of Draft Rule G-42.

Draft Rule G-42(c) is modeled in part on MSRB Rule G-23, which requires that a dealer that enters into a financial advisory relationship with an issuer must evidence that relationship in writing prior to, upon, or promptly after the relationship has been entered into. Rule G-23 (b) clearly provides that "a financial advisory relationship shall be deemed to exist when a broker, dealer, or municipal securities dealer renders or enters into an agreement to render financial advisory or consultant services to or on behalf of an issuer with respect to the issuance of municipal securities, including advice with respect to the structure, timing, terms and other similar matters concerning such issue." Rule G-

23(c) states, “Each financial advisory relationship shall be evidenced by a writing entered into prior to, upon or promptly after the inception of the financial advisor relationship”. The guidance on the Rule G-23 also provides that although Rule G-23(c) requires a financial advisory relationship to be evidenced in writing, a financial advisory relationship will be deemed to exist whenever a dealer renders the types of advice provided for in Rule G-23(b), regardless of the existence of a written agreement.

Under Rule G-23, in order to establish a financial advisory relationship one of two conditions must be present - the broker, dealer or municipal securities dealer must render financial advisory or consultant services to an issuer or enter into an agreement to render financial advisory or consultant services to an issuer. Similarly, Draft Rule G-42 provides that a “municipal advisory relationship” shall, for purposes of this rule, be deemed to exist when a municipal advisor engages in or enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person client.

Under Rule G-23, however, a financial advisory relationship shall not be deemed to exist when, in the course of acting as an underwriter and not as a financial advisor, a broker, dealer or municipal securities dealer renders advice to an issuer with respect to the structure, timing, terms and other similar matters concerning the issuance of municipal securities. A dealer that clearly identifies itself in writing as an underwriter and not as a financial advisor from the earliest stages of its relationship with the issuer with respect to that issue (e.g., in a response to a request for proposals or in promotional materials provided to an issuer) will be considered to be “acting as an underwriter” under Rule G-23(b) with respect to that issue. Thus, in order to establish a financial advisory relationship there must be a mutual desire and understanding between the dealer and the issuer to enter into a financial advisory relationship and not an underwriting relationship (even if such agreement is not in writing). This extremely important concept is also present in the Municipal Advisor Rule where an underwriter cannot take advantage of the protection of the underwriter exception without the issuer’s participation because the issuer has to grant the exception to the underwriter.

For the purposes of Draft Rule G-42, where an entity is engaging in conduct that would not trigger municipal advisor registration, such conduct should also be excluded from Rule G-42. As a result, we believe that only when such advice is given in a forum where a municipal entity has an expectation and a desire that the advice should carry a fiduciary responsibility does the entity become a municipal advisor and trigger the requirement to evidence the relationship in writing whether or not the municipal advisor will be paid for the advice. The disclosures required by Draft Rule G-42, by MSRB Rule G-17 and by the Municipal Advisor Rule would provide the issuer with the critical information it needs before engaging a party to provide advice in its designated role in connection with a specific transaction.

It is a different analysis in the case of municipal financial products. In order for a person to become a municipal advisor by providing advice with respect to municipal financial products, we believe that all of the requirements for being deemed a municipal advisor with respect to the issuance of municipal securities should apply with the following exception: a municipal advisor should only have to evidence the relationship in writing if they are to be paid for the advice. Unlike the situation where a person becomes a municipal advisor by providing advice with respect to the issuance of municipal securities, there is only one possible role for the dealer here: the role of municipal advisor in the relationship. No other role that might provide a conflict with the municipal entity or obligated person is possible. As a result, when a person becomes a municipal advisor with respect to municipal financial products, the only need for a written agreement is to lay out the scope of the terms of the relationship and the compensation. Since the written agreement is a consideration for both parties when it involves payment to the municipal advisor, we believe that this is the only instance where a written agreement should be required.

Economic Analysis

The BDA does not believe that Draft Rule G-42 should contain any exemptions or special provisions for small municipal advisors. The Dodd-Frank Act recognized the need to regulate all municipal advisors and their advisory activities in order to address a variety

of problems that had been identified with the practices and course of conduct of some municipal advisors, including a failure to place the duty of loyalty to their clients ahead of their own interests and to exercise a duty of care. We are appreciative of your concern not to place smaller municipal advisory firms at a competitive disadvantage but these regulations need to apply to all municipal advisors without regard to size much like the rules for broker-dealers. We believe that Draft Rule G-42 is consistent with the Dodd-Frank Act's provisions with respect to burdens imposed on small municipal advisors and that above all it is in the public interest and necessary for the protection of investors, municipal entities, and obligated persons that Draft Rule G-42 be applied to all municipal advisors regardless of their size.

Disclosure of Liability Insurance Coverage

Draft Rule G-42 would require a municipal advisor disclose to its client either the amount and scope of coverage of professional liability insurance that it carries and any material limitations on such coverage or that it does not carry any such coverage. The purpose of this disclosure would be to permit a municipal entity to assess the resources available to protect it in the event of a breach of the municipal advisor's fiduciary duty. We agree that issuers should be aware of financial resources of the firm they are engaging as a municipal advisor and that protection of issuers is important. However, a number of firms providing municipal advisory services have a significant amount of net capital that would be available and this resource would likely exceed the amount of any commercially available liability insurance and offer better protection for their municipal entity clients. We would suggest that rather than require all municipal advisors to disclose very detailed information about their professional liability insurance, municipal advisors should be required to disclose the mechanism (capital, insurance, or a combination of both) and amount of financial resources which would be available to a municipal entity client if needed. If a municipal advisor does not have a certain threshold amount of capital (such amount to be determined by the MSRB) or professional liability insurance, then the BDA believes Draft Rule G-42 should provide that a municipal entity be able to request or require the advisor to obtain professional liability insurance in a certain minimum amount determined by the MSRB for protection of their municipal

entity clients only in the event of a breach of the municipal advisor's fiduciary duty.

Recommendations

Draft Rule G-42 provides that a municipal advisor should not recommend a transaction unless it has a reasonable basis for believing that the transaction is suitable for the client, and also lays out specific items that the municipal advisor must discuss with its client, including the evaluation of material risks and potential benefits, the basis for suitability and whether alternatives have been considered before the municipal entity enters into a municipal securities transaction or municipal financial product. The Supplementary Material accompanying Draft Rule G-42 recognizes that there are times when a municipal entity or an obligated person may elect a course of action that is "independent" of or contrary to advice provided by the municipal advisor yet does not provide any guidance as to the meaning of the word "independent." If a municipal entity or an obligated person that has engaged a municipal advisor is acting "independently," does it mean they are no longer relying on or considering the advice of the municipal advisor (which could raise issues for the independent registered municipal advisor exclusion of the Municipal Advisor Rule) or that they are not seeking the advice of the municipal advisor they have engaged or that they are acting contrary to the advice being given by the advisor? The use of the term "independent" in this context should be clearly defined in the Draft Rule G-42 or Supplemental Material to avoid confusion and unintended consequences.

Another concern is how exactly a municipal advisor is supposed to make a suitability determination as a municipal advisor. Under Draft Rule G-42, a municipal advisor's determination of whether a municipal securities transaction or municipal financial product is suitable for the client must be based on numerous factors including the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products, financial capacity to withstand changes in market conditions and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry. What these factors

do not include is the fact that many issuers are faced with policy and political considerations that may be very complex and may also guide or influence an issuer's decision-making process. The MSRB should clarify that if a client has clearly stated its goals and objectives to its advisor, the municipal advisor in making its recommendation does not need to step into the shoes of the client and examine, analyze or assess the appropriateness of the client's stated objectives or goals but may generally accept the goals and objectives.

We are also concerned that in order to maintain proper books and records of any evaluations and recommendations made by a municipal advisor that a number of discussions that typically occur verbally between an issuer and its advisor would need to be memorialized in writing, which may be of great concern to issuers and impractical for the municipal advisor. A decision made by an issuer may make sense to the issuer at the time the decision is made for any number of reasons and may be a good decision at the time it is made, but could be subject to questioning long after the transaction is completed. If these discussions and alternatives are memorialized, this may affect the decision-making process and how much information an issuer may be willing to disclose to its advisor. In addition, the MSRB should describe in more detail exactly what records a municipal advisor will need to retain. A municipal advisor needs to know whether it should retain records or copies of all the proposals it receives, just those proposals it receives and reviews at the specific request of the issuer or only those proposals it receives, reviews and recommends to an issuer.

Prohibited Activities

Draft Rule G-42(g) sets forth a number of prohibited activities for municipal advisors. In addition to these requirements, we feel that the rule should also expressly prevent a municipal advisor from using its advisory position to engage in non-competitive practices. There have been occasions where financial advisory firms have recommended a dealer to serve as an underwriter solely because that dealer did not compete with them for advisory business. Even though this activity would be both a violation of the duty of loyalty element of the advisor's fiduciary duty and a violation of Rule G-17's fair dealing

requirement, this type of activity is so egregious that it should be expressly prohibited and included in the enumerated list of prohibited activities for municipal advisors in Draft Rule G-42(g).

In addition, we would also like to add to the prohibited activities the use of the word "independent" by municipal advisors who are not affiliated with a broker-dealer. The word "independent" has historically been used by advisors to convey to issuers that because they are not affiliated with broker-dealer that they are free from potential conflicts and implying that they would provide better advice. Under Draft Rule G-42, disclosure of actual and potential conflicts of interest is required when a municipal advisor is engaged by a client so an issuer will now know whether a firm they are considering to engage as a municipal advisor has any conflicts of interest. We believe the use of the word "independent" in this context by a municipal advisor can be misleading to municipal entities and obligated persons and its use should be prohibited in this context.

Thank you for the opportunity to present our views on Draft Rule G-42.

Sincerely,

Michael Nicholas
Chief Executive Officer

Cape Cod 5
Member F.D.I.C.
THE CAPE COD FIVE CENTS SAVINGS BANK

P.O. Box 10 • Orleans, Massachusetts 02653-0010 • (508) 240-0555

Cape Cod's Community Bank Since 1855

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314

RE: MSRB Notice 2014-1 – Draft MSRB Rule G-42 Duties of Non-Solicitor Municipal Advisors

The Cape Cod Five Cents Savings Bank appreciates the opportunity to comment on the proposed MSRB Rule G-42. The Bank is very concerned that the rule, as drafted, may prohibit the bank from providing both municipal advisory services and traditional banking services such as deposit accounts, loans or cash management services to municipal entities in Massachusetts.

Community banks like The Cape Cod Five Cents Savings Bank are an invaluable resource and partner for communities throughout Massachusetts. Many small communities are ignored by large municipal financial advisory firms simply because they do not come to market frequently enough or issue in dollar amounts that are significant. The fees charged by some larger firms can also be prohibitive for smaller communities and, therefore, become a deterrent to hiring a municipal advisor, who may be able to save these communities significant amounts of money in interest expense as well as help them avoid costly mistakes that occur in the authorization process of issuing debt.

A prohibition on principal transactions, as proposed in the Draft Rule – G42, may have the unintended effect of restricting the ability of municipal entities and obligated persons to obtain financial products and services. Such a prohibition would only serve to further decrease access of small to mid-sized municipal entities to crucial, expert advice. A likely effect of the proposed rule would be to further tax the resources of the Massachusetts Division of Local Services, who may have to fill the void left if Banks were to exit the municipal advisory business.

The American Bankers Association has made a comment, dated March 4, 2014, and in it they make three specific points for discussion:

Cape Cod 5
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Cape Cod's Community Bank Since 1855

1. The MSRB has no authority to impose a fiduciary duty on the municipal advisors with respect to obligated persons.

2. Draft Rule G-42 should not apply to the provision of products or services that are either excluded or exempted under the SEC's final rule on municipal advisor registration.

3. The prohibition on principal transactions must be narrowed substantially.

We have reviewed these points and urge the MSRB to consider them and make the necessary changes to the proposed Rule G-42 to address them.

In conclusion, The Cape Cod Five Cents Savings Bank feels strongly that the proposed draft Rule G-42 may have many unintended consequences that will only serve to make qualified, municipal advisory advice more expensive and harder to obtain for small to mid-sized communities. We also feel the MSRB should carefully review and amend the prohibition on principal transactions, so that the rule does not force banking organizations to choose between providing municipal advisory services or a full range of traditional banking services such as loans, cash management and deposit products.

Sincerely,

Dorothy A. Savarese
President & Chief Executive Officer

From:	billcaraway@sbcglobal.net
To:	Comment Letters
Subject:	MSRB Notice 2014-01
Date:	Tuesday, January 14, 2014 12:48:11 PM
Attachments:	Chancellor Financial Associates-2014-01-20140114124806.pdf MSRB Ltr 2 Aug 11 2011.doc

First name: William
Last name: Caraway
Phone number: 512-257-0202
Company name: Chancellor Financial Associates
Notice number: 2014-01
Comment:
In 2011 I submitted the attached letter relative to small advisors. To date it would seem the agency is continuing to ignore the subject matter in the letter. Indeed Congressman Gene Green's office secured the support of Barney Frank as to the issues raised in the letter of 2011.
Please respond so I may determine what further action will be needed to protect my company's interest.
1 file(s) uploaded successfully.
MSRB Ltr 2 Aug 11 2011.doc

Chancellor Financial Associates
10005 Spicewood Mesa
Austin, Texas 78759
512-257-0202
chancellorfinancial@gmail.com
billcaraway@sbcglobal.com
August 12. 2011

Ms. Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F. Street, NE
Washington, DC 20549-1090

Re: S7-45-10 Small Advisor Exemption

Dear Ms. Murphy:

Chancellor Financial Associates is a consulting firm to Independent School Districts in Texas. Chancellor has been involved with Texas School Districts since 1993. I am a former member of the Texas House of Representatives and a former member of the Texas Higher Education Coordinating Board. I have held seminars in Texas for School Administrators, Business Managers and Board members at various professional gatherings on the topic of Alternative Financing in Texas.

Having served in the Legislature, I authored legislation dealing with lease purchase financing under the Texas Public Property Finance Act as well as legislation dealing with maintenance tax notes, time warrants and a variety of financing tools available to Texas school districts. I am the only employee in the company and serve small school districts with a student population below 3,000 in rural areas of Texas. I am called on by districts to explain state financing alternatives as well as general financial procedures for implementation.

Starting in September of last year I was advised by counsel to register with the MSRB and SEC as a Municipal Advisor. I have received my registration number and have with horror read daily emails from the MSRB as to many different statutes, rules and regulations pertaining ostensibly to my business. Most of the emails site various rules and regulations alien to me and seem to be focused on large securities dealers. Now I am advised of pending rules requiring exams as well as issues regarding the distinction between advisors vs. brokers, all of which seem to be designed to quash small advisors in the marketplace.

Small Municipal Advisor Exemption:

The Dodd-Frank bill (the "Act") states that the law shall not create an undue burden on small financial advisors. On page 91 of the Release No. 34-63576, File No. S7-45-10 (the "Release") the Securities and Exchange Commission ("SEC"). The Small Business Administration ("SBA") defines small business for the purposes of entities that provide financial investment and related activities as a business that had annual receipts of less than $7 million during the preceding fiscal

year and is not affiliated with any person that is not a small business or small organization. The Commission is using the SBA's definition of small business to define municipal advisors that are small entities for the purposes of the Regulatory Flexibility Act (RFA). I request that Chancellor Financial Associates and William J. Caraway be exempted from the Act due to the burden it places on my company as a small Advisor.

Simply stated, I am the only employee of Chancellor Financial Associates, a sole proprietorship. During almost 20 years, I have never generated more than $1 million in total revenue for any given year. For the last two years my gross revenue has never been over $350,000. Further, Chancellor does not have the funds to retain a securities law firm to deal with all matters raised in the various daily emails from MSRB. Frankly, if the exemption is not granted then I will be required financially to close down Chancellor Financial after 20 years of serving rural Texas school districts. It would seem from the self-serving remarks by various associations and groups of advisors as to new regulations there is an intent to shut down any and all competition, no matter how small.

A simple solution would be to simply set a debt financing limit and exempt those firms involved in transactions at or below the limit from the Act. One suggestion is a limit predicated on the Internal Revenue Code's $10 million limit (during a calendar year) in order for an issuer's bonds to be bank-qualified.

Proposed Rule 15Bal-2:

The Rule is not within my non-legal grasp and will require legal counsel to advise what each requirement entails. Considering the makeup of the MSRB board, it would seem that the making of rules is directed toward forcing out small Advisors. I noticed First Southwest Company senior officer is now Chairman of the Board of your organization. I am familiar with this company, which together with Southwest Securities, controls about 90% of the municipal bond business in Texas. It appears that the MSRB and SEC will complete the process for these large companies to consolidate all municipal bond business not only in Texas but throughout the country under their umbrella if the rules are forced on small Advisors. Most small advisors I have spoken with indicate suspicions as to the actions by the MSRB and SEC as to providing large firms total control over transactions anticipated in the Dodd-Frank Act. Therefore it would seem Congress has enacted a law which will create by regulations monopolies in the municipal advisory business.

Summary:

Thank you for your consideration,

William J. Caraway, President
Chancellor Financial Associates
chancellorfinancial@gmail.com
512.257.0202

March 10, 2014

Thank you for the opportunity to comment on proposed Rule G-42, regulating the activities of Municipal Advisors. I applaud the Board's efforts to begin to require accountability of heretofore unregulated Municipal Advisors. The Board posed many questions that are worthy of debate. I intend to focus on only a few of the issues raised in the proposal. There is, however, one glaring omission that must be remedied and it will be addressed first.

How in the world could the Board propose to regulate the activities of Municipal Advisors and remain silent as to political contributions? G-42 was originally a pay-for-play rule. The Board elects to expand the Rule to provide for the general regulation of municipal advisory activities and leaves pay-for-play out? Who argued this was a good idea? Pay-for-play is the first municipal advisory activity the Board quotes as a cause for Congressional concern, yet nearly four years after Dodd-Frank becomes law, pay-for-play is not mentioned in the currently proposed regulations. This is an oversight that must be immediately remedied. Currently, registered broker-dealers are prohibited from making political contributions to municipal issuer officials, while heretofore unregulated municipal advisor firms, even under the proposed regulations are free to make any legal political contribution and disclose it as a "potential conflict of interest." If the Board does nothing else in the short term, the same pay-for-play rules that apply to MSRB member broker-dealer firms must also apply to all Municipal Advisor firms.

The Board has determined that engaging in principal transactions with a municipal issuer client is completely incompatible with the fiduciary obligation that an advisor has to its issuer clients and has proposed to prohibit any such activity. This is the case regardless of whether or not the advisor is involved in this area in an advisory capacity, there are bond proceeds involved, the activity occurs in another division of the firm, or the competitive nature of the investment activity involved is such that the advisor has no competitive advantage. However, an advisor is free to accept payment from a third party to recommend that the issuer engage in principal transactions with that party and must merely note the acceptance of that payment as a "potential conflict of interest." To the casual observer, the latter situation presents a larger problem for the issuer than the former. Is a municipal issuer at a larger disadvantage where the sales division of the broker-dealer is offering to sell securities in a competitive environment or where the Municipal Advisor has been paid to advise the issuer whose services to employ? An advisor is employed to provide advice related to a municipal debt issuance. In the very least, if the funds involved in a securities transaction are not demonstrably bond proceeds, the existence of an advisory relationship with the issuer should not disqualify that broker-dealer from competing for the issuer's business.

As to the review of offering documents, a Municipal Advisor receives significant compensation for services rendered absent the undertaking of risk. Consequently, review of the offering document should be one of the activities for which a Municipal Advisor is held responsible. A Municipal Advisor should not be able to negotiate their way out of this responsibility. The Board, however, has unnecessarily complicated the matter by including the word "thorough" in its regulatory dictate. A review of the

offering documents is either conducted or it is not, and if that review is **c**alled into question the answer will most likely be determined, unfortunately, in court. The current language imposes an unfair burden upon a trier of fact inexperienced in the municipal securities arena, to say nothing of a young FINRA examiner, by placing on them the responsibility for the determination of what constitutes a "thorough" review of an offering document. If a Municipal Advisor has documented a review of the offering document, the confirmation of said review should be sufficient for regulatory purposes.

The Notice requests comment as to whether or not a Municipal Advisor should be required to disclose the disciplinary history of persons employed at the Municipal Advisor. In the event the Board elects to require disclosure of disciplinary histories of parties employed by municipal advisors, only information pertaining to persons directly involved with providing services to the municipal issuer should be the subject of the requirement. Many firms that provide municipal advice have thousands, if not tens of thousands, of employees and the disciplinary history of each employee of a large firm is not relevant to the nature of the advisory services being provided to a municipal issuer.

Professional liability insurance is extremely expensive. The annual premiums for a policy of any size can be in excess of $100,000. While I am aware that many firms, my employer included, obtain coverage of this nature and certain clients require such coverage, it is difficult to argue that to such a requirement would not be an impediment to entry into the Municipal Advisory arena.

I am certain that creating a regulatory regime for an arena where none existed before is an arduous undertaking. One could not expect staff or the Board to address all the potential issues or problems created by such an undertaking in a single effort. Thank you for the opportunity to comment on the issues that that I most strongly believe need to be addressed.

Chris Melton
Executive Vice President
Coastal Securities

March 10, 2014

By Electronic Delivery

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: College Savings Foundation's Comments on MSRB Notice 2014-01: *Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisor*

Dear Mr. Smith:

The College Savings Foundation ("CSF") is a not-for-profit organization with the mission of helping American families achieve their education savings goals by working with public policy makers, media representatives, and financial services industry executives in support of 529 college savings plans ("529 Plans"). CSF serves as a central repository of information about college savings programs and trends and as an expert resource for its members as well as representatives of state and federal government, institutions of higher education and other related organizations and associations. CSF's members include state 529 Plans, investment managers, broker-dealers, other governmental organizations, law firms, accounting and consulting firms, and non-profit agencies that participate in the sponsorship or administration of 529 Plans.

CSF endorses the comments made by the Investment Company Institute in its March 4, 2014 response letter to Regulatory Notice 2014-01. We appreciate the opportunity both to comment on the Notice and to continue the dialogue with the MSRB on 529 college savings plans in general. Please do not hesitate to contact us with any questions or for more information. You may reach us by contacting CSF's Executive Director, Kathy Hamor at (703) 351-5091.

Sincerely,

Mary G. Morris
Chair,
College Savings Foundation

By Electronic Delivery

March 10, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Comments Concerning MSRB Notice 2014-01
Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

The College Savings Plans Network (CSPN), on behalf of its members, is pleased to have this opportunity to comment on MSRB Notice 2014-01, *Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors* issued January 9, 2014 (the "Notice" or "Notice 2014-01"). We appreciate the Municipal Securities Rulemaking Board's (the "MSRB") continuing commitment to assist consumers seeking to invest in 529 College Savings Plans ("529 Plans") and its interest in ensuring that State administrators of 529 Plans receive sound, balanced support from its advisors. We remain dedicated to working with the MSRB in its efforts to implement the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").

CSPN appreciates the MSRB's efforts to outline duties and obligations of municipal advisors as defined by Section 15B(e)(4)(A) of the Securities Exchange Act of 1934 (the "Exchange Act"). However, we believe that municipal advisors to 529 Plans provide different services and are organized differently than municipal advisors in other contexts. Therefore, we offer the following observations and concerns for the MSRB's consideration.

Endorsement of Investment Company Institute Comment Letter

CSPN is supportive of the comments relating to proposed Rule G-42 submitted by the Investment Company Institute (the "ICI") and endorses its comment letter dated March 4, 2014 on Notice 2014-01 (the "ICI Letter").

Additional Comments

In addition to the points raised in the ICI Letter, CSPN wishes to present the following information:

Subsection (a) and Supplementary Material .02

The requirement in Supplementary Material .02 that a municipal advisor "investigate and consider other reasonably feasible alternatives to any recommended municipal securities transaction or municipal financial product that might also or alternatively serve the municipal entity client's objectives" does not squarely apply to the 529 Plan marketplace. Because of the limitations imposed by Section 529 of the Internal Revenue Code, a municipal advisor to a 529 Plan administrator, for example, could only recommend other 529 Plan products. In this context, the advisor would be limited to recommendations of structural or investment option alternatives for the relevant 529 Plan. Accordingly, an elimination or clarification of this requirement in Supplementary Material .02 for 529 Plan municipal advisors is appropriate.

General Matters – Questions 9 and 10

Municipal advisors to 529 Plans range in size from multi-billion dollar financial services firms to small business advisors. Requiring a specified limit of professional liability insurance is unprecedented in the industry and is, at best, problematic given the diverse nature of the 529 Plan municipal advisor market. Specified limits of coverage would create an undue cost burden for municipal advisors to 529 Plans and prohibit new municipal advisors from entering the market.

Application for Rule G-42

CSPN reiterates the comments made in the ICI Letter regarding prospective application of Rule G-42. It is important to also note that, in most cases, the municipal advisor's contract with a 529 Plan state administrator has been the subject of protracted and complex state mandated procurement requirements. Retroactive application of Rule G-42 would require an undue burden on state procurement processes across the country resulting in required detailed reviews of procurement laws and regulations by state 529 Plan administrators and state procurement offices. In addition, some state procurement processes may not allow for a retroactive amendment to a current municipal advisor's contract with the state. Accordingly, CSPN strongly believes that Rule G-42 must apply only prospectively.

* * * * * * * * * *

Thank you again for providing an opportunity to comment on the Notice. We believe these revisions and clarifications to the proposed rule will protect 529 Plan investors and their

state administrators while allowing for an appropriate regulatory structure for municipal advisors in the 529 Plan marketplace. Please do not hesitate to contact us with any questions or for more information. You may reach CSPN by calling Chris Hunter at (859) 244-8177.

Sincerely,

Betty Everitt Lochner
Director, Guaranteed Education Tuition Program
Chairman, College Savings Plans Network

COOPERMAN ASSOCIATES
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111 Anza Boulevard, Ste. 107
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(650) 619-0007; fax (650) 348-7684
email: jgcooperma@aol.com

March 10, 2014

VIA Electronic Mail

Municipal Standards Rulemaking Board
www.msrb.org

Ladies and Gentlemen:

This is in reference to your Regulatory Notice 2014-01 issued on January 9, 2014.

As a sole practiiciner municipal specific financial advisory firm since 1989, I am concerned with the impact the draft Rule will have on our practice and similarly situated firms, as well as the institutionalization it may promote in the field, to the detriment of municipal clients and conduit issuers, who will face less choice and options and higher costs for professional advice.

1. ECONOMIC ISSUES; REGULATORY SCOPE

The Notice correctly states that a consequence of the Rule may be a higher cost burden on smaller firms (at 25), and that the Act only permits regulatory burdens appropriate or consistent with the Act's purposes of preventing fraud and protecting statutorily protected parties. The genesis of the Act's provisions was inappropriate conduct by a small group of advisors, which the Act mitigates against by providing a strict fiduciary standard.

Perhaps it would be better to determine first, with the actual experience of time, whether the Act itself has resolved the issues Congress was concerned with before the MSRB resorts to the regulatory authority provided in the Act. Rather than burden the entire field of FA's with time-consuming and costly regulations, it may be appropriate to determine what, if any, abuses or inappropriate conduct remain requiring the regulatory surveillance of this Rule and others. Alternatively, the Board should consider initially limiting the Rule to an enumeration of prohibited forms of conduct and practices, rather than imposing extensive compliance, supervision, etc.

Assuming a specific need for action now can be demonstrated by the Board, the proposed Rule and its accompanying Notice do not provide appropriate data or a specific cost benefit analysis showing why the regulatory burdens, particularly on small firms, are justified, The Board concedes that it has little data, but justifies compliance with its own

policies and the Act's requirements through a listing of generalized non-specific benefits. It concedes that the cost burden may reduce competition, and increase costs to the FA firms and potentially their municipal clients, but does not propose any mitigation for this. Therefore, the Board may not have adequately satisfied its own policies in formulating certain provisions of the draft Rule.

There is no suggestion of a streamlined checklist from the Board to promote compliance/reduce costs or a sample timeline for firms to consider. No proposed forms to facilitate compliance are provided, and on a recent webinar, staff from the MSRB dismissed the suggestion of a baseline compliance manual to reduce administrative costs for smaller firms. No estimate of the time or expense for compliance is provided, as is applicable to other federal agencies such as the IRS through the OMB. Rather, the Board considers FA firms like the larger broker-dealers it administers, with their larger profit margins and embedded compliance staff. However, unlike broker-dealers, FA firms do not handle client funds or direct client investments—they only offer advice and guidance to their principals (the municipal clients), which is a more restricted template for regulation. This distinction should be considered further.

Accordingly, the Board needs to address in more concrete detail specific costs of the proposed Rule, especially on small shops, and whether the benefits accruing are specifically (and not in a generalized manner) material enough to impose the burdens, as recognized by the Congressional draftsmen in the statute.

2. COMPETITIVE IMPACTS

As more entrepreneurial in nature, smaller and one-person firms can be more flexible in their terms and arrangements with clients, and can offer services on a more cost effective basis, without compromising quality. In many cases, professionals from the larger FA firms or broker dealers populate these entities, offering the same level of expertise that they provided at the larger entities. As smaller firms are not controlled by larger financial institutions, with bonus pools and parent companies to consider, they can be more accommodating on services and rates. For example, as a member of my Town's citizen's finance committee, I offer free FA services to the Town, saving it over $150,000 in FA fees, as well as $140,000 from negotiating a reduction in swap trade profits with the Town's broker-dealer I also provide discounted rates to my local elementary school district.

Furthermore, when Trinity County in Northern California faced a potential TRAN default and Chapter 9 filing, at the County Treasurer's request I organized a team of 3 FA's to provide services to replace the County's debt with a longer term obligation, with reduced FA fees, closing a very difficult transaction the day before the potential default. The amount of services required did not justify the fee for the assignment, which larger broker-dealer firms had declined. Two of the FA's subsequently used their expertise to assist Vallejo and Stockton with their bankruptcy problems.

The Board is correct in its assumption that negative competitive consequences may flow from the Rule for smaller firms, and lead to consolidations or exit from the field, apart from those whose exit is welcomed. Should the Rule require an extensive formalized policy and procedure ritual, even for one-person operations, this burden may diminish the pool of firms and individuals available, and lessen competition. It could also lead to the institutionalization of the field, where larger firms, akin to oligarchies, dominate, and where alternatives and ideas available to issuers are limited to those accepted by larger institutions. For example, in 1996 I was asked to assist a Christian school to finance a new junior high-high school campus on a 40 acre site in San Jose. Despite the negative feedback from one large bond counsel, through a lengthy two year process we were able to arrange an initial $28 million tax-exempt private placement financing, avoiding closure of the school as its lease of public facilities had lapsed. It is now a 2000+ student facility. The initial negative reading (which differed from that of other large bond counsel) and extensive time commitment would have made this difficult to undertake in a larger, more bureaucratized setting.

3. INSURANCE MANDATES

The market for FA e&o insurtance is very sparse and spotty, particularly for small firms, which do not generate significant premium income to insurers. Deductibles and premiums have increased, and in the case of my carrier, policy terms have been cut from three years to two years, which could herald their exit (I have a zero controversy and claims history). The Act was not intended to address such administrative issues, as its emphasis was preventing fraud, and the Board's focus should remain there.

The Board can be helpful by fostering and approving insurance pools for smaller firms and estabilishing a national database on claims to provide insurers with industry-wide data that hopefully indicate this is a profitable line of business.

No mandate for insurance should be required of FA's and disclosure of insurance terms should be voluntary with the issuers, much as it is now with individualized requirements by issuers in each FA RFP, etc.

4. EXTENSION OF RULES TO DODD-FRANK ACT NON-LISTED PARTIES

This concept is again broadening the scope of the statute, without Congressional evidence of concern here, as well as having mischievous consequences respecting multiple fiduciary relationships. For example, in conduit transactions, the FA usually is engaged by the borrower, not issuer. In fact, the obligation is non-recourse to the issuer, whose involvement is principally for the upfront fee income and smaller annual payments. If the FA is obligated to both parties, not by their choice but by regulatory fiat, this may lead to conflicts that potentially may not be waivable, as well as extra expense. For FA's to operate most effectively, they need to be answerable to one client per transaction.

5. OFFICIAL STATEMENT REVIEW

Any action by the Board on this topic vis-à-vis FA's only adds additional requirements and cost where clear lines of responsibility already exist. Disclosure counsel is responsible for the Official Statement, both its drafting and content. To the extent it is based upon information provided by the issuer or borrower, this is frequently noted in a disclaimer by the Disclosure Counsel in the Official Statement. While most FA's review it, adding regulatory responsibility will create unnecessary potential conflicts among the financing team, including potential impasses regarding language or revisions, and add cost to the issue. It also potentially makes the FA a guarantor of the issuer and the disclosure counsel, which position is not appropriate to the FA's role (and for which it is not being compensated).

Many FA's now add a statement in their fee paragraph as to their involvement, which should suffice to guide investors, without further mandates from the Board. . A corollary consequence is that this imposition potentially diminishes insurance availability for FA's given the uncertainties it creates in responsibility, liability and risk.

6. FEASIBILITY STUDY/ANCILLARY DOCUMENT REVIEW

The FA's role is not to guarantee the financing, the Issuer, the borrower or the work of bond counsel or disclosure counsel, which may be a potential consequence of your proposal on feasibility study evaluation. The FA's role is more limited in nature, to review of financial structures, cashflows, financial assumptions, financial risk to the issuer or its enterprise and similar questions.

The FA is not acting as, nor is capable of serving as, supervisory engineer, architect, zoning administrator, attorney, real estate professional or appraiser, and it is inappropriate to require these responsibilities of FA's. Nor are they expert enough to be legally able to evaluate the bonafides of these professionals. As a matter of caution, FA's may review these documents, but mandating review creates a legal liability that merges the FA's role to that of supervisory professional over the other participants. This is beyond the scope and purpose of the statute, and the FA's expertise. It creates the very circumstances for FA's that the Board should want to avoid.

7. FEE SPLITTING

Smaller FA firms may outsource some of their back office tasks, such as computer run generation, to other entities, which may include FA's. This may be done on a per project or per hour basis, and payment to the entity would typically not be dependent upon successful conclusion of the financing or payment to the FA of its fee. As the payments are made by the FA firms for discrete services, akin to payments to a temporary employment agency or consultant, they should **not** be considered within the concept of fee splitting.

Similarly, where two FA firms contract with the issuer to perform services for a predetermined fee, that is disclosed to the issuer (similar to what was required by keep Trinity County from a Chapter 9 filing), this type of arrangement should be permissible under the Board's rules.

8. TIMING OF FA CONTRACT APPROVAL; IMPLIED CONFLICT WAIVER

Issuers prefer to approve all documents, including fee agreements, at one time, which may be close to the date the POS is released. Potentially the draft rule imposes a new timeline, requiring the FA fee agreement approval first, before any other steps are taken. This doubles the internal work for the issuer's staff.

To avoid unnecessary additional steps, the Board should clarify that so long as an issuer is provided the specifics of the fee arrangement in writing ab initio by the FA, which ratification can occur subsequently, this will satisfy the Rule.

Similarly, FA's may provide computer runs and other financing strategy materials to a prospective issuer, as part of the outreach efforts of the FA. This also may arise in the context of presentations to an issuer or multiple issuers on debt alternatives or specific potential debt issuances; The Board should clarify that this does not constitute the performance of FA services for purposes of timing of fee disclosures, until the issuer(s) consent(s) to proceed.

Regarding conflicts of interest arising from compensation arrangements, all fee arrangements or services contracts by definition involve adverse interests between parties. Other personnel in the municipal finance business, subject to similar SEC anti-fraud rules, do not have written conflicts disclosure. What is the justification or need for action here? Ditto for the issuer "consent" mandate under consideration by the Board.

"Common sense" says that logically the parties to a fee agreement, just like an underwriting purchase agreement, by definition have adverse interests, without further need for disclosure.

9. RECORD RETENTION/POLICY MANUALS

To avoid unnecessary costs and duplication for one-person and small FA shops, the Board should clarify that maintenance of drafts of documents and emails on the firm's email site or through their ISP (such as gmail, Microsoft, facebook, yahoo, aol, etc.) will comply with the records retention requirements. Absent this clarification, smaller firms may feel compelled to invest in duplicative services, incurring needless expense.

To reduce costs of compliance for smaller firms, the Board should also provide a draft of a prototype baseline policy and procedures guide that smaller FA firms can adopt or modify, as needed, or assist FA user groups with this type of endeavor.

This will reduce potential deficiencies in any later supervision or examination of FA firms through the Board's rules.

10. COST RECOVERY; MAINTAINING FA PROFESSIONALS

Depending upon the level of support from the Board or its staff, the costs of compliance could become very large and extensive. My firm does not "nickel and dime" its clients with charges for each item or request,, but rather seeks long-term relationships.

However, should the costs for compliance be significant, which I fear will occur under the draft's current version, I will need to surcharge for regulatory compliance, much like San Francisco restaurants now do for City-imposed health care insurance on restaurant personnel. This will be an economic disadvantage for smaller firms.

As fewer firms translate to less competition and potentially greater institutionalization, (possibly leading to an oligarchy), the Board should review the economic and competitive consequences of the draft Rule in more detail before proceeding.

Higher cost will also create a barrier to entry for newer FA's or those transitioning from other fields, particularly if the proposed exam is not properly designed and implemented. Ditto for any supervision rules. The touchstone of Dodd-Frank was fraudulent or improper behavior, and the Board should not wander from this specific purpose with myriad other proposals.

11. ADMINSTRATIVE- QUESTIONS POSED (AT 25-28)

#1 The Board should not list the required deliverables, as they are customized to each client.
#4 Obligated person expansion discussed in Para. 4 above.
#6 , 7 ;and 9 Discussed above. All should be as simple as possible and use existing technology or information disclosures already available.
#10 and 11. Discussed in separate paragraphs above, including Para. 3 and 9. .
#12 Extensive oversight activities will likely reduce the willingness of FA's to consider creative solutions—rather adopting "run of the mill" responses.
#13 and 15. See Para 10 above.
#14. I believe the very fact of a registration requirement, which can be revoked, has already promoted FA utility among issuers. Further strictures will at most provide minor incremental benefits.
#16 and 17. Negative.
#20 See Para. 1, 2 and 10 above.
#21. See Para. 10 above. Remember that we are competing for new blood against hedge funds and potentially more lucrative industries.
#24 and 25. Draft Rule G-42 will create advantages for larger firms, whose economic consequence has not been sufficiently addressed by staff, other than a mention in passing.

The Board should wait for some period of time to determine how the Act is ameliorating the problem with which Congress was concerned. There is always time later to create and implement new regulations. See above generally.

As a 25 year veteran of this industry, at the tail end of my career, the concerns above are only partially for me. Much of my cautionary suggestions are intended to alert the Board to long-term deleterious effects its rulemaking may have. The vitality and vibrancy of this "niche" depend upon an appropriate regulatory matrix not impacting adversely the desirability for both present and future participants.

While Congress gave the Board rulemaking authority, it should be used judiciously, timely, efficiently and effectively, and should work to sustain and leverage on the benefits obtained from this industry, whose vast majority of participants provide appropriate financial and economic advice to issuers.

Respectfully Submitted,

Joshua G. Cooperman

Comment on Notice 2014-01

from Erika Miller,

on Wednesday, February 4, 2015

Comment:

I strongly feel that if you work for a broker/dealer, the registration requirements whether you are an Underwriter or a Municipal Advisor should be the same. If you are an independent MA, then the requirements can be different that what is required if you work for a broker/dealer.

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March 17, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Comment on Draft MSRB Rule G-42 on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

Thank you for the opportunity to respond to your request for comments on Draft MSRB Rule G-42, Regulatory Notice 2014-01 as regards to Duties of Non-Solicitor Municipal Advisors. We are submitting our comments specifically with regard to the category of *"Economic Analysis"*.

FCS GROUP is a small (<25 employee) firm that provides advice to municipal entities and publicly owned utilities in the form of utility rate studies, revenue sufficiency studies, financial chapters for master plans, cost of service analysis, user fees, indirect allocation, utility valuations, asset management, and other financial planning and analysis matters. We do NOT provide **direct** advice to clients on the choice of or with regards to the structure timing, terms and other similar matters concerning debt instruments, financial products or issues.

The data that we provide is simply a projection or forecast of the estimated cost to provide water, storm, sewer, electric, solid waste or transportation services to a municipality's constituents and include estimates and recommendations of how those costs might be recouped from or spread out between various classes of customers: single family homes, multifamily homes, apartments, commercial and industrial businesses. As part of our studies we make **assumptions** as to whether the municipality might need additional outside funding to finance their costs such as a loan, developer fees, bonds, etc.

There is always an **independent registered municipal advisor** or financial advisor as an intermediary between us and the decision to issue a debt instrument. Our role is limited to evaluating whether the client has sufficient cash flow needs to meet WHATEVER debt service coverage requirements are needed. We have no control over, nor do we team with other firms, on how our deliverables will be used. We DO NOT select financial instruments, recommend financial instruments, participate in financial transactions, or deal in specific transactions. The work product that we do provide that is closest to our understanding of the definition of a municipal advisor activity as defined in Rule G-42 is parity certification.

That being said, we are concerned about the economic impact of the Draft MSRB Rule G-42 on the Duties of Non-Solicitor Municipal Advisors. Specifically three items will directly or indirectly impact us: 1) competition from engineering firms; 2) annual fees; and 3) certification.

1. Certain engineering firms offer the same services that we do and compete for the same clients. In fact a number of our employees worked for engineering firms before joining our firm. We understand that engineering firms are exempt from compliance with MSRB Rule G-42 by definition. We argue that either we should also be exempt to level the playing field, or that the exemption should not apply to **a type of firm**, but rather to the **type of work** being performed. Therefore, if revenue sufficiency studies or the financial chapter of a master water plan are to be governed by MSRB Rule G-42, than either 1) engineering firms should not be allowed to perform them without registering as municipal advisors; OR 2) revenue sufficiency studies, parity certifications, financial planning, etc. should not be regulated under MSRB Rule G-42. Without leveling the playing field, small firms like ours will be unable to compete against the HDRs, CH2M Hills, and Black and Veatches of this world and essentially we will be forced out of business. The MSRB Rule G-42 states that engineering firms are exempt if they are providing engineering advice. Does that exemption extend to an engineering firm that provides both engineering advice and financial advice?

2. The MSRB plans to seek approval from the SEC to charge municipal advisor firms an annual fee of $300 per professional. Our projects typically require an analyst, a project manager and a principal. This is designed intentionally so that we can DECREASE the cost to the municipality by using lower paid entry level employees on more routine tasks, but ensuring the client has access to the knowledge and expertise of our 20- to 30-year veteran consultants. How is the MSRB defining "professionals"? Does it include anyone working on the project or is it anyone working for the firm? If there is a principal assigned who is responsible for ensuring quality control and assurance as well as compliance with the MSRB and SEC rules and regulations, could the fee then only apply to that individual or that category of individuals? This fee will have to be added to the cost of our services. Being a small firm our profit margins are already extremely tight and this seems to be an unnecessary financial burden not only to us, but to our clients who costs must be increased to cover the fees paid by us as well as the fees paid by financial advisors or independent registered municipal advisor who may also be assigned to the same project. A revenue-based fee applicable to the firm as a whole might be easier to administer and more fair. Finally, if engineering firms are not required to pay these fees, it puts our firm at a distinct competitive disadvantage when it comes to competitive bidding.

3. The rule proposes the development of a test to certify municipal advisors. We contend that the definition of municipal advisor is so broad as to put those firms whose services are only tangentially connected to the diverse list of municipal advisor services outlined in MSRB Rule G-42 at a distinct disadvantage. Certification creates an additional cost burden on these firms in the form of increased salary expenses to recruit and hire employees who are certified in areas of municipal advice that do not even apply to and/or are not necessary to know in order to do the work that we perform. It is like asking every doctor to be certified to perform brain surgery. If there is to be a test, it must in some way be adapted to the various categories within the definition of municipal advisor. For example the Life Underwriter Training Council (LUTCF) certification has three parts. Two parts are mandatory for everyone, but the applicants have a choice in which test they take for the

third part. A similar approach would allow the test to be more adaptable to the various disciplines within the definition of municipal advisor.

Even with that change, the addition of certification requirement would be burdensome for firms and cumbersome to administer. Unfortunately certification is never a one-time event. You have to study for the test as well as take additional classes for continuing education units on an on-going basis. This burns up available resource time forcing firms to hire more individuals to be able to perform the same amount of work that they did before the certification was required and in turn increases the cost of doing business. The MSRB might consider replacing this requirement by recognizing college approved degrees in finance or related fields in place of certification at least for those municipal advisors who are not dealing with debt issuance and transactions.

Finally, we believe that it is overkill for every employee in a firm to be required to pass the test. Similar to the structure of an accounting firms where not everyone must be a CPA or an engineering firm where not everyone is a licensed PE, a firm in the municipal advisor field should not need to have all employees certified if that is the ultimate direction the MSRB chooses. For example a CPA firm is simply a firm that is owned, at least in part by a Certified Public Accountant, licensed in the state in which they operate.

The CPA firm usually consists of people at various levels in their accounting career. Some come to work as a Staff Accountant, working through their experience requirements, and others come to work as seasoned accountants experienced in all aspects of accounting. The one common factor is prior to working with clients at a CPA firm most have at least attained a bachelor's degree in accounting and are well on their way to becoming accounting experts. Accounting is a skill acquired over many years of experience, it is not something learned overnight or by taking an test. It is our belief that the same is true of municipal advisors and not every professional in the firm should be required to pass the certification test. Nor is certification any assurance that the municipal advisor knows the “right stuff”.

Again, we thank you for this opportunity to provide our input on this matter. I can be reached at 425-867-1802, ext. 226 or tareeb@fcsgroup.com for further comment.

Sincerely,

Taree Bollinger
Vice President

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SHELLEY J. ARONSON
PRESIDENT
Certified Independent Public Finance Advisor
NAIPFA DIRECTOR AT LARGE, 2012 – 2014

January 16, 2014

Mr. Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Dear Mr. Smith

I appreciate the opportunity, on behalf of my firm, to comment on the Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors, released on January 9, 2014. My firm, First River Advisory L.L.C., is a registered Municipal Advisor (MA) specializing in the non-profit health care sector. Since First River Advisory's formation in 1995, nearly all of its clients have been obligated persons rather than municipal entities.

I strongly support the MSRB's initiative to apply the fiduciary standard to obligated persons as well as to municipal entities. Obligated person clients of MAs deserve the same consideration with respect to the fiduciary standard as other issuers and borrowers in the municipal bond market. I do not believe that carrying forward this distinction due to differences in the services provided to municipal entity and obligated person clients, or for any other reason, is warranted. As a principal of a small MA firm, I do not believe that a requirement to accept the fiduciary standard with respect to all clients would represent a compliance burden.

In comparing notes with leaders of other firm members of the National Association of Independent Public Finance Advisors (NAIPFA) whose practices are more oriented to municipal entity clients, I have found that my firm's engagements are far more extensive and complex. For instance, First River Advisory's agreement with a current client was executed in September 2013 for a financing that is not expected to be concluded until the first calendar quarter of 2015. One of my activities earlier this week was my participation in an all-day planning session with this client's executives and its architects and construction managers to produce a comprehensive schedule for an ambitious facilities improvement project. My primary role was to ensure that accurate and complete project development information would be available in a timely manner for disclosure in a preliminary official statement. Due to these more extensive and complex engagements with obligated person clients during which more comprehensive scopes of services are ordinarily provided, it may be even more important that MAs be required to apply the fiduciary standard to obligated person clients than to municipal entity clients.

For the past 18½ years, First River Advisory has routinely accepted the fiduciary standard with respect to all of its clients. Between the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) in the autumn of 2010 and the release by the U.S. Securities and Exchange Commission of its Final Rule regarding Municipal Advisors in September 2013 (the SEC Final Rule), First River Advisory had taken the position that it has a fiduciary duty to obligated person clients, even though not specifically required by Dodd-Frank. It had been First River Advisory's expectation that the fiduciary standard inconsistency between municipal entity clients and obligated person clients would eventually be corrected. Further, it had always seemed to First River Advisory that in order to comply with MSRB Rule G-17, First River Advisory would have had to maintain a *de facto* fiduciary duty to its obligated person clients. First River Advisory's acceptance of the fiduciary standard was included in all client agreements executed during this period.

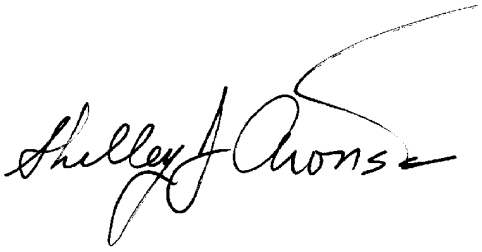
In order to prepare for the effective date of the SEC Final Rule, First River Advisory has prepared Written Policies and Procedures. First River Advisory's declared policy is the acceptance of the fiduciary standard, including the duty of loyalty and the duty of care, to all clients. This policy has been reflected in the one obligated person client agreement executed since the release of the SEC Final Rule.

First River Advisory has had a few municipal entity clients during its existence. They were not treated any differently than obligated person clients with respect to the fiduciary standard. I believe that it would be impractical for an MA firm to apply the fiduciary standard differently with respect to different types of clients. Moreover, I would not want to be put in a position to explain to an obligated person client that First River Advisory's municipal entity clients get the benefit of my firm's adherence to the fiduciary standard but that they are not entitled to such benefit.

I can also envision conflicts arising in connection with financings involving a conduit issuer (a municipal entity) which has its own MA. The objectives and concerns of conduit issuers and their borrowers (obligated persons) are not always aligned. In those cases, without consistent application of the fiduciary standard, the conduit issuer's MA would be required to accept the fiduciary standard, but the borrower's MA would not. Again, I would envision the borrower's executives asking "how come ..." questions, the responses to which would not likely be considered satisfactory by those executives.

Thank you for the opportunity to submit these comments. I may submit comments on other aspects of Draft Rule G-42, either on behalf of First River Advisory or in concert with other NAIPFA member firms.

Cordially,



325 North St. Paul Street
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March 7, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Suite 600
Alexandria, VA 22314

RE: Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisor

Dear Mr. Smith,

Thank you for the opportunity for First Southwest Company ("FirstSouthwest") to respond to the Proposed Rule G-42 (the "Rule") referenced above. We applaud the MSRB for taking prompt action regarding regulation of municipal advisors ("MA") once the final version of the Securities Exchange Commission definition of municipal advisor was promulgated. As former MSRB Chairmen, knowing first-hand the complexities and challenges of writing a rule that has many different facets, we will focus our comments on structural issues that we believe will help create a fair and efficient market for issuers and the professionals who practice in this area who will be affected by the Rule. As we have stated on many occasions, we are proponents of a fair and efficient marketplace that is not over burdened with regulation in terms of costs, but provides necessary protection to investors, issuers and creates a level playing field for professionals to compete on their merits. In general, we are supportive of the professional standards but are concerned that some of the standards and prohibitions could limit competition, increase costs to professionals and issuers and create standards that are simply not achievable. The public finance industry has demonstrated the benefits of any issuer who complies with the rules can access long term financing, giving them certainty of project cost. Overly burdening this market could have the adverse consequence of pushing issuers, small issuers in particular, to less transparent markets and with reduced long term certainty. We hope the MSRB can strike a balance between costs and issuer and investor protection.

With respect to market participants, we are concerned by some of the standards that are put forward that potentially create an uneven level of competition between professionals, through rewarding firms or MA's who have no ability to handle liability created in the course of providing financial advisory services will inevitably increase the cost of professional liability insurance to those who desire to have this level of protection. We are also concerned with the discrepancy between the MSRB's rules and regulations promulgated by the Commodities Future Trading Commission.

Principal Transactions

FirstSouthwest finds the proposed prohibition on principal transactions particularly troubling. As you know, the municipal market is large and diverse, with millions of individual CUSIPs, some of which can be traded for many years. Transacting in such securities may not necessarily be relevant or have any bearing on a current advisory engagement, as well as, potentially create higher costs or lower investment income for issuers that are investing with monies that are not attributable to the transaction that the MA has been engaged on. It is unclear how a blanket prohibition on a company or any affiliate of the advisor would serve the best interests of the issuer.

Fiduciary Duty and the Suitability Standard

While FirstSouthwest is supportive of improving the quality of advice to issuers through the implementation of a suitability standard for recommendations, there are a few important comments we wish to make. First, we feel that certain issuers are capable of independently evaluating risks in issuing municipal securities, and exercising independent judgment in evaluating recommendations of a municipal advisor. For this select group of issuers, it is appropriate to provide for an exemption to the suitability standard similar to the concept of "sophisticated municipal market professionals" exemption for large institutional investors.

Additionally, the extension of a duty of care to obligated persons in G-42(a)(i) is problematic and inconsistent with Dodd Frank and other SEC Rules. It is unclear why private parties would be subject to a fiduciary duty in this context. Additionally, such a provision would prove to be unduly burdensome on municipal advisors and hence increase costs.

Scope of Services and Compensation

Because of the complex realities in issuing municipal securities and serving governmental units, FirstSouthwest is a strong proponent of the idea that the scope of services should be determined through communication and negotiation between issuers and advisors. As such, we strongly disagree with any effort to prescribe services to be performed or regulate advisors' compensation for performing said services.

Specifically, the provisions in the Rule that impose upon the advisor an obligation to consider feasible alternatives, review third-party recommendations, and review official statements and feasibility studies, is inappropriate. In practice, this will result in advisors performing additional services that issuers may consider unnecessary and impose additional costs upon the issuer and evaluating unsolicited proposals that the issuer may not want to implement or require other professionals such as bond counsel to evaluate, for what may be minimal difference, and potentially increase risk to the issuer. Should an issuer pay for an evaluation of a proposal it is not comfortable with, such as an interest rate swap, which on paper may or may not be of financial benefit to the issuer. Furthermore, such a provision may violate pre-existing contracts between issuers and advisors where specific services have been negotiated or where other professionals are engaged such as disclosure and bond counsel. The standard or thorough review is vague and can lead to costly litigation, increase liability insurance costs and or reduce availability which could hurt issuer protection.

Additionally, FirstSouthwest has seen instances in the marketplace of municipal advisors facilitating private placements. When addressing scope of services under the Rule, is this considered an allowable duty or does it fall under the prohibition on principal transactions in the proposed G-42(f), in that it is considered an underwriting? The MSRB should be clear on this position because it affects all Municipal Advisors.

In the matter of compensation, the proposed G-42(g)(i) prohibits municipal advisors from receiving compensation that is "excessive". FirstSouthwest strongly objects to this language, as we feel it will lead to problems when comparing scope, quality, complexity of transactions and timeliness of services as well as differences in firm's resources or financial resources. "Excessive" is a subjective term, and changes over time and between individuals or firms. Issuers, at the time of negotiation, and not examiners or other third parties, are in the best position to judge the value of these services. Services provided and the level of expertise required varies greatly from issuance-to-issuance, and compensation should vary to reflect those differences. This is analogous to ranges in compensation for individuals in that there is no one right level for everyone because of differences in skills, experience and resources.

Disclosure

For some time, FirstSouthwest has felt that disclosure to issuers by some municipal advisors has been lacking and we applaud the MSRB for addressing these matters in the Rule. However, there are a few comments we would like to make on the Rule to assist the MSRB in arriving at a robust, fair and practical rule.

First, proposed Rule G-42(b)(ii) requires disclosure of "any affiliate of the municipal advisor that provides any advice, service or product to or on behalf of the client.... ." Because not *every* relationship rises to a level to create an irreconcilable conflict of interest or affect investors, we feel that there should be a materiality standard. Particularly in the case of large financial institutions, an advisor may have affiliated entities that provide any number of services to a client and/or their associated persons, such as brokerage, banking, insurance, or mortgage services. In the vast majority of these cases, the relationship is not of enough significance to create a true conflict of interest on the particular transaction or was secured through a competitive process where a governmental entity determined it was in the best interest to secure these services through a particular firm. The imposition of such a standard without a materiality provision would only create additional unnecessary administrative tasks when entering into a contract and thereafter, again ultimately increasing costs to the issuer.

We seek clarity for the requirement in G-42(b)(vii) to disclose other advisory engagements, which may not be appropriate and will dilute the value of disclosure. The section of the Rule "any other engagements or relationships of the municipal advisor or any affiliate of the municipal advisor that might impair the advisor's ability either to render unbiased and competent advice to or on behalf of the client or to fulfill its fiduciary duty to the client, as applicable... ." Because of the use of this standard of "might impair" used in conjunction with ability to fulfill its fiduciary duty creates an ambiguous standard and could be true in any circumstance that a firm has any client other than the client. Because of this standard, firms in an abundance of caution will disclose all their clients and this will in our opinion dilute the value of the disclosure. To our understanding neither lawyers nor accountants have this standard. Issuers when selecting

advisors evaluate experience and resources of a firm, as is evident in many issuers requesting experience and using ranking tables.

FirstSouthwest has long been a proponent of ensuring that issuers are contracting with municipal advisors with appropriate financial wherewithal as currently required by broker dealer municipal advisors, pursuant to SEC Rule 15c3-1. However, the proposed G-42(b)(vii) is concerning in that it requires the municipal advisor to disclose the existence and terms of advisors' professional liability insurance. Our fear is that such disclosure will result in a greater number of plaintiffs' firms targeting advisors with an eye on the advisor's insurance policy with the unintended result of either firm not having this protection, setting up special purpose entities with no resources, all of which would adversely affect the purpose of issuer protection. In our view, it is more appropriate to disclose the capital position of the firm, as required by SEC rules for other financial institutions such as broker-dealers.

Finally, the Rule's requirement to affirmatively state if the advisor has concluded that it has no material conflicts is troubling. If an undisclosed conflict is later discovered, it would surely be in violation of the very requirement to disclose it. Having an additional requirement to affirmatively state that there are no conflicts only serves to increase administrative requirements, and could provide an unnecessary "tack-on" violation in the event a conflict is later discovered.

In conclusion, we applaud the effort the MSRB is making to regulate municipal advisors, in a fair and efficient manner. We hope that our comments have illuminated issuers that may not have been considered during the drafting of the Rule. Please contact either of us directly at (214) 953-4128 or (713) 654-8641 if you have any questions regarding my comments or concerns.

Sincerely,

Hill A. Feinberg
Chairman and Chief Executive Officer

Michael G. Bartolotta
Vice Chairman

Frost

Post Office Box 1600
San Antonio, Texas 78296-1600

March 10, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: Request for Comment on Proposed MSRB Rule G-42, Duties of Non-Solicitor Municipal Advisors: MSRB Notice 2014-01

Mr. Smith:

Frost Bank, a commercial banking institution chartered in the State of Texas, appreciates the opportunity to comment on the above proposed rule, specifically section (f) regarding the prohibitions against a municipal advisor, or any affiliate of a municipal advisor, from engaging in any transaction in a principal capacity to which the municipal entity is a counterparty.

The proposed regulation would preclude banks such as Frost Bank from providing advisory services from our Trust Department regarding a municipality's pension fund assets or from our Capital Markets area regarding a municipality's issuance of a debt security and simultaneously provide that municipality with other traditional and necessary commercial and fiduciary banking services. These precluded service offerings would include deposit services, cash management including account sweeps, securities lending, lockbox services, securities safekeeping, bond proceeds investing, traditional lending services, employee payroll services, etc., all services that commercial banks have traditionally provided to the local governmental entities. When forced to choose between the advisory roles and that of being the provider of other banking services, commercial banks will likely exit the advisory role process, thus narrowing competition for and limiting the availability of such services.

A better solution would be to provide a specific and clear exemption for commercial banks who provide such advisory services from being subject to the proposed prohibitions on being a provider of other such traditional services to the municipalities. We do not believe it was the intent of Congress, nor is it the intent of the MSRB to lessen the competition in the marketplace or to lessen the availability of traditional banking or advisory services. Commercial banks have had a long history of providing such services to their local governments for many years in a forthright manner without undisclosed conflicts of interest. We trust that the MSRB will find a solution that enables these relationships to continue.

Sincerely,

William H. Sirakos
Senior Executive Vice President

George K. Baum & Company

INVESTMENT BANKERS SINCE 1928

March 10, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Notice 2014-01 (January 9, 2014): Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

On behalf of George K. Baum & Company ("GKB" or the "Firm"), we are pleased to provide our response to Municipal Securities Rulemaking Board ("MSRB") Notice 2014-01 (the "Request for Comment"). To help put our response in context; GKB is a small broker dealer whose principal business is municipal finance. Our firm provides a multitude of services to our clients, both municipal entities and obligated persons, including underwriting services and financial advisory services. When serving in an underwriting capacity, our principal bond distribution network is to institutional investors. We also have a relatively small retail distribution capacity. Accordingly, our comments are restricted only to our areas of expertise and therefore are not intended to be comprehensive of all of the provisions of Proposed Rule G-42.

Please also note that our firm is a member of both the Bond Dealers of America ("BDA") and the Securities Industry and Financial Markets Association ("SIFMA"). The BDA and SIFMA are submitting separate comment letters in response to the Request for Comment. GKB approves, endorses and supports all of the comments and suggestions being provided by the BDA and by SIFMA.

Comprehensive Rules Pertaining to Municipal Advisors

The MSRB previously has stated that it will be issuing various proposed regulations pertaining to Municipal Advisors, in addition to Proposed Rule G-42. The MSRB has announced its intention to issue such proposed regulations in phases, beginning first with Proposed Rule G-42 (and related proposed revisions to Rules G-8 and G-9). While we acknowledge that forthcoming additional regulations beyond Proposed Rule G-42 would be prudent and appropriate, we are concerned that this phased approach to issuing proposed regulations may lead to unintended inconsistencies and related undue burdens. Because we cannot know or predict with certainty where the purview of each such future additional proposed rule will begin or end, or how each might impact or correlate to Proposed Rule G-42, in our opinion it is likely that such future proposed rules might necessitate or warrant additional comments regarding the scope, purview or application of Proposed Rule G-42. Therefore, we urge the MSRB to not

finalize any of the rules governing the behavior of municipal advisors, including but not limited to Proposed Rule G-42, until all of those rules which the MSRB intends to propose at least have been published for comment. Doing so, in our opinion, will help mitigate any unintended inconsistencies in drafting, interpretation and application of comprehensive rules for municipal advisory activities.

Whether Proposed Rule G-42 Should Require a Duty of Care to an Obligated Person

The Request for Comment on Proposed Rule G-42 properly notes (on page 3) that, "the Dodd-Frank Act itself specifically establishes that a fiduciary duty is owed by a municipal advisor to its municipal entity clients. By contrast, the Dodd-Frank Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients." (footnote citations omitted) As so acknowledged by the MSRB, federal securities law dictates that a Municipal Advisor owes a fiduciary duty when it acts as an advisor "to [a] municipal entity." (See Securities Exchange Act of 1043, as amended (the "Exchange Act"), § 15B(c)(1).) Congress did not authorize or impose a fiduciary duty on Municipal Advisors when acting as an advisor to obligated persons. The Securities and Exchange Commission ("SEC"), in promulgating its final municipal advisor registration rules (the "SEC MA Rules"), clearly recognized these distinctions and expressed its opinion that Municipal Advisors owe a duty of fair dealing to obligated person clients under MSRB Rule G-17, and not a fiduciary duty. (See SEC Adopting Release, No. 34-70462, at page 156.)

Proposed Rule G-42, however, does not adopt this same approach, instead proposing to impose a duty of care on a Municipal Advisor when acting as an advisor to an obligated person client. Because neither Congress nor the SEC requires or imposes such an obligation, we believe that if the MSRB wishes to impose a duty of care on a Municipal Advisor when acting as an advisor to an obligated person client, the MSRB should clearly state the legal authority for that requirement, and the justification for taking this additional step, including providing evidence of abuses which demonstrate the need for a more robust regulatory framework than that adopted by Congress and the SEC. We recommend instead that the MSRB revise Proposed Rule G-42 to remove any imposition of a duty of care on a Municipal Advisor when acting as an advisor to obligated persons, and instead rely upon the existing provisions of Rule G-17 that impose a duty of fair dealing on all Municipal Advisors. In our opinion, that approach will enhance simplicity and consistency between the requirements, interpretation and application of federal securities laws, the SEC MA Rules and applicable MSRB Rules pertaining to duties owed by Municipal Advisors to obligated person clients. In our opinion, non- municipal entity obligated persons have different characteristics than municipal entities. Non-municipal entity obligated persons are not associated with the handling of public funds. Non-municipal entity obligated persons are private business, either for-profit or not-for-profit, and therefore operate with a different level of public accountability. Since the MSRB requires only that a duty of fairness apply when brokers, dealers, or municipal securities dealers deal with other types of private business (such as other broker dealers), we believe this same duty should be applied when Municipal Advisors deal with the type of private business class defined as obligated persons.

Municipal Advisors Acting as a Principal

Proposed Rule G-42(f) is summarized in the Request for Comment (page 6), as follows: "Draft Rule G-42 prohibits a municipal advisor (and any affiliate) from engaging in any transaction in a principal capacity to which the municipal entity or obligated person client of the municipal advisor is a counterparty, except for activity that is expressly permitted by underwriters under Rule G-23." The Request for Comment and Proposed Rule G-42(f), however, do not specifically identify which provisions of Rule G-23 were intended to be included within this exception. Accordingly, Proposed Rule G-42(f) is too ambiguous and overly broad. If the MSRB intended the exception to incorporate the provisions of Rule 23 (d) (ii) and (iii), we believe that affirmatively stating similar exceptions, revised to apply to Municipal Advisors to municipal entity clients and limited to specific transactions, would be much more direct and clear. Accordingly, for the reasons set forth below, we recommend that Proposed Rule G-42(f) should be revised to state as follows:

> "A municipal advisor for a municipal entity on a transaction is prohibited from engaging in any principal capacity on that transaction, except as stated below:
>
> A municipal advisor for a municipal entity shall not be prohibited from acting as agent for the municipal entity in arranging the placement of the entire issue with any state, local or federal governmental entity as part of a plan of financing by such entity for or on behalf of the municipal entity, but only if such municipal advisor does not receive compensation from any person other than with respect to municipal advisory services related to such placement and does not receive compensation from any person for underwriting any contemporaneous financing transaction directly or indirectly related to such issue undertaken by the state, local or federal governmental entity with which such issue was placed.
>
> The limitations set forth above shall also apply to any broker, dealer, or municipal securities dealer controlling, controlled by, or under common control with the broker, dealer, or municipal securities dealer having a municipal advisory relationship with a municipal entity client with respect to the issuance of municipal securities. The use of the term "indirectly" shall not preclude a broker, dealer or municipal securities dealer that has a municipal advisory relationship with a municipal entity client with respect to the issuance of municipal securities from purchasing such securities from an underwriter, either for its own trading account of for the account of customers, except to the extent that such purchase is made to contravene the purpose and intent of this rule."

In our opinion, Rule G-42(f) should be revised as suggested above for two reasons. First, as currently proposed by the MSRB, Proposed Rule G-42(f) would overstep the guidance in other existing regulations (such as Rule G-23 and the SEC MA Rules) which clearly recognize that a municipal advisory relationship related to the issuance of municipal securities is a transaction-by-transaction decision between a service provider and a municipal entity. Under the current version of Proposed Rule G-42(f), however, a

municipal advisory relationship instead would become a client based relationship which seemingly would continue forever in time. Given the nature of the municipal securities business, it will be almost impossible for a broker dealer to never act as a Municipal Advisor for a client. Under Proposed Rule G-42(f), as currently written, if a broker dealer ever worked as a Municipal Advisor for a client, that broker dealer would be prohibited from acting as a principal on any of the client's transactions forever. If Proposed Rule G-42(f) becomes effective as currently proposed by the MSRB, ultimately no broker dealer will be available to act as an underwriter for any client.

Second, as noted above, Proposed Rule G-42(f) would overstep the guidance in other existing regulations (such as Rule G-23 and the SEC MA Rules) which currently recognize the difference between a financial advisory or municipal advisory relationship with a municipal entity or an obligated person. In the MSRB's Notice On Application Of Board Rules To Financial Advisory Services Rendered To Corporate Obligors On Industrial Development Bonds (May 23, 1983), the MSRB states:

> "Board rules G-1 and G-3 provide that rendering "financial advisory or consulting services for *issuers*" is an activity to which those rules are applicable (emphasis added). Similarly, Board rule G-23, on the activities of financial advisors, applies to brokers, dealers, and municipal securities dealers who agree to render "financial advisory or consultant services to or on behalf of an *issuer*" (emphasis added). Clearly these rules are applicable to financial advisory services rendered to state or local governments and their agencies, as well as to municipal corporations. In the Board's view, however, rules G-1, G-3, and G-23 do not apply to financial advisory services which are provided to corporate obligors [obligated persons] in connection with proposed IDB financings."

Moreover, the SEC states in its Registration of Municipal Advisors, Frequently Asked Questions, issued on January 10, 2014 (last updated on January 16, 2014) (the "FAQs"), in the section titled "Question 5.2: Switching Roles From Municipal Advisor to Underwriter":

> "If a broker-dealer acts as a municipal advisor to a municipal entity with respect to an issuance of municipal securities, it owes a fiduciary duty to the municipal entity with respect to that issue and must not take any action inconsistent with its fiduciary duty to the municipal entity. Additionally, the broker-dealer must comply with MSRB Rule G-23, which prohibits persons from switching from the role of financial advisor to the role of underwriter with respect to the same issuance of municipal securities."

Only here, in all of the SEC's FAQs and answers, does it omit any mention of obligated persons. The SEC expressly mentions obligated persons in many other places in its FAQs and the SEC MA Rules. The SEC could have included obligated persons in its discussion of restrictions imposed by MSRB Rule G-23 on role switching, but did not do so. Clearly the SEC intended that a person can be a Municipal Advisor for an obligated person and still be an underwriter on the municipal securities issued by the municipal entity.

Evidencing a Municipal Advisory Relationship in Writing

In describing Proposed Rule G-42(c), the Request for Comment (page 9) states, "Under draft rule G-42(c), municipal advisors must evidence each of their municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship."

Section 15B(e)(4)(A) of the Exchange Act (as amended by the Dodd-Frank Act) and the SEC MA Rules define a Municipal Advisor to mean a person (who is not a municipal entity or an employee or a municipal entity) that: 1) provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms and other similar matters concerning such financial products or issues; or 2) undertakes a solicitation of a municipal entity.

In summary, there are three activities which can make someone a Municipal Advisor:

- Providing advice with respect to the issuance of municipal securities;
- Providing advice with respect to municipal financial products; or
- Undertaking a solicitation of a municipal entity.

In our opinion, each of these circumstances should be dealt with and addressed separately in determining when and how a Municipal Advisor must evidence its relationship with its clients.

<u>Providing advice with respect to the issuance of municipal securities</u>

Rule G-23(b) states, "For purposes of this rule, a financial advisory relationship shall be deemed to exist when a broker, dealer, or municipal securities dealer renders or enters into an agreement to render financial advisory or consultant services to or on behalf of an issuer with respect to the issuance of municipal securities, including advice with respect to the structure, timing, terms and other similar matters concerning such issue." Clearly for a broker, dealer, or municipal securities dealer, when providing advice to or on behalf of an issuer with respect to the issuance of municipal securities to an issuer, acting as a Financial Advisor or as a Municipal Advisor are functionally the same.

Rule G-23(c) states, "Each financial advisory relationship shall be evidenced by a writing entered into prior to, upon or promptly after the inception of the financial advisor relationship". The MSRB's Guidance on the Prohibition on Underwriting Issues of Municipal Securities for Which a Financial Advisor Relationship Exists Under Rule G-23 states, "Although Rule G-23(c) requires a financial advisory relationship to be evidenced in writing, a financial advisory relationship will be deemed to exist whenever a dealer renders the types of advice provided for in Rule G-23(b), regardless of the existence of a written agreement."

Therefore, according to Rule G-23, in order to establish a financial advisory relationship two conditions must be present. The first is that there must be an agreement between the broker, dealer, or municipal securities dealer and an issuer that there is mutual desire to enter into a financial advisory relationship

(even if such agreement is not in writing) and second, that the financial advisor has to provide advice. The fact that these two requirements exist in combination is very important because it means that a broker, dealer, or municipal securities dealer doesn't inadvertently become a financial advisor without the participation by the issuer. This extremely important concept is also present in the SEC MA Rules where an underwriter cannot take advantage of the underwriter exemption without the participation of the issuer, because the issuer has to grant the exemption to the underwriter.

For the purposes of Proposed Rule G-42, we believe that the regulatory requirement for becoming a municipal advisor when providing advice with respect to the issuance of municipal securities should require: (1) that the municipal advisor must provide advice, and (2) that the municipal entity or obligated person must have recognized that it is advice and have the expectation and desire that it carried a fiduciary duty or a duty of fairness, respectively. Without this second prong, unintended problems or complications are likely to arise. An example of when this would be a problem would involve an employee of a broker dealer whose firm has invented a new type of financing mechanism. If the sponsors of a municipal entity conference invite the employee to make a presentation at the conference about the new financing mechanism, then the employee presenting that information could be viewed as giving "advice" to every municipal entity in attendance. We believe, however, that none of the municipal entities in attendance would be hearing the information with any expectation or desire that the presenter had a fiduciary responsibility to the municipal entity. As a result, we believe that only when information is conveyed or given in a forum or manner where a municipal entity has an expectation and a clearly stated desire that the presenter owes it a fiduciary responsibility, does the employee/presenter or his or her firm become a municipal advisor and trigger the requirement to evidence the relationship in writing, whether or not the municipal advisor will be paid for the advice.

<u>Providing advice with respect to municipal financial products</u>

When a person or entity becomes a municipal advisor by providing advice with respect to municipal financial products, we believe that all of the requirements for being deemed a municipal advisor with respect to the issuance of municipal securities should apply, with the exception that the municipal advisor should only have to evidence the relationship if they are to be paid for the advice. Unlike the situation where a person becomes a municipal advisor by providing advice with respect to the issuance of municipal securities, when providing advice with respect to municipal financial products, there is only one possible roll - municipal advisor. No other role which might provide a conflict with the municipal entity or obligated person is possible. As a result, when a person becomes a municipal advisor with respect to municipal financial products, the only need for a written agreement is to clearly describe the consideration to be exchanged between the parties for those services - the payment to be made to the municipal advisor. We believe that this is the only instance where a written agreement should be required when rendering advice with respect to municipal financial products.

Undertaking a solicitation of a municipal entity

Even though Proposed Rule G-42 does not address the duties of a Municipal Advisor when undertaking the solicitation of a municipal entity, the rule as currently proposed would require a written agreement for any municipal advisory relationship, even one obtained through a solicitation. We recommend the language in Proposed Rule G-42 be changed so that it is clear that Proposed Rule G-42 covers only those instances where an entity becomes a municipal advisor by providing advice on the issuer of municipal securities or municipal finance products.

In the Request for Comment, the MSRB states that it intends to issue, at a later date, additional proposed rules with regard to solicitation activities. When the MSRB is drafting any such future proposed rules, we urge the MSRB to separately address and treat differently a solicitation of municipal entity with respect to the issuance of municipal securities, and a solicitation with respect to municipal financial products. In our opinion, a person who becomes a municipal advisor because they undertake a solicitation of a municipal entity with respect to the issuance of municipal securities should have to evidence the relationship in writing as illustrated above. We also believe that a person who becomes a municipal advisor because they undertake a solicitation with respect to municipal financial products should only have to evidence their relationship in writing if they are successful in the solicitation, and as described above, if the resulting engagement will result in the municipal advisor being paid a fee for their advice.

Thank you in advance for your attention to our concerns and suggestions.

Sincerely,

Guy E. Yandel
EVP & Head of Public Finance

Dana L. Bjornson
EVP, CFO & Chief Compliance Officer

Andrew F. Sears
SVP & General Counsel

Government Finance Officers Association
1301 Pennsylvania Avenue, NW Suite 309
Washington, DC 20004
(202) 393-8020

March 13, 2014

Mr. Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Draft MSRB Rule G-42 – Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

Thank you for the opportunity to comment on the important topic of the Municipal Securities Rulemaking Board's (MSRB) draft Rule G-42, pertaining to the duties of non-solicitor municipal advisors (MAs). The MSRB's development of regulations related to the SEC's final Municipal Advisor Rule is of great interest to many of our members, as issuers will be affected by the proposed regulatory framework for these professionals, particularly with regard to fiduciary duty.

Members of the Government Finance Officers Association's (GFOA) Governmental Debt Management Committee helped develop these comments, and remain concerned about the fiduciary responsibilities of MAs as discussed in the draft rule, as well as the roles that MAs should serve as defined and referred to throughout the rule.

Below are our comments on the specific provisions in the proposed rule that relate to our members.

Principal Transactions

This section is one of the most important parts of the proposed rulemaking but one that we find confusing. Before we can provide more substantive comments on this issue, we request clarity on the MSRB's definition of a *principal transaction.* While the rule should specifically identify material conflicts and prohibit the MA firm from acting in a separate capacity that could create or cause a conflict, it is unclear exactly where the proposed rule draws the line. Again we request further clarification on this issue including examples of prohibited and acceptable practices before we can further comment.

Municipal Advisor/Issuer Relationship and Scope of Work

We understand and support the MSRB's responsibilities to develop regulations for MAs. A recurring issue throughout the proposed rule is whether the MSRB should develop specific criteria governing the type of work a MA should provide to an issuer. Rather than having the MSRB dictate the scope of work between MAs and issuers, we believe the issuer should set the standard for the scope of work and control the engagement with the MA. In this regard, the issuer should determine whether it wishes to have the MA review the official statement or assist in its development. In addition, the issuer could define the scope of work to include review of feasibility studies and financing strategies provided by other professionals. We agree that the MA/issuer relationship should be stated in writing, which allows the issuer to clearly delineate the scope of work that it intends for its MA.

Recommendations to Clients/Suitability and Duties

We support the proposed rule's standards for suitability, duty of care, duty of loyalty, and to know your client regarding financing strategies. These should be maintained in subsequent revisions of the rule.

Prohibited Activities/Conflicts of Interest

As we noted above regarding principal transactions, we request further explanation of the term *principal transaction* and greater clarity on when a firm may serve as an MA and also be party to other transactions of a municipal entity. We support the list of prohibited activities on page 13 of the release. We also support the need for municipal advisors to disclose conflicts of interest. However, the MA's fiduciary duty to the client should remain the dominant feature of the rule. While the issuer should acknowledge any conflicts that may exist with the MA firm, we would expect the rule to incorporate how the acknowledgements of such conflicts relate to the MAs fiduciary duty. Of note, we agree that fee splitting appears to be an inherent conflict, and should be avoided.

Fee Structure Used by MAs with their Issuer Clients

On the topic of fees paid to the MA by the issuer, we would like to reference GFOA's best practice on *Selecting and Managing the Engagement of Municipal Advisors*[1]. While the Best Practice discusses concerns with the common practice of paying municipal advisors on a contingency basis, we do not support having the MSRB mandate the manner in which an MA charges for its services. Rather, as we noted above, the issuer should determine the manner and amount of the MA compensation.

MSRB Fees Imposed on MAs

We request that the MSRB include similar language in the rule that is in place for bond dealers that prohibits fees from being passed through to issuers.

Request for Re-proposing this Rulemaking

We strongly urge the MSRB to re-propose the rule for comment following review of comment letters and the Board's subsequent updates to this proposed version. Due to the importance as the first set of major rulemaking governing MAs, it would be helpful to all municipal market stakeholders, including the MSRB, to allow market participants to further review how comments are clarified by the Board prior to the proposed rulemaking submission to the SEC.

Thank you again for the opportunity to comment on this important rulemaking.

Sincerely,

Dustin McDonald
Director, Federal Liaison Center

[1] *Selecting and Managing the Engagement of Municipal Advisors* - **Basis of Compensation**. Fees paid to municipal advisors should be on an hourly or retainer basis, reflecting the nature of the services to the issuer. Generally, municipal advisory fees should not be paid on a contingent basis to remove the potential incentive for the municipal advisor to provide advice that might unnecessarily lead to the issuance of bonds. GFOA recognizes, however, that this may be difficult given the financial constraints of many issuers. In the case of contingent compensation arrangements, issuers should undertake ongoing due diligence to ensure that the financing plan remains appropriate for the issuer's needs. Issuers should include a provision in the RFP prohibiting any firm from engaging in activities on behalf of the issuer that produce a direct or indirect financial gain for the municipal advisor, other than the agreed-upon compensation, without the issuer's informed consent.

Mr. Ronald W. Smith
Municipal Securities Rulemaking Board
Comment on the Draft MSRB Rule G-42

Government Investment Officers Association

www.gioa.us
702-255-3224

March 7, 2014

Mr. Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Draft MSRB Rule G-42
Duties of Non-Solicitor Municipal Advisors

Comments Submitted Electronically

Dear Mr. Smith:

The Government Investment Officers Association ("GIOA") represents government investment officers across the United States. While primarily an educational institution, we felt it appropriate to comment on potential changes and proposed rules that could affect cash management practices for our organizations.

The GIOA appreciates the opportunity to provide comments to the Municipal Securities Rulemaking Board ("MSRB") on its proposed standards for non-solicitor municipal advisors. The GIOA urges the Board to consider the following thoughts on the municipal advisor rule, especially with regard to the investment of bond proceeds.

Prohibition Against Principal Transactions for Bond-Related Proceeds

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") specifically established that a fiduciary duty is owed by an advisor to its municipal entity clients. Neither the Dodd-Frank Act nor the SEC's Final Rule for municipal advisors define what is meant by the term "fiduciary duty". Your draft Rule G-42 elaborates on the role of a Municipal Advisor, including defining the fiduciary duties an advisor may have toward municipal entities such as ourselves.

We manage bond proceeds for ourselves, but also manage significant assets on a fiduciary basis for related governmental entities within our states and counties. These Local Government Investment Pools, or "LGIPs", allow our communities to enjoy the benefit of professional money management at significantly reduced costs. Our communities deposit operating as well as capital funds, such as bond proceeds, in these funds and therefore these

funds would be directly affected by the terms of draft Rule G-42.

We strongly support the MSRB's initiative to apply a fiduciary standard to issuers and borrowers in the municipal bond market. However, the proposed draft Rule G-42 specifically prohibits a municipal advisor (and any affiliate) from engaging in any transaction in a principal capacity to which municipal bond-related funds are involved.

In most cases, this prohibition would extend to our bond proceeds accounts which, of course, represent proceeds of municipal bond transactions. The draft Rule G-42 allows an exemption for activities that are permitted under Rule G-23, but those provisions do not include the typical investment activities which we perform on a daily basis.

Some unintended consequences of the draft Rule G-42 would be:

- Not allowing us to invest the proceeds of any municipal bond transaction with any broker-dealer firm acting in a principal capacity. Firms would have to consider themselves acting as fiduciaries with regard to the investment of our funds;
- Similarly, the draft Rule G-42 would not allow us to invest our Local Government Investment Pools with any broker-dealer firm acting in a principal capacity; and
- Potentially require an outside investment advisor acting as Fiduciary for our bond proceeds and Local Government Investment Pools in order to comply with the restrictions.

Each of the above scenarios represents increased costs which would ultimately be paid by state and local governments and the communities we serve through a reduction in interest earnings.

Clarification of the Role and Duties of the Securities Professional with Regard to Public Clients

As public investors, we are exempt from the registration requirements. What the rules do not specifically address are how the securities firms and banks that we utilize (as principal counterparties) are supposed to maintain their independence while acting as a fiduciary for a portion of the funds that we manage.

As mentioned above, we manage capital funds, operating funds and fiduciary funds for entities within our states. The proposed rules suggest that our investment counterparties (broker-dealers) act in the following manner with regard to our transactions:

Public Fund Type	Counterparty Role
Operating Funds	As Principal
Capital Funds	As Fiduciary
LGIPs	As Fiduciary

Thankfully, the burden of compliance is not our responsibility; however the "costs" of maintaining compliance with the proposed rules would certainly be paid by state and local governments and the communities we serve through a decrease in investment earnings.

If we were to decide that we would need to "split off" management of our capital and fiduciary funds in order to comply with the restrictions in draft G-42, we would lose oversight of those monies and increase management fees on the ultimate beneficiaries of those funds.

In 2011, the MSRB circulated draft rules which addressed the above issues and created an exemption to those firms which were swept up in the definition of municipal advisor even though there was advice only being given for investment assets.

Mr. Ronald W. Smith
Municipal Securities Rulemaking Board
Comment on the Draft MSRB Rule G-42

Your draft rules at that time addressed what draft Rule G-36 called an "unmanageable conflict" with municipal advisors that acted as principals to other transactions.

As you know, draft Rule G-36 was not adopted and was superseded last year by the SEC's Municipal Advisor rule. We would urge that the MSRB include some similar language in Rule G-42 to that proposed in Rule G-36 to address the restriction on principal investment activity by municipal entities.

Thank you for the chance to comment on the draft Rule G-42. If we can offer any assistance to the MSRB in your deliberations, or if we can answer any questions concerning about the investment of bond proceeds or pooled funds by public sector entities, please don't hesitate to contact us.

Respectfully,

Laura B. Glenn, CFA
Georgia State Treasurer's Office

Sheila Harding
City of Lynwood, California

Mary Christine Jackman
Maryland State Treasurer's Office

Pamela Jurgensen
Nevada State Treasurer's Office

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Rick Phillips, President Emeritus, GIOA
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March 4, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: MSRB Notice 2014-01 Relating to
Standards of Conduct for Municipal Advisors

Dear Mr. Smith:

The Investment Company Institute (ICI)[1] appreciates the opportunity to provide comments to the Municipal Securities Rulemaking Board (MSRB) on its proposal to adopt a new Rule G-42 to govern standards of conduct for non-solicitor municipal advisors.[2] Inasmuch as the new rule will expressly apply to municipal advisors to sponsors or trustees of 529 college savings plans,[3] the Institute has reviewed the rule from the perspective of such advisors and, based on our review, supports its adoption. We commend the MSRB for giving deliberate consideration to the duties that a municipal advisor should owe to its municipal clients and for taking the lead in setting standards of conduct for this new category of registrants. Notwithstanding our support for the rule, we recommend several revisions to it to clarify how these new standards will apply in the context of 529 college savings plans. We also recommend that the MSRB clarify that the rule shall only apply prospectively.

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[1] The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $16.3 trillion and serve more than 90 million shareholders.

[2] *See Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors,* MSRB Notice No. 2014-01 (Jan. 9, 2014), which is available at: http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-01.ashx?n=1. Consistent with the scope of the proposed rule, as used in this letter the term "municipal advisor" or "advisor" refers to a "non-solicitor municipal advisor."

[3] *See* Supplementary Material .10 to proposed Rule G-42. We appreciate the MSRB including this clarification in the rule. Our comments on the rule are limited to its impact on our members that must register as municipal advisors due to their involvement in a state's 529 college savings plan. We note that our members that are registered under the Investment Advisers Act of 1940 and render advice to municipal entities other than 529 college savings plans are not required to register as municipal advisors and therefore will not be subject to the rule.

I. Overview of Proposed Rule G-42

As proposed, the new rule would subject a municipal advisor to a duty of care as well as to a fiduciary duty that includes a duty of loyalty. The rule would also: impose disclosure requirements on municipal advisors; require documentation of the terms and extent of the advisor's relationship with each municipal client; prohibit recommending a municipal securities transaction or product unless the advisor has a reasonable basis for believing that it is suitable for the client; requiring the advisor, upon request of a client, to review another party's recommendation to the client; prohibit principal transactions except in limited circumstances; and prohibit specified conduct. The rule includes Supplementary Material to provide additional guidance on its provisions.

We recommend that, prior to finalizing its proposal and filing it with the U.S. Securities and Exchange Commission for adoption, the MSRB address each of the issues discussed below, which arise as a result of the rule's application to those municipal advisors whose activities as a municipal advisor are limited to serving as a sponsor or advisor to one or more state 529 college savings plans.

II. Issues Raised by the Rule's Application to Advisors to 529 Plans

A. Subsection (a) and Supplementary Material .01 and .02, Standards of Conduct

Subsection (a) of Rule G-42 would define a municipal advisor's standard of conduct as a (1) duty of care and (2) fiduciary duty that includes a duty of loyalty and a duty of care. According to Supplementary Material .01, the advisor's duty of care would require the advisor to "undertake a reasonable investigation to determine that it is not basing any recommendation [made to the municipal client] on materially inaccurate or incomplete information." In the context of 529 college savings plans, it is not uncommon for the municipal advisor that is acting as a plan sponsor to work with the appropriate representatives of a state's plan to design a plan that best meets the needs and requirements of the state and complies with any state or Federal laws governing the plan's operations. As part of this process, the advisor oftentimes relies upon its state partner to provide the advisor information that is necessary for the advisor to fulfill its obligations and duties to the plan. We believe that, in such circumstances, a municipal advisor should not be required to verify the veracity or completeness of information provided to it by those state employees or officials who are authorized to act on behalf of the plan. We recommend that the MSRB expressly affirm in Supplementary Material .01 that a municipal advisor is not required to investigate whether information provided to it by persons who are authorized by a municipal client to act on behalf of a state's 529 plan is materially inaccurate or incomplete.

Supplementary Material .02, which is also related to this subsection of the rule, would require, in part, that a municipal advisor "investigate and consider other reasonably feasible alternatives to any recommended municipal securities transaction or municipal financial product that might also or alternatively serve the municipal entity client's objectives." We are uncertain how this requirement

would apply in the context of a municipal advisor advising a state on its 529 plan. In particular, we question what other "securities transactions or municipal financial products" such advisor is expected to investigate or consider as part of its duty of loyalty. Indeed, this provision seems to have been drafted to address concerns with advisors who render advice regarding municipal securities other than municipal fund securities in mind. We recommend that the MSRB either eliminate this requirement for advisors to 529 plans or clarify that it may not be applicable to all advisory relationships.

B. Subsection (b) and Supplementary Material .07, Disclosure of Conflicts of Interest

Subsection (b) of the rule lists nine different items of information that a municipal advisor must disclose to its client at or prior to the inception of a municipal advisory relationship. As a preliminary matter, we recommend that the prefatory language to this list of items clarify that the advisor is only required to disclose those items that are applicable to its relationship with the client.[4] This would ensure that advisors are not required to provide "negative" disclosure to the client.[5] In addition, we recommend that subdivision (b)(viii), which would require disclosure of "the amount and scope of coverage of professional liability insurance that the municipal advisor carries" and related information, be deleted from this list. We are not aware of any other financial industry professionals that are required to disclose information regarding their insurance coverage to a client, and we do not understand the public purpose of the MSRB imposing such a requirement.[6] Indeed, requiring disclosure of such information to each and every municipal client would appear to be both unprecedented and unnecessary.[7] For these reasons, we recommend deleting this information from the list of required disclosures.

Supplementary Material .07 provides additional guidance regarding an advisor's disclosure obligations. Among other things, it requires a municipal advisor to "provide written disclosure to investors" of certain affiliations that must be disclosed pursuant to Rule G-42(b). We do not understand why the MSRB would include in a rule that governs the standards applicable to an advisor's relationship with a municipal client, a provision that requires the advisor to make specified disclosures

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[4] In particular, we recommend that this prefatory language read in relevant part [new language indicated by underscoring]: " . . . including disclosure of <u>each of the following as applicable:".</u> We also recommend deleting the "as applicable" qualifier from subdivision (b)(i) of the rule because it would be unnecessary if you follow our recommended edit to this provision.

[5] This approach would be consistent with the requirements of the SEC's "brochure rule." Rule 204-3(d) under the Investment Advisers Act, which permits an adviser to omit "inapplicable information" from the disclosure it is required to provide to clients.

[6] We note that, when the MSRB enhanced the disclosure that underwriters must provide to their clients under MSRB Rule G-17, relating to fair dealing, to alert them to conflicts of interest, among other information, it did not require disclosure of insurance coverage. *See Interpretive Notice on Duties of Underwriters to Issuers,* MSRB Notice 2012-25 (May 2012).

[7] It also seems as though this disclosure is an implicit invitation for a municipal client to sue an advisor up to the limit of its liability insurance, which seems inappropriate.

"to investors." It is unclear, for example, how this provision is intended to apply in the context of a municipal advisor interacting with a state on its 529 plan. Indeed, because of the structure of 529 plans and Federal and state restrictions on the ability of financial institutions to share their customers' non-public personal information, a municipal advisor likely has no access to information about the plan's investors or how to contact them and would, therefore, be unable to provide such investors the written disclosure required by this provision.[8] Moreover, the advisor may have no control over the contents of the official statement used by the plan or its underwriter, so it would be unable to require the plan or its underwriter to include the required disclosure in such document. Accordingly, we strongly recommend that the MSRB either delete Supplementary Material .07 in its entirely or clarify that its disclosure requirements do not apply to advisors that provide advice to 529 plans.

C. Subsection (c), Documentation of the Municipal Advisory Relationship

This provision in the rule would require a municipal advisor to provide its municipal client written disclosure of certain terms of its advisory relationship, including the compensation arrangements. It would further require the advisor to promptly amend or supplement the required disclosure "to reflect *any* change in or addition to the terms or information." [Emphasis added.] The only exception to this is if there is a change to the amount of reasonably expected compensation. In such event, updated disclosure is only required if the change is "material." It seems unnecessarily burdensome to require *all* changes to an advisor's written disclosure to be revised except material changes to the compensation disclosure. A more reasonable approach that would not adversely impact the client would be to utilize the materiality standard as the trigger for all updates to the disclosure, not just those relating to compensation. This approach would be more consistent with the updating requirements the SEC imposes on the disclosure documents of Federally-registered investment advisers.[9] We therefore recommend that the rule be revised to require updating of the written disclosure only when there is a material change to information previously disclosed, regardless of the nature of the change.

D. Subsection (d) and Supplementary Material .08, Recommendations

Subsection (d) of the rule imposes a suitability standard on advisors. In particular, it provides that a municipal advisor "may only recommend a municipal securities transaction or municipal financial product that is in the . . . best interest" of the municipal entity client. It is not clear how this requirement would apply to an advisor to a 529 plan. As noted above, 529 plans are typically

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[8] Even assuming the advisor could contact investors in the plan, such investors would likely (1) be confused by such disclosure as they may have no relationship with the advisor and (2) question why the information is being provided to them.

[9] *See* Instruction 4 to SEC Form ADV, which requires an adviser to amend the disclosure document it provides to investors when the material in such document becomes "materially inaccurate." The instructions to Form ADV are available on the SEC's website at: http://www.sec.gov/about/forms/formadv-instructions.pdf.

authorized and established by state law with a state office or agency assigned responsibility for the plan's creation, operation, and oversight. Due the nature of the relationship between the plan and the municipal advisor in establishing, operating, and overseeing the plan, we are uncertain which recommendation(s) in this relationship would be subject to the proposed suitability requirement. The mismatch between a suitability requirement and the conduct or responsibilities of municipal advisors in a 529 plan context is further demonstrated when one considers the factors that Supplementary Material .08 requires to be taken into account in making this suitability determination. According to Supplementary Material .08, the advisor's suitability determination

> . . . must be based on the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued in the municipal securities transaction are reasonably expected to be outstanding and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry.

These factors do not make sense in the context of the relationship between a municipal advisor and a 529 college savings plan. Indeed, they appear to contemplate situations in which a municipal advisor provides advice or recommends a municipal security to an individual or retail investors rather than in the context of providing advice to a state offering a 529 plan. We recommend that the MSRB address this incongruity by either affirming that these suitability factors do not apply to municipal advisors advising 529 plans or, alternatively, clarifying how the MSRB intends them to apply in this context.

III. PROSPECTIVE APPLICATION OF RULE G-42

Finally, the Institute recommends that the MSRB clarify that, once adopted, Rule G-42 will only apply prospectively. As such, a municipal advisor will only be required to comply with the relevant requirements of Rule G-42 when it either enters into a new advisory relationship with a municipal client or when it recommends a new municipal securities transaction or municipal financial product to an existing municipal client. This clarification, which will avoid disrupting existing relationships and contracts, is particularly important to advisors advising 529 plans due to the nature of the advisory relationship and the duration of existing contacts.

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We appreciate the opportunity to provide these comments and your consideration of them. If you have any questions, please contact the undersigned at (202)326-5825.

Sincerely,
/s/
Tamara K. Salmon
Senior Associate Counsel

J.P.Morgan

March 10, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Draft MSRB Rule G-42 on the Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

JPMorgan Chase Bank, N.A. and J.P. Morgan Securities LLC (collectively, and including relevant affiliates, "JPMC") appreciate the opportunity to comment on draft Rule G-42 ("Proposed Rule G-42") as proposed by the Municipal Securities Rulemaking Board (the "MSRB") in connection with its implementation of Section 975 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Proposed Rule G-42 is directed primarily at the standards of conduct and other duties and responsibilities of municipal advisors to their municipal entity or obligated person clients.

JPMC is a member of the American Bankers Association (the "ABA") and the Securities Industry and Financial Markets Association ("SIFMA"), both of which have submitted or will submit comment letters on Proposed Rule G-42. JPMC wishes to express its full support of the views expressed in such letters[1]. In particular, although JPMC supports and agrees with the MSRB's desire to provide more clarity to the statutory fiduciary duty and other duties or responsibilities that municipal advisors may owe to their municipal entity or obligated person clients, we share the ABA's and SIFMA's significant concerns about Proposed Rule G-42, including without limitation with respect to the absolute prohibition on all "principal transactions" and the MSRB's suggestion that it might consider expanding the municipal advisor's fiduciary duty to cover its dealings with obligated persons (which among other things we believe clearly conflicts with Congressional intent). We also have significant concerns over how various parts of proposed Rule G-42 appear to override the concept of a separately identifiable department or division of a bank and the existence of exemptions to municipal advisor registration for various types of bank and other activity. Finally, we believe that Proposed Rule G-42 effectively ignores the substantial protections already provided under other applicable laws with respect to bank fiduciary activity, creating a duplicative regulatory environment.

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[1] We would like to note that we did not have an opportunity to review the final version of the SIFMA letter before submitting this letter today. Our statements herein referring to comments and recommendations made in the SIFMA letter are based on the close-to-final draft which we reviewed. In the event such letter subsequently filed changes in any material respect, we may submit a supplement to this letter to address any such changes.

In addition to the foregoing, as the MSRB also knows there are significant interpretive issues concerning when a financial institution may inadvertently become a municipal advisor and, although the Securities and Exchange Commission has provided very helpful guidance in some areas, not all of those issues have been resolved (nor is it reasonable to assume that they all will be). Accordingly, JPMC expects that if the issues with Proposed Rule G-42 are not adequately addressed in the final rule, JPMC and many other financial institutions that currently provide products and services to municipal entity and obligated person clients will have to seriously consider which products or services they would continue to provide to such clients (in whole or in part) in light of the sizeable new risks and burdens imposed by Proposed Rule G-42.

In conclusion, JPMC supports the MSRB's desire to provide clarity on a municipal advisor's standards of conduct and other duties and responsibilities. However, JPMC urges the MSRB to consider carefully the concerns and issues raised by the ABA, SIFMA and in this letter, among others, in crafting a revised rule. JPMC would further urge that the MSRB release any such revised rule for another round of public review and comment before considering adoption of a final rule. Finally, we respectfully request that the MSRB, together with the SEC, consider providing guidance well in advance of the July 1, 2014, effective date for the SEC's final municipal advisor rules of how persons or entities that are expected to comply with those rules can effectively do so if Rule G-42 is not finalized in advance of that effective date.

Sincerely,

Paul N. Palmeri

Managing Director

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March 10, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Suite 600
Alexandria, VA 22314

Re: MSRB Notice 2014-01: Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

This letter is written in response to the request of the Municipal Securities Rulemaking Board (the "MSRB") in Regulatory Notice 2014-01 ("the "Notice) for comments on the draft MSRB Rule G-42 with respect to the standards of conduct and duties of non-solicitor municipal advisors (the "Proposed Rule"). The Proposed Rule sets forth suggested standards of conduct and duties of municipal advisors when engaging in advisory activities other than the undertaking of solicitations. We endorse the MSRB's broad request to solicit comments with respect to the Proposed Rule, and we offer our comments based on our firm's broad-based national municipal finance practice and the experience we have accumulated in our daily interactions with numerous municipal entities and municipal advisors, both large and small. We are not commenting as counsel to any client. We assume the initial breadth of the Proposed Rule will be followed by a revised rule which is reflective of both comments received and the practices and realities of the municipal finance world. We particularly note the Executive Order issued on January 18, 2011 by the President which states, inter alia, that each federal regulatory agency "must . . . tailor its regulations to impose the least burden on society, consistent with obtaining regulatory objectives . . . .", and that (as the Notice states) the Dodd-Frank Act provides that MSRB rules should not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities and obligated persons provided that there is a robust protection of investors against fraud.

The Notice contains many requests for comments, but we have restricted our comments to those requests for which we feel we have sufficient experience to respond appropriately. To facilitate our response to the MSRB's requests for comments, we have organized our comments by following the Notice and noting those pages of the Notice in which comments are requested and to which we are responding.

Page 6 (Top)

You ask whether a fiduciary duty of a municipal advisor should be expanded to include obligated persons under the MSRB's municipal issuer protection mandates. We would strongly suggest that a fiduciary duty should not be expanded to include obligated persons. The universe of obligated persons is quite broad, and generally includes larger and more sophisticated parties than the universe of municipal issuers, which includes tens of thousands of small relatively unsophisticated issuers which issue small amounts of bonds and often on only an infrequent basis. For example, the universe of obligated persons includes multinational corporations who are registered with the SEC, such as Exxon, Cargill, U.S. Steel, numerous privately owned utilities and the like – entities which are large and sufficiently knowledgeable to be aware of the capital markets, financing options and the roles of finance professionals. Clearly an advisor owes a duty of care to all its clients; however, the fiduciary duty is so much broader and all-encompassing that it would unnecessarily impede sophisticated broad-based advisors from interacting at all with sophisticated business organizations.

Page 13 (Top) (Also see page 16, #s 12 & 13)

The Notice asks whether it is appropriate to prohibit principal transactions by municipal advisors with their clients, even if the client consents. We believe such an absolute prohibition is inappropriate, and would advocate instead for a general prohibition with an exception where informed consent is obtained. There clearly are many municipalities that are sufficiently sophisticated to adequately assess principal transactions. Moreover, as noted above there are many large obligated parties who are similarly situated. It is clearly anomalous that the Proposed Rule would purport to protect New York City, the State of California, GE, Exxon or Berkshire Hathaway because they are deemed incapable of assessing a transaction with an entity which happens to technically be a "municipal advisor" to them. Especially if these financially sophisticated entities believe that their technical "advisor" offers them the best execution with respect to a transaction.

We believe that a municipal advisor should be permitted to engage in certain types of principal transactions with its clients, with full and fair disclosure informing written client consent. We think this is particularly true with respect to transactions involving securities or investments for which there is an established open market and for which a price is easily determined by the public. For example, it would seem to be overkill to prohibit a municipal advisor from selling Treasuries to its client, when there's clearly an established Treasury market and the client can readily ascertain the reasonableness and fairness of the price. Furthermore, we do not think this rule should differ based upon whether or not the municipal advisor has a fiduciary duty to the client. Rather, the rule should be based upon those concepts of fairness and full disclosure applicable to all activities of a municipal advisor.

Page 15 (#2)

We strongly believe that a municipal advisor should be permitted to limit the scope of its engagement with its client, as discussed below – consistent with the idea that the SEC municipal advisor rules are "activities" based, implying that there are multiple possible activities that an advisor could be providing. In particular, an advisor should be permitted to limit the scope of its engagement with respect to review of the official statement, and if agreed upon by the client it should not be required to review the official statement. Any limitation should be specifically spelled out in the contractual arrangement between the client and the municipal advisor. There are organizations which provide special types of limited advice which would make them a municipal advisor within the technical definition of that term, but the advice is limited to less than the full panoply of services included in the definition. For example, there are a number of cashflow consultants who provide computer cashflows to municipal issuers, and as part of that make suggestions to issuers about how they might structure more efficient bond issues or cashflows that depend upon bond issues. Arguably, the provision of that advice with respect to the bond issue would make them a municipal advisor. However, these consultants are not providing advice with respect to the timing of the bond issue, its legal or financial covenants or other matters. Such an advisor should be permitted to limit its engagement accordingly and, likewise, to limit its review of the official statement. The same thing could happen with respect to entities which provide feasibility studies in conjunction with a project being financed by a bond issue where the advice technically goes beyond the feasibility exemption, but which clearly does not go to the timing, financial structure or other provisions with respect to a bond issue, and thus it would be inappropriate to require them to review an entire official statement for matters beyond their scope of employment and expertise.

Page 16 (#8)

We do not believe that it is appropriate to require disclosure of legal and disciplinary events that relate to an individual employed by a municipal advisor if that person is not reasonably expected to be part of the advisor's team or working for the client in question. This would be a particular burden for larger municipal advisory firms, which may employ numerous, even hundreds, of people. If the individual in question is not part of the advisory team, query the relevance of such disclosure. Requiring such disclosure would seem to unnecessarily highlight those individuals, and in very large organizations may well simply produce a constant stream of information which will be disregarded (and may effectively bury information about team members). This would also seem to be in keeping with the exception of a material person associated with registered municipal advisors from registration under SEC Rule 15Ba1-3.

We would endorse the idea of having disciplinary histories and legal events disclosed through registration forms instead of directly to clients. We would strongly suggest that municipal advisors be required to inform clients in their written engagement agreement of how the client can access such information, thus leaving it up to the client to determine whether or not

it wishes to do so. Moreover, from a practical standpoint, and particularly for large municipal advisors who may have ongoing histories and numerous legal events to disclose, the requirement of continually disclosing such information to all clients would be time consuming and expensive. One also would question its value, for clients would probably quickly become inoculated to the information. Imagine what it would be like to be the city clerk for a small city who happens to have hired a large national municipal advisory firm and who receives an almost daily stream of such information.

Page 16 (#9)

We do not believe the MSRB should require professional liability insurance be carried by municipal advisors, nor specify the minimum amount in terms of such coverage. We do believe that in some cases it may be an appropriate question for an issuer to ask in an RFP process, just as on occasion such a question is asked with respect to lawyers or accountants, but we would note that it is extremely unusual for that question to be asked with respect to comparable financial entities such as broker-dealers or underwriters. Also, we would note that such liability insurance normally has numerous acts that are not covered so its true coverage (and value to the client) is not clear and often even ephemeral, and that such insurance is expensive. And, there is no doubt that the cost of such insurance would create a barrier to entry for potential municipal advisors, particularly small municipal advisors.

Moreover, the requirement that a municipal advisor disclose that it does not carry professional liability insurance creates a potential competitive advantage for those municipal advisors which either already have such insurance or have the resources to afford this insurance. While the Proposed Rule does not require the insurance, the requirement for disclosure regarding the status of this insurance may create an expectation from municipal entities that the absence of professional liability insurance is indicative of the qualifications of the municipal advisor. This creates a barrier to entry into the municipal advisor market not based on competence or level of service but rather upon the existing resources of the municipal advisor which may serve to drive out small municipal advisors contrary to the Dodd-Frank Act provision that the MSRB may not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities and obligated persons provided that there is a robust protection of investors against fraud.

And, in case the MSRB is not familiar with plaintiff class-action securities lawsuits, plaintiffs' firms regularly go to almost any length to determine whether a potential defendant carries liability insurance and the amount of the coverage, clearly targeting those that have insurance policies. Requiring professional liability insurance and specifying minimum coverage would be of minimal value to an issuer but of great value to plaintiffs' class-action lawyers and could well encourage expensive and often frivolous litigation involving both advisors and their clients.

Page 16 (#11)

In light of the fact that we believe a municipal advisor should be permitted to contractually limit its activities and services as an advisor, we think it inappropriate to require an advisor to review any feasibility study as part of the information considered in its evaluation of whether a transaction it recommends is suitable for the client. We are assuming that "suitability" is intended to be broadly read and cover all aspects of suitability for a client. If an advisor limits the nature of the advice it provides to an issuer, and the nature of that advice does not encompass the topic of a feasibility study, it seems entirely inappropriate to require an advisor to review the feasibility study with respect to any recommendation it makes. This is especially true if the advisor's expertise clearly does not encompass the topic of the feasibility study – in fact, in such a case the advisor should totally disclaim the value of any advice it provides. For example, a computer cash flow consultant "advisor" may know nothing about the feasibility of a proposed nuclear power plant or a low income housing tax credit project.

Page 25

The MSRB requests meaningful feedback regarding the potential economic impact of the Proposed Rule and amendments on small municipal advisors. In our practice, we routinely work with a number of very small municipal advisors, including some which are single-person organizations. Obviously, the Proposed Rule has not been fully implemented as yet, nor have all the administrative details been worked out. However, anecdotal evidence clearly indicates that this rule is going to impose a significant burden upon small municipal advisor organizations, and in fact will probably result in a substantial decrease in the number of such operations. The MSRB has recognized this natural result, and appears to be attempting to take steps to minimize the effect on small advisors. We heartily encourage the MSRB to continue to do so, as our experience is that in many geographic areas, particularly non-urban areas, small municipal advisors are the norm rather than the exception, and they provide personalized advice that cannot economically be provided at the same level by larger municipal advisors, particularly for municipal issuers who infrequently access the capital markets (that is, the small towns, villages and school districts which geographically populate a large part of our country). Again, anecdotal evidence is that the municipal entities which will ultimately suffer the most include the small municipal issuers, for they will no longer receive the kind of personalized economical advice that they are presently obtaining either from underwriters (due to the limitations on underwriters set forth in SEC Release No. 34-70462) or from small municipal advisors (that find the regulatory landscape too expensive to navigate). In fact, the overhang of the Proposed Rule is already beginning to have this effect.

Page 27 (#12)

To the extent that Rule G-42 establishes or clarifies standards of conduct and duties, it will certainly establish a floor for the same, which we believe is commendable. However, it may

also effectively establish a ceiling, which in some cases may lower the quality of services provided unless the MSRB is clear that these are minimal standards expected of municipal advisors and not general "industry standards."

Page 27 (#s 13, 14, 15 and 16)

It is highly likely that the additional cost imposed on municipal advisors by virtue of the MSRB rules will be passed on to municipal entities or obligated persons in the form of higher fees. To think otherwise is to ignore economic reality. This in turn will increase issuance costs for issuers. It will probably not lead to a concomitant reduction in the costs to the issuer for underwriters or other professionals, for the additional cost will largely relate to the administrative burdens imposed on municipal advisors and not reduce the expenses of other financial professionals or redound to the benefit of issuers. We do not believe the requirements of the Proposed Rule will affect the willingness of market participants to use municipal advisors and may indirectly encourage issuers to retain municipal advisors to enable them to utilize the municipal advisor exemption so underwriters can continue to provide a free flow of information to issuers; such free flow of information to issuers is otherwise clearly going to be inhibited by the municipal advisor rules. On an overall basis, anecdotal evidence at present would indicate that the Proposed Rule will probably result in less competition among municipal advisors (because there will clearly be fewer of them), may increase the efficiency and capital formation for large issuers but will substantially decrease efficiency and capital formation for the thousands of periodic small municipal issuers, and clearly will not decrease issuance costs. In fact, we are already seeing the issuance cost increases and inefficiencies in our daily practice involving small infrequent issuers.

Page 29 (Rule G-42(c)(i))

The requirement that the municipal advisor contract include an estimate of the reasonably expected compensation in dollars is cumbersome and such an estimate may be contingent upon too many factors to be of benefit to the parties. If the compensation under the municipal advisor contract has as a component a transaction-related fee, there is no way of knowing how often the municipal entity will issue debt and in what amounts so as to be able to accurately estimate the overall compensation due under the contract at the time the contract is executed. By including this requirement, the municipal advisor will either overestimate its fees and potentially run afoul of the Proposed Rule's restriction against excessive compensation or the municipal advisor will underestimate the compensation and will be left in the difficult position of explaining to its municipal client why its actual invoice for fees exceed the estimate included in the municipal advisor contract.

We would be pleased to discuss any of the foregoing comments in greater detail. Please feel free to contact me or my colleague, Josh Meyer, at (402) 346-6000.

Very truly yours,

John J. Wagner

LAMONT
Financial Services Corporation

March 10, 2014

Mr. Ronald Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Dear Mr. Smith,

Thank you for the opportunity to comment on the Proposed Rule G42, the Duties of Non-Solicitor Municipal Advisors. I appreciate that the Board thoughtfully considered the role of the municipal advisor with respect to its duties to issuer clients and the increased transparency that the rule should help foster. However, there are several aspects of the rule that are laced with probably incorrect assumptions and that may result in the Rule being less effective or more burdensome than desired. There are other aspects in which the Proposed Rule may have over-reached and may negatively affect the cost structure of the industry.

I believe that the municipal advisor industry accepts that they have a fiduciary duty, which includes both a duty of loyalty and a duty of care. However, in implementing these principals, like everything in life, the devil is in the details.

Recommendations. The proposed Rule has a flawed assumption that all municipal advisors would be making recommendations in nearly every instance regarding a municipal financial product or financing. For approximately half of Lamont's issuer clients, they do not seek a recommendation from their municipal advisor about whether to proceed with a transaction. They believe they are sufficiently capable of weighing the risks in a transaction and making their own decision about whether to proceed. These are large sophisticated issuers with multi-billion dollar debt portfolios. They want their municipal advisor to assist them in executing the transaction and helping them get the best price when the issue comes to market. Does this fact pattern suggest, for those clients who do not seek a recommendation from their municipal advisor, only a suitability review/determination is necessary from the municipal advisor? If the answer is in the affirmative, then this should be made explicit in the discussion of limiting the municipal advisor arrangement. If the answer is no, then the Rule will have the consequence of increasing the cost of compliance to the municipal advisor, which will in turn increase the cost to the issuer client.

The Rule will make work for the municipal advisor in order to comply with the requirements of the Rule. My fear is that if the issuer does not want the advisor to make a recommendation, the municipal advisor will be faced with a very difficult problem: the issuer will not want to pay the advisor to consider and paper over its work as though a recommendation to move forward was

made, even though a recommendation was not required, just to avoid a books and records examination problem by the SEC or FINRA. This could create a cost to the municipal advisor, since the client may refuse to pay for the compliance related cost.

Official Statement. In general, I agree with the premise that municipal advisors should thoroughly review an issuer's official statement to make sure that the official statement fairly presents the client to investors. This would especially be true for issuers that come to market infrequently, have had economic set-backs or are under any distress. This would also be true for obligated parties in a transaction, as they are the credit behind the issuer of the bonds. However, if the issuer has issued bonds multiple times in the course of a year, I would submit that an initial thorough review of the official statement in any year with a review of the changes in each subsequent issuance should be sufficient for the municipal advisor to discharge its duties. Further, if the issuer has competent disclosure counsel that it hired for multiple transactions, then a municipal advisor should be able to rely on competent disclosure counsel to provide accurate and full disclosure about the issuer and the transaction.

E&O Insurance Disclosure. While I believe that Errors and Omissions insurance should be required of all municipal advisors as part of their overall professional qualifications, it may create a barrier to entry in the municipal advisor business. However, before the Board explicitly requires such insurance, the Board should do research to thoroughly understand the coverage being provided. For example, very few carriers actually provide E&O insurance for practitioners in the municipal bond business. Some advisors carry E&O insurance designed for management consultants under the theory that they solely provide advice to municipal issuers, but do not have any other duties regarding the recommendation of municipal financial products. The cost differential may be five times or more for bond business coverage versus management consultant coverage. In addition, the policy limits are more restrictive for the bond business coverage. As a result of this disparity, unless or until the Board had satisfied itself as to which coverage was appropriate to address its concern over professional qualifications, I would not recommend that the Board take any position on what is sufficient coverage while ascertaining that such coverage would be generally available in the marketplace. We have seen numerous RFPs where an issuer has established insurance requirements that are not generally available to municipal advisors, and have to back-track on the requirements during the RFP process.

Affiliates. Lamont, like many municipal advisors that created investment advisory affiliates in order to comply with SEC rules regarding bidding escrows and similar matters for its municipal clients, has an affiliate that is staffed by persons who work at Lamont Financial Services (LFS) but are specifically licensed to work as an investment advisor. Some broker dealers who bid to provide such escrows require that Lamont Investment Advisors (LIA, registered with state regulators since it does not manage money) establish a brokerage agreement with them, where the BD places the securities versus payment until such time as the issuer's trustee settles the account with the broker dealer. We are concerned that while such practices would satisfy the

broker dealer, that under the Rule it would have the appearance of being a principal transaction while it is really an agent transaction.

In addition, we are concerned about the compensation disclosure requirements of the Rule. At Lamont, LIA does not pay commissions or referral fees to LFS personnel whose clients ask us to bid escrows, investments, or value swaps. However, for employee compensation, both LIA and LFS are treated as one pool. The distribution of such employee compensation would occur at the end of our fiscal year and would not be known and is not necessarily tied to the fees for which the affiliate actually did the work. Conflict of Interest disclosures related to this activity would, of necessity, be so general as to be virtually meaningless.

General Conflict Disclosures. True conflict disclosures, as opposed to conflicts regarding the method of payment, should be discussed at the outset of the relationship and signed off by the issuer official. Fee splitting and other similar arrangements are very problematic and should be prohibited. Payment of fees by a third party, such as an investment provider, should be fully disclosed as to the dollar value of the payment. . This approach benefits the issuer, since the fee is included in the yield on the investment, reducing any arbitrage payment to the IRS. Further, the permissible fees are limited by the IRS.

Payments by affiliates would represent a potential conflict and should be disclosed if the affiliate is engaged in a principal transaction or if it directly manages investments with authority to actively manage the investments

Conflict Disclosures Regarding Method of Payment. While I appreciate the need to provide disclosures regarding payments by third parties to the municipal advisor, providing the proposed disclosures regarding methods of compensation seems to run the risk of being so obvious as to insult the intelligence of the issuer official. All of Lamont's issuer clients actively manage their municipal advisor relationships as they are very cost conscious. For certain clients, who have multiple municipal advisors, the issuers are required to determine which advisor will do what task to avoid duplication of effort. The level of disclosure being proposed could be provided to issuers but should only be done based upon an analysis by the municipal advisor as to the level of sophistication of the client as an issuer and manager.

Protecting Issuers. In discussing the SEC definition and the Proposed Rule G42, the most common refrain I hear from Issuers large and small is that the SEC and MSRB's desire to protect issuers only makes more work for the Issuer. This may be because Lamont has mostly large and sophisticated clients. However, regarding the MA rules, it should be recognized by the Board that large and sophisticated issuers have devised their own approaches to interacting with underwriters and municipal advisors, and the Board should consider developing a sophisticated issuer exemption for those portions of the Rule that would not benefit sophisticated issuers. If the Board is unable to define a sophisticated issuer, the Board could allow the municipal advisor to make such a determination based upon his knowledge of his client in its suitability assessment.

Books and Records. While I clearly understand that much of the books and records requirement is necessary to establish that the advisor is following the Rule, there are a few aspects that are not particularly clear that could create substantial burdens on municipal advisors. For example, would it be MSRB's intent to have all emails and client records saved in the same folder in electronic media? This could represent expensive updates to our systems if this is required. Further, is it the intent of the Rule that municipal advisors save every presentation made by an underwriter to its MA client, or only the ones the issuer decides to go forward with? Would this also be true for RFP's? Lamont's clients regularly receive RFP's from underwriters that may be four or more inches thick. For some of our clients, we receive up to 50 proposals in an RFP cycle. This is a lost of paperwork to be stored.

Is the "saving of presentations" requirement to tie to underwriter recommendations that might be prompted by an IRMA letter? This could create a very large document management problem, since many of these pitch books and presentations come in paper versions only. Scanning these documents will also cause the municipal advisor to expend a lot of clerical time for little benefit and would be burdensome to municipal advisors both large and small.

Economic Justification. I believe that the Board took an "easy pass" on economic justification by taking a position that the SEC requires most of this in its rule making and the Board is just making clear what the duties and responsibilities would be for recordkeeping. While I agree that this is a baseline, the Board should not approach this as a shelter from engaging in further econo9mic analysis. Some of the administrative requirements are all part of running an advisory business, such as contracts, engagement letters, and retention of files and emails. However, based upon the issues outlined above, I can easily imagine that the paperwork associated with the Rule could take 20-25 percent of an advisor's time to complete, some of it against the client's wishes. In addition, as discussed above, the costs associated with professional liability policies vary greatly based upon the type of coverage being provided.

I believe that the effect of the SEC definitions and the Rule will be that over time, a substantial number of small firms will find it difficult to comply with the requirements and seek to merge with larger or better equipped partners. It would not surprise me to see that the headcount of the industry will be relative constant, but that the number of reporting firms will decline by 20%.

I do not agree with the view that compliance costs will be spread amongst all of a firm's clients and should not raise the cost of doing business or the cost to issuers. The cost of compliance with the Rule is mostly going to be in the daily cost of documentation the MA's review of presentation by underwriters, considering and documenting alternatives, and the requirement to develop recommendations in writing to our clients, all in preparation for an eventual examination by the SEC or FINRA. This is not a small task. The problem for MA's is that their clients may not find the notion of documenting all these facts helpful to getting the transaction done, and will not appreciate the effort to comply with the Rule. As a result, they may not be willing to pay for this, and the MA may have to eat it as an expense. Given the small margins in the MA business,

a 20% loss of productivity can be debilitating to a MA firm in the short-term, before prices can be adjusted by the MA and the client.

Answers to Questions

Q1. Should the fiduciary standard apply to all of a municipal advisor's clients? Yes for its municipal advisory activities. However, we think that the Dodd Frank standard is appropriate, especially since certain municipal advisors are being hired in cases of municipal distress. In such cases, the municipal advisory firm may not represent the municipal entity or the obligated party, but may represent other creditors.

Q2. Should the advisor thoroughly review the entire official statement? As discussed above, this is a case-by-case issue, and depends upon how often the issuer is in the market, disclosure counsel, etc.

Q3. At the outset of a transaction, the issuer client is usually asking questions regarding what resources it will need to complete the transaction. I don't really think the Rule will serve to foster this in any material way.

Q4. I think that the disclosure of conflicts related to compensation sends a message to the issuer official that they are not competent.

Q5. To be clear, I am not in favor of fee splitting. However, allowing an investment provider to pay fees related to the solicitation of the investment by the municipal advisor, and which is within the permitted limits of the IRS rules, should be acceptable so long as it is disclosed to the issuer and to each investment provider on the bid list.

Q6. True conflicts should be disclosed at the outset of the relationship or during contract development.

Q7. Yes, which could be done in an email, in the engagement letter, or in a contract with the issuer?

Q8. I believe that if the offending individual has been terminated from the firm, then such disclosure of past events is less than useful unless there was also a finding of supervisory weaknesses. If the individual is still at the firm, then disclosure is required.

Q9. As stated above, E&O insurance should be a professional qualification. I would suggest that the MSRB be quite careful in making this a requirement, as discussed above. Before requiring such insurance, the Board should determine that there are sufficient providers and the average cost of a policy that covers practitioners in the municipal advisor business that work on transactions is commercially reasonable.

Q10. It may become a barrier to entry to small firms who provide MA services on less than a full time basis.

Q11. This question is too general to answer in the affirmative. I think that the municipal advisor should review documents that support the credit structure of the bond issue. In most circumstances, the municipal advisor will be involved in all aspect of the transaction, and so would have reviewed the documents and may have provided comments to the documents. However, depending upon when the municipal advisor is engaged, the balance of the financing team may have already thoroughly vetted the feasibility document. In some cases, the municipal advisor is the last to be hired, and in such circumstances is generally hired to supervise the pricing of the transaction. It is difficult to write rules that govern all circumstances, since situations vary so much.

Q12 and Q13. I don't think that the MA rule should conflict with dealer rules regarding principal transactions, recognizing that a fiduciary duty to the issuer will require additional verification steps to ensure that the pricing has been at least as good as having a third party in the transaction. The MA who is acting as a principal should provide the issuer with a third party data source to verify the pricing of investments or municipal financial products. Failing that, the MA should offer to bring in a third party verification of the pricing from firms for which it does not engage in active trading relationships.

Closing Comment

I believe that the Rule addresses issues related to fiduciary duty and suitability, and does a good job at providing insight about the issues that MAs must address and procedures for demonstrating compliance with the Rule. Further, I think the MA industry should be regulated, provided that we can find ways to make it less burdensome.

Portions of the Rule should have further review by the Board to insure that the number of unintended consequences can be minimized.

Thank you for the opportunity to provide my comments on the Proposed Rule G-42.

Yours truly,

Robert A. Lamb
President

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LEWIS YOUNG
ROBERTSON & BURNINGHAM, INC.
AN INDEPENDENT MUNICIPAL FINANCIAL ADVISORY
AND CONSULTING FIRM

March 3, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: MSRB Notice 2014-01, Request for Comment on Draft MSRB Rule G-42

Ladies and Gentlemen:

Lewis Young Robertson & Burningham ("LYRB") is pleased to submit comments on the above-referenced Notice.

LYRB is an independent financial advisory firm which has elected, since its inception 18 years ago, to be regulated as a broker dealer and, therefore, has been and remains subject to MSRB regulations. We are now also registered as a municipal advisor with the Securities and Exchange Commission and the MSRB pursuant to Rule 15Ba2-6T of the Commission. We have a staff of 21 and currently carry liability insurance.

LYRB does not underwrite or purchase securities for our own account or for sale to others nor do we carry customer accounts of any kind. We do not participate as a co-manager or member of selling groups and do not act as a remarketing agent. We are a major financial advisor in the State of Utah and work in some other states as well. LYRB has acted as a financial advisor on hundreds of transactions with a volume of over $7 billion. These transactions run the gamut from small to large, and include general obligation bonds, various types of revenue and tax backed bonds, revenue and bond anticipation notes, and taxable and tax-exempt (including Build America Bonds) bonds in both fixed rate and variable rate structures.

Proposed Rule G-42 generally covers the subject matter of Proposed Rule G-36, which was later withdrawn. We commented on that proposal in a letter to you dated April 11, 2011. While the Proposed Rule G-42 represents an improvement in several respects over the draft G-36, we nevertheless have several comments and concerns. We also address some of the questions set out in the notice. We first address the Questions under "General Matters" set out in notice 2014-01. Our numbered responses correspond to the items set forth in the Notice.

1) The rule is satisfactory as it stands. While we would likely apply a fiduciary standard to ourselves in advising obligated persons, we see no reason for the MSRB to go beyond the statutory mandate and possibly invite litigation.

2) While it is obvious to anyone with extensive experience in the municipal bond business that, among all transaction participants, each official statement needs a "thorough review," we object to the statements relating to review of official statements appearing in

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the second half of .01 Supplementary Material, which addresses this matter and to the specificity of proposed Rule G-42(b)(v). Our objections are manifold. First and foremost, the imposition of a "thorough review" default standard on one transaction participant, the financial advisor, in a situation which is highly variable, not only from client to client, but from transaction to transaction, is unwise at best. While the rule allows departures, documenting the deviations from the "default" standard will be the rule, not the exception, and will be time consuming for both the advisor and the client for no gain in utility. To illustrate, one of our clients issues, from time to time, general obligation bonds, lease revenue bonds, water and sewer revenue bonds, redevelopment agency (tax increment) bonds, sales and excise tax revenue bonds, and assessment bonds, as well as refunding bonds of each of these types. The focus and scope of our work on the respective official statements will depend on such factors as: How long it has been since the last public offering of that credit, is there disclosure counsel, and how much overlap of information is there in, say, a current lease revenue bond compared to a recent general obligation bond, among many others. The scope of review of the official statement by the financial advisor in each case will vary. Typically, we will review the transactional details very carefully, leaving legal details, document summaries and litigation matters primarily to lawyers and the issuer's financial and operational matters primarily to its own staff with more general or overview work from our office. If we are required to "thoroughly review" all of an official statement we will be duplicating effort and unnecessarily generating increased costs (to the irritation and disadvantage of our client). If we must carefully adjust and document our review standard and scope in each case we will take our client's time and our own unnecessarily. Second, as rational participants in the disclosure process, we work to have various parts of the official statement reviewed by those professionals or issuer staff members most competent to do so. This will often not be the advisor. Third, it is unclear what "thoroughly review" means. If it includes the common sense meaning, it will require much unnecessary duplication of effort in many cases in a process which is already (and necessarily) time consuming and exacting. The review of an official statement is necessarily a flexible and dynamic process that must be tailored to the specific circumstances of each bond offering. The initial review may identify topics where additional disclosure is necessary, which in turn results in further review and discussion between the advisor and its client. A "thorough review" default standard is overly simplistic and misleading.

We recommend the rule be silent on this point, leaving to the issuer and its advisors to apportion the necessary work among its various staff members, attorneys, auditors, and the financial advisor as each case appears. This approach is consistent with an advisor's fiduciary duty to assist an issuer (if engaged to do so) with its official statement(s) by seeing that an issuer is well advised (or staffed) to cover the various aspects of the official statement and that the proper subject matters are addressed, regardless of which employees or professionals actually do the detailed work. The vast majority of the professionals filling these roles know what to do and how to do it.

3) No, these should not be required to be written. We typically agree to assist the issuer and its counsel in preparing the official statement, leaving the scope of assistance to a case by case determination as needed. A detailed documentation of the adjustments in these

responsibilities is unnecessary. In any event, the participants in the preparation process know what is needed (or in the case of an unsophisticated or occasional issuer, can be more intensely guided on these matters). There is no need to document these allocations and doing so would unnecessarily add time and expense to each transaction.

4) This is unnecessary and should be deleted. Advisors rarely, if ever, work on an uncompensated basis. Some form of compensation would, if we are to believe the underlying premise of this proposed regulation, call for "conflicts" disclosure. A broader issue was raised by the detailed compensation conflicts disclosure under Proposed Rule G-36, since withdrawn. In the "real world" many if not most advisors' engagements are based on contingent fees. The proposed baseline compensation conflict disclosure would probably result in a disclosure statement to the effect that this may give the advisor an incentive to recommend that the client execute a transaction that was not in its best interest. This amounts to saying that the mere fact of being paid gives the advisor an incentive to breach its fiduciary duty, which would seem to accomplish nothing other than confusing the client. This is a solution in search of a problem.

5) Fee splitting arrangements should be fully disclosed but not prohibited. One example of an occasional situation calling for application of this rule would be fee-splitting with a structuring agent that was engaged to provide specific quantitative services on a transaction. Prohibition would be against the client's interests in such issues.

6) This matter is complex due to the wide ranging possible fact patterns. Requirements to disclose prior to inception of the agreement will often be unreasonable in that a newly retained advisor may not be familiar enough with the client's affairs to perceive the potential conflict.

   In addition, in the case of an engagement for a time, most conflicts will arise during the course of the engagement. For example, advisor A works for City B and City C, both of whom wish to attract manufacturer D to their city, for economic development reasons. If one, or both of these cities wishes assistance from A, she will need to disclose the conflict. If both parties agree, she then may need to limit her work to confidential analyses. Any situation in which negotiation assistance is called for on both sides would be untenable, but full disclosure and appropriate waivers should enable analytic work. Timely disclosure of and resolution of conflicts, if possible, as they arise should be the rule. For these reasons, conflict disclosure should be limited to actual conflicts. Potential conflicts should either not be covered, or be addressed generically with more specific disclosure required when they actually arise. Tailored explanations directed to potential or hypothetical situations will be expensive, time consuming, and not very helpful. Actual conflict resolution is best handled by discussion between advisor and client, rather than by additional or hypothetical disclosure.

7) No. Municipal advisors should not be required to obtain a written acknowledgment for disclosures before proceeding with the engagement, so long as the disclosures are provided and not objected to.

8) No. The bigger issue under proposed G-42(b)(ix) is whether advisors should be required to disclose a legal or disciplinary event that was already disclosed in the most recent Forms MA or MA-I. These are already public information. Perhaps the MSRB could require that the advisor provide a generic statement directing the client to the appropriate websites if it wants to view this information.

9) No.

10) It may be. Even if it is not currently, what are now reasonable premiums and coverage limits may change. Smaller firms may be driven from the market if they find they cannot afford coverage or if coverage limits rise to a level small firms cannot afford. Insurance should be left to the economic interest of the firm, as it is with attorneys. Further, insurance should be disclosed only when requested. Rule 42(b)(viii) should be deleted.

11) This should be left to the parties to decide.

12) Never. One cannot be both a fiduciary and principal party in a buyer/seller relationship if the subject of the sale is an asset, financial product, or something other than services compatible with the fiduciary role.

13) This seems fine, so long as a party cannot step into and out of a fiduciary relationship in a facile way.

Comments of 42(b)

We have largely addressed G-42(b) in the foregoing Q&A responses. However, we note that the final sentence of 42(b) is problematic. It is subject to all the logical problems of proving a negative. In addition, it could be confusing if an unknown or potential conflict either comes to light or becomes an actual conflict. For example; If advisor A has client B and is then hired by client C, then later the interests of B & C on a matter A is expected to advise them on come into conflict, a statement that there are no conflicts is true when C hires A, then ceases to be true when the conflict arises. It seems much better to disclose and address the conflict when it arises, rather than to make generic and hypothetical disclosures which then must be modified.

Comments on 42(c)

In general, (c)(i)(iv), and (vi) are always covered by written agreement between our firm and our clients. With respect to (ii), the proposed rule seems vague. This duplicates (i) or calls for a precision in the face of uncertainty (for example, does this require if a fee is based on dollars per $1000 issued, that estimates be given based on hypothetical sizes? If so, this requirement is unnecessary, adding no useful information for a client). (ii) Should be deleted. With respect to (c)(iii), known conflicts can and should be disclosed at the relations formation state (see response to Question 6 above).
With respect to (c)(v), see response to Question 2 above. A general description of this work should be included in the material called for, and under (c)(iv). However, it is unnecessary to cover this in detail in writing for multiple issue engagements. (c)(v) is superfluous and should be deleted.

Comments on 42(d)

The premise of this section is based upon a flawed assumption, i.e., that recommendations are made in all cases. In a long term client relationship, the advisor does make recommendations from time to time on his own initiative. This will be more common in the case of refunding transactions. However, the mine run case is that the client calls the advisor with a project in mind. This might be anything from an entirely new credit creation to step five of a multi-phase general obligation financed construction program stretching over years. The client will often have a financing vehicle in mind. In such cases, it will not make any sense to go over the risks and benefits of a particular structure or product either because it has already been done, because there is no other option, or because other available options are obviously inferior or disfavored by policy or circumstance. Discussion will often be a waste of time in these circumstances. Documenting such a discussion so as to have a "good answer" for the next regulatory audit would be even more a waste of time and resources.

There are, of course, many times where detailed discussions of a novel (to the client) financing mechanism, a financial "product" or a situation in which several possibilities for accomplishing the financing are available which would call for detailed discussion. There is no need to mandate the discussion in such cases, as it is covered by 42(a)(i). 42(d) should be deleted.

Comments on 42 (e)

This rule is unnecessary, as it is covered by 42(a)(i) and is a basic part of a generally engaged financial advisor's work.

Comments on 42(g)

The prohibition in 42(g)(i) is evaluated by what standard? There is no standard or set of standards which could rationally be applied. By its very nature a "price" is designed to encompass a vast amount of information (all of which is relevant). The market is all the discipline needed here.

Supplementary Material.

In addition to the comments on .01 given above with respect to official statement review, we note that .05 implies a level of disclosure on conflicts of interest such that only material conflicts should be disclosed rather than potential hypothetical conflicts. See our response to Question 6, above. Presumably, only potential conflicts which could affect A's judgment and full representation should be disclosed at the onset, leaving further disclosure to the change of circumstances. At the point it arises the conflict would be dealt with by several means, after full disclosure. Any requirement to disclose this at inception would entail multiple hypotheticals so voluminous as to be impossible.

Economic Analysis

We have several comments on economic analysis issues raised by the Notice and by the text of the Proposed Rule.

In general, we believe the increased oversight of the municipal advisor market represented by the core concept of the Dodd-Frank Act applicable to municipal advisors, in conjunction with the SEC rules defining municipal advisor and Rules G-17 and G-23 will assist

in capital formation and lower costs to municipal issuers generally in the form of better structure and lower interest costs. That said, several aspects of the proposed Rule G-42 unnecessarily increase costs and potentially burden smaller service providers, to the detriment of the overall potential positive effects mentioned above. For best results, MSRB must carefully consider the effect of the rules on the availability and cost of financial advisor services to all municipal entities, but especially small, mid-size and infrequent issuers. We note that these entities are likely to receive less coverage from broker-dealers. While this has many positive effects in protecting such issuers from self-interested presentations from non-fiduciary professionals, it points up a need for fiduciary advice. If anyone is going to pay continuing attention to them (e.g., pointing out savings refunding opportunities) it will and should be their Financial Advisor (if they have one). Rule G-42 should enable and facilitate longer-term Financial Advisory engagements. All aspects of the rule need a robust cost-benefit analysis to ensure that the costs imposed on advisors (which will be passed through to their clients) are justified by substantial and demonstrable benefits. It is also fair to observe that the cost-benefit analysis included with Proposed Rule G-42 is superficial and conclusionary.

More specifically, problematic cost increases we have identified include: (depending on how "potential" is ultimately interpreted under G-42 (b)(i)), excessive hypothetical speculation as to potential rather than actual conflicts of interest may require burdensome and ongoing drafting which will waste time and resources, confuse the client and generally add no value to a client's decision making.

G-42(b)(v) adds no value and should be deleted.

G-42(b)(viii) gives too much weight to insurance. See our discussion above. Over time, this may adversely affect the number of smaller firms offering services. The decision to carry insurance and its disclosure should be left to the advisory firm. Clients who require insurance currently request this information.

Rule G-42(b)(ix) should be limited to the item in clause (a). Clients who want the other material will ask for it.

Rule G-42(d) and (e) require excessive record keeping associated with "defensive" documentation in order to show compliance.

Rule G-42 (g)(i) should be deleted. It seems completely unworkable—there's no way to tell where the line is drawn. This could well lead to meaningless defensive paperwork for advisors to document all of their work—a $250,000 FA fee could appear excessive for a $10M deal, but not if it involved a new credit and three years of work. This is best left to market forces and a general fiduciary standard.

One of the unnecessary cost burdens imposed by the draft rule is found in the thoroughly review standard in .01 of the Supplement relating to Official Statements. This standard will usually need to be modified. The necessity of documenting this, probably in the case of each issue, will require far more time and energy than it is worth.

The overall effect of excessive documentation, record keeping and "defensive" record keeping will be to increase costs, across the board, but disproportionately so to smaller firms. This will result in increased service fees and, on the margins, less competition which will also increase service fees. The gains provided by the general tenor of the proposed Rule for the overall municipal bond market need not be diminished by these effects if the Rule text is modified as we suggest throughout our comments. As a medium size firm, some of that might work to our advantage in the event smaller competitors are forced out, but it is not in the best interests of the purposes of Dodd Frank.

Additional/Big Picture Comments:

One final thought, an orderly transition provision or phased effective date is necessary. Many Financial Advisory engagements are longer-term arrangements and advisors should be provided with a reasonable opportunity to conform existing agreements to the requirements of G-42 when they are renewed or after a reasonable phase-in period after G-42 is approved by the SEC.

Lewis Young Robertson & Burningham, Inc.

By: Laura D. Lewis

Principal

MSA PROFESSIONAL SERVICES
TRANSPORTATION • MUNICIPAL
DEVELOPMENT • ENVIRONMENTAL

March 10, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 223 14

Re: MSA Professional Services, Inc. Comments on Draft Rule G-42

Dear Mr. Smith:

On behalf of the MSA Professional Services, Inc. – a Midwest leader in engineering, architectural, transportation and planning services for municipalities - I appreciate the opportunity to comment on the Municipal Securities Rulemaking Board's (MSRB) draft Rule G-42, regarding the duties of non-solicitor municipal advisors.

MSA would appreciate direction and clarification from the MSRB on the following topics as we proceed with drafting internal and external policy frameworks to achieve and sustain compliance with Municipal Advisor (MA) provisions contained within Dodd-Frank. While Dodd-Frank provisions draw a large swath across numerous professional services previously unregulated by the Securities and Exchange Commission (SEC) and MSRB, it fails to clearly state, define or demonstrate the intended level of analysis and due diligence expected of regulated MAs.

Suitability Analysis Required for Recommendations

"Draft Rule G-42 subjects municipal advisors to a duty of care in the conduct of their municipal advisory activities. In addition, draft Rule G-42 requires municipal advisors to disclose conflicts of interest and certain other information to their clients and document their municipal advisory relationship. Draft Rule G-42 does not permit a municipal advisor to recommend that a client enter into any municipal securities transaction or municipal financial product unless the advisor *has a reasonable basis for believing that the transaction or product is suitable for the client."*

- What specific metrics (standard debt issuance options) should be used to determine suitability?
    - Local bank financing
    - State Revolving Loan Fund (SRF) or equivalent
    - State Trust Fund or equivalent
    - USDA Rural Development

- Open bond market

- Will there be standards set for this quantitative review or will it be the responsibility of the individual MA to define the suitability metrics based on the unique circumstances of each client or project?

Documentation of the Municipal Advisory Relationship
"Under draft Rule G-42(c), municipal advisors must evidence each of their municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship."

- Can adherence to this rule be accomplished through contract (Master Services or Professional Services Agreement) or does this need to be done on an individual MA activity to MA activity basis?

Specifically, the Act itself sates that "Engineers may provide advice beyond engineering advice when such an independent registered municipal advisor is present without triggering the requirement to register as a municipal advisor."

- Can an engineering firm, under contract, mitigate the inherent MA responsibilities outlined if the municipality, in writing, releases the firm from the MA role?

- Can such a release be made based upon the municipality's ***intent*** to engage an MA at a later date, or does the engagement need to be in place in order for the engineer to be exempted from the MA responsibilities?

- If the contracted MA is not physically "present" when advice and/or services identified as within the realm of MA responsibilities is discussed with the community, is the engineer in breach of the MA provisions?

- Once a community releases a firm from the duties of the MA role, who is ultimately responsible to ensure that the MA protections of the client are enforced?

Limited Scope for MA Duties
"Supplementary Material .04 provides that a municipal advisor and its client may limit the scope of the municipal advisory relationship to certain specified activities or services. The municipal advisor, however, is not permitted to alter the standards of conduct or duties imposed by the draft rule with respect to that limited scope."

- Can adherence to this rule be accomplished through contract (Master Services or

Professional Services Agreement) or does this need to be done on an individual MA activity to MA activity basis?

- For communities that pursue multiple annual projects with an engineering firm through a Master Services Agreement, can the community elect to exempt the firm from the MA role on an annual basis through contract?

- How should this be handled by both parties if some of the annual engagement is in need of MA compliance and some is exempted?

Recommendations

"Section (d) provides that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product *unless the advisor has a reasonable basis for believing that the transaction or product is suitable for the client.* The advisor also is required to discuss with its client its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the advisor reasonably believes the recommended transaction or product is suitable for the client and whether the municipal advisor has investigated or considered other reasonably feasible alternatives. With respect to a municipal entity client, the advisor must only recommend a transaction or product that is in the municipal entity client's best interest."

- Can this information and recommendation be transmitted to the client orally or will each alternative require empirical evidence demonstrating the material risks, potential benefits, structure and characteristics? If oral transmission is acceptable, does said discussion need to be documented by both parties?

- Please define "client's best interest".
  - Is this to be inferred as the lowest overall cost?
  - Least subject to market volatility?
  - Most stability in terms of guaranteed interest rate over the life of the loan (vs. speculative balloon financing or bond re-issuance)?
  - Will the MSRB be drafting a suitability matrix to more clearly define "best interest"?

Review of Recommendations of Other Parties

"Section (e) addresses situations when a municipal advisor may be asked to evaluate a recommendation made to its client by another party, such as a recommendation by an underwriter to an obligated party of a new financial product or financing structure."

- Prior to said review, will it be necessary to have documentation regarding the other parties' MA dealings, recommendations and contracts with the client?

- It would seem rational and necessary to require the other party to disclose any and all documentation used in the recommendation for this analysis and review. Would this best be accomplished through the client or directly between MAs?

Specified Prohibitions
"Draft Rule G-42(g) specifically prohibits certain types of activities by a municipal advisor, including: receiving excessive compensation; delivering an invoice for fees or expenses that does not accurately reflect the municipal advisory activities actually performed or the personnel that actually performed those services; misrepresenting its capacity, resources and knowledge in response to requests for proposals or qualifications or in oral presentations to a client or prospective client."

- "Excessive compensation" – please define a metric to determine excessive compensation as multipliers, engineering and professional services costs vary tremendously by geographic region, firm, and overall scope of services.

Questions Identified in G-42 Correspondence:
1) Do commenters agree or disagree that a need exists for the MSRB to articulate the duties of municipal advisors or to prescribe means of preventing breaches of a municipal advisor's fiduciary duty to its municipal entity clients? If so, do commenters agree or disagree that the draft rule addresses those needs?

While the Draft Rule identifies the areas of concern and resultant compliance required to protect and preserve a fiduciary duty related to MAs, it fails to clearly articulate the specific mechanisms to achieve said compliance. For example, it identifies that policies and procedures need to be in place for MA compliance yet that requirement is not underscored with an identifying traits, qualifications or specific standards which outline the types of policies and procedures that will be acceptable by the MSRB for compliance.

2) The MSRB proposes to use the fiduciary duty already imposed on municipal advisors by the Dodd-Frank Act to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for municipal entity clients. Is this an appropriate baseline?

No. The 2010 Dodd-Frank Act has, in effect, been in place for 3+ years, the enforceable

portions related to fiduciary duties and MA rules and responsibilities is brand new. In fact, to date, I would not suppose many existing or "to be classified as" MAs have spent much in the wake of hard economic dollars on compliance strategies, policies, procedures or protocols. I assume there will be whirlwind of compliance activity prior to the July 1, 2014 permanent registration phase-in date as MA firms prepare for compliance activities beginning in the new fiscal year (once the rules become enforceable). Using compliance with 2010 Dodd-Frank Act fiduciary duty provisions as the baseline for determining economic impact related to MA compliance would not be a fair comparison for determination as the level of firm activity required for MA compliance will be increasing in future months with enforceability and compliance provision engagements.

3) The MSRB proposes to use the fair-dealing requirements under MSRB Rule G-17 to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct and duties for municipal advisors when engaging in municipal advisory activities for obligated persons. Is this an appropriate baseline?

Yes.

4) The MSRB proposes to use the Dodd-Frank Act's prohibition on municipal advisors from engaging in any fraudulent, deceptive, or manipulative act or practice in connection with advising a client to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct for municipal advisors (regardless of whether the client is a municipal entity or obligated person). Is this an appropriate baseline?

Yes.

5) The MSRB proposes to use the existing requirements for dealers who act as financial advisors to issuers with respect to the issuance of municipal securities to serve as a baseline for evaluating the economic impact of the draft rule's articulation of standards of conduct and duties for this subset of municipal advisors. Is this an appropriate baseline?

No Comment.

6) The MSRB proposes to use the required disclosures in registration forms of certain disciplinary history and legal events contained in the SEC Final Rule to serve as a baseline for evaluating the economic impact of the draft rule's disclosure requirements. Is this an appropriate baseline?

No Comment.

7) The MSRB proposes to use the recordkeeping and record preservation requirements contained in the SEC Final Rule to serve as a baseline for evaluating the economic impact of the draft rule's recordkeeping and record preservation requirements. Is this an appropriate baseline?

Yes.

8) In addition to the baselines proposed above, are there other relevant baselines that the MSRB should consider?

No Comment.

9) Please compare the costs and benefits of having disciplinary histories and legal events disclosed through registration forms versus disclosure directly to the client.

No Comment.

10) Are there lower-cost alternatives to requiring disclosure of the amount of professional liability coverage carried by the municipal advisor that would provide comparable benefits to clients of municipal advisors?

No. Direct professional liability coverage disclosure can easily be integrated into existing disclosure documents for transmittal to clients.

11) Would additional benefits accrue if the MSRB were to impose different or additional recordkeeping requirements and, if so, what would these requirements entail?

No.

12) To the extent that draft Rule G-42 establishes new, or clarifies existing, standards of conduct and duties for municipal advisors, will this cause a change in the quality of advice offered by municipal advisors?

Potentially. Our main concern is that with the additional MA responsibilities imposed, the "message" relayed to municipalities might be that only traditional financial services firms have the authority or ability to provide quantitative and qualitative analysis of various debt service and municipal financing mechanisms related to municipal projects or have the ability to assist in developing feasible alternatives for project funding. This may reduce the overall quality of recommendations. Furthermore, for firms that refuse

to register, the new regulations may prevent candid conversations with communities regarding rate studies, economic development options, etc. that are usually critical to success at early stages of project planning.

13) To the extent that draft Rule G-42 and the draft amendments to Rules G-8 and G-9 impose costs on municipal advisors, will these costs be passed on to municipal entities or obligated persons in the form of higher fees?

Yes. Any cost for compliance re: MA duties and responsibilities will result in higher fees for municipal entities. The evaluation and transmission of information that would now be considered within the realm of MA activities has been traditionally billed as services rendered. Now, however, with the new recordkeeping and compliance requirements, firms will find a way to re-coup, if not all, a significant portion, or this value-added service to clients, driving up the ultimate cost for municipal projects and, ultimately, municipal services.

14) To the extent that the requirements of draft Rule G-42 enhance the oversight of municipal advisors, will this affect the willingness of market participants to use municipal advisors?

Some municipalities may determine that it is cost-prohibitive to use MAs to the extent outlined in Dodd-Frank. This may have the detrimental impact of diluting the quality of information used in the pre-planning and project stages of municipal work.

15) To the extent that the requirements of draft Rule G-42 enhance the oversight of municipal advisors, will this lead to different issuance costs and financing terms for issuers?

Yes, as the overhead and maintenance costs required for MA compliance will be rolled into the overall debt issuance cost equation.

16) To the extent that the requirements of draft Rule G-42 lead to reduced issuance costs and better financing terms for issuers, will this improve capital formation?

We do not agree that provisions outlined in G-42 will lead to reduced issuance costs.

17) Would the requirements of draft Rule G-42 assist municipal entities or obligated persons in making hiring decisions with respect to municipal advisors?

Yes. Clear documentation of MA experience, qualifications and disclosure will improve transparency for the solicitation of MA activities.

18) What are the initial and ongoing costs associated with making and preserving the additional records required by the draft amendments to Rules G-8 and G-9?

Records preservation costs appear to be negligible. The primary increase in costs will be in achieving a compliance program and the related documents needed to maintain compliance on a project-to-project and client-to-client basis. Firms will find a way to include up-front and on-going MA compliance costs as a component of billable projects that contain Municipal Advisor compliance requirements.

19) Are there additional costs or benefits to recordkeeping that the MSRB should consider? If so, please explain.

No.

20) If the draft rule is adopted, what are the likely effects on competition, efficiency and capital formation?

No Comment.

21) How will the requirements of draft Rule G-42 affect potential municipal advisors' decisions with respect to entry into the market?

The systematic approach required for an acceptable and sustainable MSRB MA Compliance program may prevent entry into the MA market and may, in fact, consolidate the existing market accordingly. A firm who wishes to achieve and maintain compliance must have the appropriate administrative, legal, accounting and supervisory systems in place, upon which an appropriate compliance platform can be achieved. These upfront costs may deem MA activities as cost-prohibitive for smaller firms and prevent entry for some market participants.

22) What training costs would the requirements of draft Rule G-42 cause at municipal advisory firms to ensure compliance?

Without the appropriate level of direction from MSRB re: up-front certification requirements, appropriate number of individuals required for compliance review purposes, continuing education requirements, etc., it would infeasible to determine a training cost at this time. It is impractical to determine the potential cost of training when the specific training requirements have not been spelled out by the MSRB.

23) Will draft Rule G-42 have benefits in terms of protecting municipal entities, obligated persons and investors?

No Comment.

24) Will the requirements of draft Rule G-42 impose any burden on small municipal advisors that is not necessary or appropriate?

Small municipal advisors may be driven from the marketplace as it may become economically infeasible to achieve compliance without an economy of scale to help absorb initial overhead costs for policy and procedure creation and implementation.

25) Will the requirements of draft Rule G-42 create advantages for large municipal advisor firms relative to smaller municipal advisor firms?

Yes.

MSA appreciates the opportunity to provide comment on the draft Rule G-42 and would appreciate any direction the MSRB could provide on the above questions and comments that will help facilitate a smooth transition in the A & E industry to adopt the appropriate Municipal Advisor compliance policies, protocols and procedures.

Gilbert A. Hantzsch, P.E.
CEO, MSA Professional Services

National Association
of Bond Lawyers

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March 18, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

RE: NABL Comments on MSRB Notice 2014-01 (January 9, 2014)
Request for Comments on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

The National Association of Bond Lawyers ("**NABL**") respectfully submits the enclosed response to the Municipal Securities Rulemaking Board's ("**MSRB**") solicitation of comments on MSRB Notice 2014-01 related to draft MSRB Rule G-42 and Supplementary Material to the draft rule (the "**Notice")**. The comments were prepared by an ad hoc subcommittee of the NABL Securities Law and Disclosure Committee comprising those individuals listed on Exhibit A and were approved by the NABL Board of Directors.

In the Notice, the MSRB requests comments regarding specific questions posed by the MSRB and NABL has provided comments in response to certain of those questions. In addition, NABL is providing general comments on the draft rule and comments on specific aspects of the draft rule.

NABL exists to promote the integrity of the municipal securities market by advancing the understanding of and compliance with the law affecting public finance. A professional association incorporated in 1979, NABL has approximately 2,700 members and is headquartered in Washington, DC.

If you have any questions concerning the comments, please feel free to contact William Daly, Director of Governmental Affairs, at (202) 503-3302 or bdaly@nabl.org.

Thank you in advance for your consideration of these comments.

Sincerely,

Allen K. Robertson

Allen K. Robertson

CC:: Michael Post

COMMENTS OF

THE NATIONAL ASSOCIATION OF BOND LAWYERS

REGARDING

MSRB NOTICE 2014-01, REQUEST FOR COMMENT ON DRAFT MSRB RULE G-42 ON DUTIES OF NON-SOLICITOR MUNICIPAL ADVISORS

In 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**")[1] which, among other things, amended Section 15B of the Securities Exchange Act of 1934 (the "**Exchange Act**") to provide for the regulation by the Securities and Exchange Commission ("**SEC**") and the Municipal Securities Rulemaking Board (the "**MSRB**") of municipal advisors[2] in order to protect "municipal entities"[3] and "obligated persons."[4] The regulation of municipal advisors and their advisory activities is, as the SEC has recognized, generally intended to address problems observed with the conduct of some municipal advisors, "including 'pay-to-play' practices, undisclosed conflicts of interest, advice rendered by financial advisors without adequate training or qualifications, and failure to place the duty of loyalty to their clients ahead of their own interests."[5]

[1] Pub. Law No. 111-203, 124 Stat. 1376 (2010).

[2] Section 15B(e)(4)(A) of the Exchange Act defines the term "municipal advisor" to mean, in relevant part and subject to certain exceptions, "a person (who is not a municipal entity or an employee of a municipal entity) that (i) provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues; or (ii) undertakes a solicitation of a municipal entity."

[3] Section 15B(e)(8) of the Exchange Act defines the term "municipal entity" to mean "any State, political subdivision of a State, or municipal corporate instrumentality of a State, including - (A) any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (B) any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (C) any other issuer of municipal securities."

[4] Section 15B(e)(10) of the Exchange Act defines the term "obligated person" to mean "any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities."

[5] 78 FR 67468 (November 12, 2013) ("**SEC Final Rule**") at 67469 (Nov. 12, 2013).

In keeping with its stated purpose, the Dodd-Frank Act specifically establishes that a fiduciary duty is owed by a municipal advisor to its municipal entity clients.[6] By contrast, the Dodd-Frank Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients.[7]

The SEC and MSRB have developed registration regimes for municipal advisors. In September 2010, the SEC adopted, and subsequently extended, a temporary registration program for municipal advisors.[8] In November 2010, the MSRB amended its rules to require municipal advisors to register with the MSRB.[9] In December 2010, the SEC proposed a permanent registration regime for municipal advisors.[10]

On September 18, 2013, the SEC adopted final rules to, among other things, define who is a municipal advisor, establish a permanent registration regime for that defined set of persons, and establish basic recordkeeping requirements for such advisors (the "**SEC Final Rule**").[11] The SEC Final Rule was originally scheduled to take effect on January 13, 2014, but on that day, the SEC announced that the SEC Final Rule would be stayed until July 1, 2014.[12]

The Exchange Act, as amended by the Dodd-Frank Act, requires that the MSRB propose and adopt rules to effect the purposes of the Exchange Act with respect to advice provided to or on behalf of municipal entities or obligated persons by municipal advisors regarding municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons. The rules must prescribe records to be made and kept by municipal advisors (and the periods for which such records must be preserved) and must prescribe means reasonably designed to prevent acts, practices, and courses of business that are inconsistent with a municipal advisor's fiduciary duty to its clients.[13]

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[6] Section 15B(c)(1) of the Exchange Act provides "A municipal advisor and any person associated with such municipal advisor shall be deemed to have a fiduciary duty to any municipal entity for whom such municipal advisor acts as a municipal advisor, and no municipal advisor may engage in any act, practice, or course of business which is not consistent with a municipal advisor's fiduciary duty or that is in contravention of any rule of the Board."

[7] *See* SEC Final Rule at 67475 n.100.

[8] *See* Exchange Act Release No. 34-62824 (September 1, 2010); 75 FR 54465 (September 8, 2010).

[9] *See* Exchange Act Release No. 34-63308 (November 12, 2010); 75 FR 70335 (November 17, 2010).

[10] Exchange Act Release No. 34-63576 (December 20, 2010), 76 FR 824 (January 6, 2011).

[11] *See supra* note 5.

[12] Registration of Municipal Advisors – Temporary Stay of Final Rule, Exchange Act Release No. 34-71288, 79 Fed. Reg. 2777 (Jan. 16, 2014).

[13] Exchange Act §15B(b)(2).

On January 9, 2014, the MSRB published a Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors (the "**Request for Comments**"), which included the text of draft Rule G-42 and Supplementary Material to the draft rule.[14]

Summary of Draft Rule G-42

Draft Rule G-42 proposes basic duties and responsibilities of a municipal advisor. Central among the obligations proposed in draft Rule G-42 are duties of a municipal advisor as a fiduciary to its municipal entity clients, including a duty of care and a duty of loyalty. Draft Rule G-42 would also require municipal advisors to disclose conflicts of interest and require a municipal advisor to have a reasonable basis for believing that a transaction or product is suitable for its client prior to recommending it.

Under draft Rule G-42, municipal advisors would be required to evidence their municipal advisory relationship with a client by a writing entered into prior to, upon, or promptly after the inception of the municipal advisory relationship. Draft Rule G-42 would require the writing establishing the relationship to describe the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement.

Overview of NABL's Comments

As more particularly described below, NABL writes to urge that careful consideration be given to the precise language used in final Rule G-42 to ensure that municipal advisors are clearly informed of their duties and not unduly burdened, and that the choices available to municipal entities and obligated persons in engaging municipal advisors are not inadvertently or unduly limited.

We also focus our comments on the fiduciary duty aspect of the G-42 draft rules. As lawyers, we are familiar with fiduciary duty principles under common law. We are also subject to certain rules of professional conduct, which may be analogized in certain respects to fiduciary duties, and which we believe should be considered as examples for the rules applicable to municipal advisors. Our comments are divided into three categories, the first of which consists of general comments related to the framework of the municipal advisor rules. The second section of our comments is responsive to certain of the MSRB's questions. The third section consists of comments related to specific provisions of, and language in, the draft Rule G-42.

NABL's General Comments

- ***In undertaking to define the duties of municipal advisors as fiduciaries to municipal entities, MSRB Rule G-42 should draw on established common law and similar standards that have been used to express or elaborate fiduciary duties, for example, the standards that are applicable to attorneys.***

[14] MSRB Notice 2014-1 (Jan. 9, 2014).

- *Rule G-42 appears to comingle broker-dealer duties with traditional fiduciary duty standards.* For example, the provisions of draft Rule G-42 applying to the disclosure of conflicts of interest and recommendations are drawn from comparable requirements for broker-dealers rather than from standards that apply to common law fiduciaries or attorneys.

- *Rule G-42 also appears to draw heavily from registered investment advisor duties.* The relationship between a registered investment advisor and its client arises in narrower contexts than the municipal advisor-client relationship, and, thus, there are limits to how much the MSRB should draw from the duties applicable to registered investment advisors in defining the duties of municipal advisors. The attorney-client relationship is more comparable to the municipal advisor-client relationship, because both relationships can have (a) a wide spectrum of scopes of responsibilities, (b) similar contexts in which there are interactions with the client, and (c) a longer duration over which the representation occurs. The duties of attorneys tend to be more principle-based, allow for wide latitude in how the attorney and client fashion their relationship, and tend to be less specifically proscriptive.

- ***The provisions in draft Rule G-42 concerning conflicts of interest are currently unclear. Such provisions could be structured in a way that is similar to the provisions for attorneys.***

  - To that end, we believe that the ABA Model Rules of Professional Conduct (the "**Model Rules**") are helpful because they incorporate concepts applicable to an attorney's ability to address conflicts, including a procedure for obtaining informed consent that protects his or her clients.

  - The Model Rules provide a definition of conflicts, which, broadly stated, involve the representation of one client while being adverse to another client, or involve a significant risk that the representation of one or more clients will be materially limited by the attorney's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

  - If an attorney has a conflict of interest, the Model Rules provide that: "Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if: (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client; (2) the representation is not prohibited by law; (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and (4) each affected client gives informed consent, confirmed in writing."[15]

[15] ABA Model Rules of Professional Conduct, Rule 1.7(b).

- We believe that the regulation of conflicts of interest affecting municipal advisors could be similar. In particular, we believe that MSRB Rule G-42 could incorporate the following concepts:

  - Municipal advisors should be required to disclose all material conflicts of interests as paragraph (b) of draft Rule G-42 currently requires.

  - Borrowing from the Model Rules, municipal advisors could be required to obtain "informed consent, confirmed in writing" to each waivable material conflict of interest. We think that this requirement should not be different for municipal advisors than it is for common law fiduciaries or attorneys. Consent could take the form of a writing evidencing an engagement, including a letter of intent, after disclosure to the client sufficient to establish informed consent. We believe that the requirement to obtain informed written consent from an advisory client is a necessary corollary to the requirement that an advisor disclose and provide sufficient detail about the nature of all material conflicts of interest.

  - Like the Model Rules, MSRB Rule G-42 could also preclude municipal advisory engagements that involve unwaivable conflicts of interest. The Model Rules describe such a conflict as one that will cause the attorney to be unable to provide competent and diligent representation to each affected client. Under draft Rule G-42, a municipal advisor could proceed with an engagement if it merely disclosed any "actual or potential conflicts of interest of which it is aware after reasonable inquiry that might impair its ability either to render unbiased and competent advice to or on behalf of the client or to fulfill its fiduciary duty to the client, as applicable" We believe that, if a municipal advisor concludes that a conflict of interest substantially impairs its ability to render unbiased and competent advice, final Rule G-42 could prohibit the municipal advisor from undertaking the representation.

- ***We believe that the proposal's requirements concerning recommendations are more formal than is necessary***.

  - Paragraph (d) of draft Rule G-42 places certain obligations and restrictions on municipal advisors with respect to recommendations provided to clients. However, just like attorney-client relationships, municipal advisor-client relationships could include a wide spectrum of activities. Just like attorney-client relationships, the task that municipal advisors must perform in providing their advice should be governed by the terms of the engagement. For example, a municipal advisor should be free to provide advice regarding or otherwise recommend pricing of a transaction even if it does not believe that the transaction is preferable to other possible transactions, if its client instructs it to do so. In addition, a municipal advisor should be free to recommend a transaction based on facts given to it by its client, without exercising any diligence to check the facts, if consistent with its engagement.

- Suitability is a regulatory concept that may not be appropriate in all municipal advisor-client settings. In addition, if a municipal entity or obligated person has determined to undertake a transaction, a municipal advisor should be permitted to make a recommendation as to pricing or some other limited aspect of the transaction, even if it does not agree that the transaction is suitable for the client.

- If a municipal advisor represents a municipal entity, the municipal advisor should be permitted to recommend a range of transactions that would be in the client's interest, even though only one could be in the "best" interest of the client.

- ***We believe that MSRB Rule G-42 should contain a provision describing how municipal advisors may withdraw from or terminate municipal advisor relationships with municipal entities***.

  - As with other fiduciary standards, MSRB Rule G-42 should provide for the withdrawal and termination of municipal advisory relationships. Municipal advisors must ensure that their withdrawal or termination complies with fiduciary duty standards. Further, any rule or guidance should state that when a municipal advisory relationship is no longer in existence, the municipal advisor no longer owes duties to its former client.

NABL's Responses to MSRB's Specific Questions Numbers 1 and 7

"1) Draft Rule G-42 follows the Dodd-Frank Act in deeming a municipal advisor to owe a fiduciary duty, for purposes of the draft Rule G-42, only to its municipal entity clients. Is carrying forward that distinction in the draft rule appropriate in light of the services a municipal advisor provides to its obligated person clients? Would having a uniform fiduciary standard applied to <u>all</u> of a municipal advisor's clients facilitate compliance with the draft rule or provide better protection for issuers? If so, are there any legal impediments to the MSRB extending a fiduciary duty in the draft rule to all clients of a municipal advisor?"

- ***We do not recommend that the MSRB mandatorily extend the fiduciary duty of a municipal advisor to obligated persons, but Rule G-42 should leave them free to do so by agreement .***

  - Obligated persons include a wide spectrum of entities (for instance, universities, hospitals, corporate borrowers, and developers), and applying a fiduciary duty to each and every one of those entities could lead to unintended consequences.

  - Municipal advisors and their obligated person clients should be free to fashion their relationships in any way that they deem appropriate for both of their interests. Obligated persons are free to impose fiduciary duties on their advisors by contract, if they choose. Since the Dodd-Frank Act specifically omitted advice to obligated persons from statutory fiduciary duties, the MSRB, consistent with statutory intent, should not extend fiduciary duties to their advisors. To do so would unnecessarily reduce the choices available to obligated persons and, in many cases, increase their transaction expenses.

"7) Should a municipal advisor be required to obtain a written acknowledgment from the client of receipt of the conflicts disclosure and consent to any conflicts disclosed before proceeding with a municipal advisory engagement?"

- We believe municipal advisors could be required to obtain "informed consent, confirmed in writing" to material conflicts of interest. Please see our discussion of the conflicts disclosure and prohibition provisions above as they relate to the Model Rules. Requiring informed consent, confirmed in writing also would be consistent with the requirements of the Commodities Futures Trading Commission for commodity trading advisors. We believe consent could take the form of a writing evidencing an engagement, including a letter of intent, after disclosure to the client sufficient to establish informed consent.

NABL's Comments Related to Specific Provisions and Language

- ***Paragraph (b) of draft Rule G-42 - Disclosure of Conflicts of Interest and Other Information.***

  - If retained, the lead-in to draft Rule G-42(b) should be revised to clarify its intent. As worded, draft Rule G-42(b) would require a municipal advisor to make "full and fair disclosure of all material conflicts of interest, *including disclosure of*" [emphasis added] the matters described in the nine subparagraphs following the lead-in. This lead-in sensibly suggests that only conflicts that could materially affect the municipal advisor's advice would need to be disclosed. However, the nine subparagraphs include matters that would not appear to present a conflict of interest, but rather might otherwise influence a client's decision to engage the municipal advisor (e.g., whether the municipal advisor has professional liability insurance or has been a party to disciplinary proceedings). The inclusion of these items confuses whether disclosure of other items is required only if they could materially affect the municipal advisor's advice. For example, must payments to third parties be disclosed if they will have no impact of the independence of the advice? If draft Rule G-42(b) is retained, we believe it should be revised to describe less ambiguously what must be disclosed.

  - We question the proposed requirement to disclose professional liability insurance coverage, since policies insure the advisor, not the advisee; advisors are not guarantors of results; and policy coverage provisions can be very complicated, so it would be difficult to make a "full and fair disclosure…of…the amount and scope of coverage of professional liability insurance." Issuers are free to (and often do) ask for such information, if material to them. If the requirement is retained, to avoid unnecessary risk and expense, the MSRB should consider a safe harbor of some type for the fullness and fairness of policy summaries.

  - Municipal advisors should not have a disclosure obligation to investors, as proposed in Supplemental Materials .07. Mandated disclosure of conflicts that are not material to an issuer's credit or an investment in its securities will nonetheless create an impression that they are material to the offering. Since the Dodd-Frank Act does not require a municipal advisor for offerings, it follows that

the intent of the municipal advisor provisions is to protect issuers, not investors. Consequently, the MSRB should leave to issuers whether to disclose conflicts of interest that they choose to waive.

- The phrase "inception of a municipal advisory relationship" is used in both paragraphs (b) and (c). Draft Rule G-42 provides that a "municipal advisory relationship" is ". . .deemed to exist when a municipal advisor engages in or enters into an agreement to engage in municipal advisory activities. . ." Further guidance on when and how casual or preliminary discussions would constitute "engaging in municipal advisory activities" and thus trigger the delivery of documentation would be helpful.

- ***Paragraph (d) of Draft Rule G-42 – Recommendations.***

  - Draft Rule G-42(d) would provide that a municipal advisor may recommend a municipal securities or financial product transaction to a municipal entity only if the transaction *is* in the client's best interest. By contrast, the preceding portion of the same paragraph would impose a suitability requirement that requires only a *reasonable basis for believing* that a recommended transaction is suitable. If retained, final Rule G-42(d) should clarify that compliance with the best interest test will be satisfied by a municipal advisor's reasonable belief, rather than whether a transaction objectively was in the issuer's best interest, especially if judged in retrospect.

- ***Paragraph (f) of Draft Rule G-42 – Principal Transactions***.

  - The MSRB should revise draft Rule G-42(f) to be consistent with our suggestions for conflicts of interest above. Final Rule G-42 could provide a standard that governs which conflicts can and cannot be waived by a client. If Final Rule G-42 provides that certain conflicts cannot be waived by a client, we recommend that the only unwaivable conflicts be transaction-based, i.e., a municipal advisor cannot serve as a municipal advisor and act as a principal in the same transaction.

    - Unless the principal prohibition is limited as described above, it would unnecessarily and substantially restrict the choices available to municipal entities in engaging municipal advisors and engaging in other transactions with them or their affiliates. Under common law, an agent's fiduciary duties of loyalty (including avoiding conflicts of interest) and care may be waived or otherwise modified by the principal, if the principal is not legally incompetent.[16] As a result, any unwaivable conflicts of interest would be inconsistent with these established common law principles.[17]

[16] See Restatement of the Law Third, Agency Sec. 8.06 (duties described in Sec 8.01 [to act loyally], Sec 8.02 [not to acquire material benefit], and Sec 8.03 [not to deal with the principal as or on behalf of an adverse party in a transaction in connection with the agency relationship], may

- Consistent with the duties of other fiduciaries, if a municipal advisor is representing a client on a specific transaction, the advisor or its affiliates should be able to act in a principal capacity on an unrelated transaction with the client upon full disclosure of the unrelated transaction and, if it presents a conflict, informed consent by the client. A transaction-based prohibition aligns with the SEC's guidance on the scope of the fiduciary duty that attaches to a dealer that "acts as an advisor" to a municipal entity. Furthermore, we note that the SEC permits registered investment advisors to act as principals in transactions with clients as long as they provide disclosure and obtain informed consent, and municipal advisors should be permitted the same relief in dealings with their clients. Consistency with the SEC's guidance will provide clear guidance to market participants and will avoid confusion.

- The prohibition on principal transactions should also be revised to exclude traditional banking services provided to municipal entities. Many banks provide financial advisory services to municipal entities through separately-identifiable departments or divisions, subsidiaries or affiliates, in addition to traditional banking services. These banking services are essential to the daily operations of municipal entities throughout the U.S., and include checking and deposit account relationships and extensions of credit that are specifically permitted to be undertaken by banks under the SEC's municipal advisor rules.

    - In addition, as proposed, Paragraph (f) would preclude a bank that serves as a municipal advisor for a municipal entity's general obligation bond offerings from acting as a principal in a direct purchase transaction for bonds issued by the municipal entity and secured wholly by special revenues. The two transactions would be entirely separate and, given full disclosure by the bank and informed consent by the municipal entity, there would be no confusion regarding the role or interests of the bank in the direct purchase transaction.

- As proposed, Paragraph (f) is an overly broad prohibition, and a possibly unintended regulation of entities not engaged in non-exempt municipal advisory activities. The MSRB should confirm that all activities exempted or excluded under the SEC's municipal advisor rules, as well as those activities already regulated or exempted by the SEC or other federal agencies, are not prohibited by Paragraph (f).

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be waived by the principal, if in obtaining consent the agent acts in good faith, the agent describes all facts known or that should be known, and the agent otherwise deals fairly), and Sec. 8.08 (duty to act with care, competence and diligence is subject to the terms of the principal-agent agreement).

[17] Because there is no guidance as to whether Congress intended to depart from established common law principles and impose a heightened fiduciary duty on municipal advisors, we would encourage the MSRB to carefully consider any fiduciary duties that go beyond those principles.

- As the MSRB does not have apparent authority to regulate the conduct of affiliates of municipal advisors that are not brokers, dealers or municipal securities dealers, any prohibition on principal transactions should be narrowly-tailored and addressed to the municipal advisor's right to advise, rather than its affiliates' right to engage in unrelated transactions.

- The phrase "Except for an activity that is expressly permitted under Rule G-23" is unclear as to exactly what activity is permitted. The interplay between the activities expressly permitted under Rule G-23 and the SEC's guidance on the fiduciary duty and associated prohibitions that attach to a person that "acts as advisor" to a municipal entity have created considerable uncertainty among market participants. To avoid further uncertainty, and pending any further guidance by the MSRB on Rule G-23, we recommend that this phrase be deleted.

- ***There are several places where draft Rule G-42 appears to apply to persons engaged in unregulated activities, and we think these portions of the draft Rule should be amended to clarify that the Rule does not so apply.***

  - Draft Rule G-42 would impose business conduct rules on municipal advisors when they engage in "municipal advisory activities" or "municipal advisory relationships" (e.g. G-42(a)(i) and (ii), G-42(b), and G-42(c)), and it would define those phrases by reference to Section 15B(e)(4)(A) of the Dodd-Frank Act and the SEC Final Rule, except that it would exclude solicitation activities. The phrase "municipal advisory activities" is not used in the Dodd-Frank Act. In the SEC Final Rule the phrase is defined as specified activities that, *absent an exemption or exclusion contained in the definition of "municipal advisor,*" would cause a person to be a municipal advisor. Consequently, unless clarified, draft Rule G-42 would refer to activities that are unregulated (because exempted or excluded by the SEC Final Rule) in addition to those regulated under the SEC Final Rule. To avoid that surely unintended and possibly overreaching consequence, the definition of "municipal advisor activities" in draft Rule G-42 should be clarified to refer to the activities described in paragraph (1) of the definition of that term in the SEC Final Rule, but only when the activities do not qualify for an exemption or exclusion included in the definition of "municipal advisor" in the SEC Final Rule.

  - Similarly, draft Rule G-42 would require disclosure of and/or prohibit certain payments made to obtain or retain "municipal advisory business," and it would define that phrase to include the provision of any advice in connection with municipal securities and municipal financial products, even if the advice is excluded (by the Dodd-Frank Act) or exempted (by the SEC Final Rule) from the definition of "municipal advisor" under the SEC Final Rule. While the MSRB might have authority to require disclosure of or prohibit unregulated activity as a condition to lawfully conducting regulated activities, we believe that extending these disclosure and prohibition provisions to unregulated activities would be inconsistent with legislative intent (at least for activities excluded from regulation by the Dodd-Frank Act). In addition, if all other aspects of the MSRB's business

conduct rules were to apply only to regulated activity, expanding the scope of these disclosure and prohibition provisions to unregulated activities would complicate and substantially increase the cost of compliance. For these reasons, we believe the definition of "municipal advisor business" should be clarified to exclude exempt advice.

- Similarly, draft Rule G-42(e) (requiring a reasonable basis for recommendations and, for municipal entity clients, limiting recommendations to those in the clients' best interest) on its face appears to apply to all recommendations for transactions in municipal securities or municipal financial products, including those excluded or exempted from the definition of "municipal securities" by the Dodd-Frank Act or the SEC Final Rule. For the reasons discussed above, it should be limited to non-excluded, non-exempt recommendations.

- Similarly, draft Rule G-42(g)(iv) (prohibiting certain fee-splitting arrangements) on its face appears to apply to transactions even when advice with respect to the transaction is exempted or excluded from the term "municipal advisor" by the SEC Final Rule. A dealer-advisor may be a municipal advisor in one transaction with one client and an underwriter in another transaction with another issuer. We believe the prohibition on fee-splitting should apply only when a municipal advisor is giving non-exempt advice as part of the same transaction, not when it is giving exempt advice as an underwriter or otherwise. Otherwise the draft ban on fee-splitting with underwriters could effectively make it illegal for dealer-advisors to join underwriting syndicates for issuers whom they do not advise.

- ***The proposed prohibition or requirement of some other activities should be revised to avoid unintended consequences.***

  - The duties proposed to be imposed by draft Rule G-42 in connection with offering documents are ambiguous, because they provide that issuers may control the scope of engagement, but not the duties of municipal advisors in performing the engagement. Draft Rule G-42(a)(i) would impose a duty of care in the conduct of municipal advisory activities, which the Supplementary Material states would include a duty to make a reasonable inquiry as to relevant facts and, unless otherwise directed by the client, to undertake a thorough review of the official statement for municipal securities transactions. Consequently, it is not clear whether issuers would be permitted to engage a municipal advisor to prepare a draft offering document without also engaging it to "make a reasonable inquiry as to the relevant facts" by checking the accuracy and completeness of the information in the document. The provisions of draft Rule G-42 should be clarified to unambiguously permit an issuer to engage an advisor to assemble an offering document without imposing a duty on the advisor to check the information supplied to it, especially if the information is supplied by the issuer. In addition, the advisor should not have a duty to check information supplied by others if the issuer prefers to check that information itself or to engage disclosure counsel to do so.

EXHIBIT A

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March 10, 2014

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Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
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Re: Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors; MSRB Regulatory Notice 2014-01

Dear Mr. Smith:

The National Association of Health and Educational Facilities Finance Authorities (*"NAHEFFA"* or the *"Association"*) appreciates the opportunity to submit its comments on the above-referenced notice (the *"Notice"*) and draft proposal for MSRB Rule G-42 (the *"Proposed Rule"* or the *"Rule"*).

The Association is a national association of mostly statewide tax exempt bond issuing authorities (each an *"Authority"* and, collectively, the *"Authorities"*) which are created and empowered by state laws and recognized by the Internal Revenue Code to provide conduit financing for nonprofit healthcare and education institutions and other nonprofit organizations. (Some of the Authorities also issue bonds for governmental purposes and other private activities.) NAHEFFA's mission is to support access to readily available, low-cost capital financing options for these institutions. The Association promotes the common interests of its member organizations and seeks to enhance the effectiveness of all such organizations and their programs. The Association focuses its efforts on issues which directly influence the availability of, or access to, financing options, including tax-exempt financing, for health and educational institutions.

I. OVERVIEW

Our comments on the Notice are focused on (i) the ability of an Authority's financial advisor to advise the borrower in conduit financing transactions, (ii) the ability of a conduit borrower's financial advisor to advise the Authority in conduit financing transactions, (iii) whether the borrower and an Authority can use the same municipal advisory firm and (iv) the distinction between the duty of loyalty and other obligations set forth in the Proposed Rule. These comments stem in part from the request in the Notice for comment on whether the MSRB should extend the fiduciary duty owed by municipal advisors to municipal clients to a municipal advisor's obligated person clients, which, in our case are our conduit borrowers.

We appreciate that the MSRB has highlighted and requested comment on how the Rule should apply in conduit financings. The Association is supportive of the basic purpose behind the Proposed Rule and the underlying statutory provisions. The final Rule should work effectively to protect issuers and, in conduit financings, borrowers and we offer in that spirit a proposal in this submission that we believe will ensure this. We also are sensitive, however, to the special structure and considerations which apply in our sector where the issuer and borrower are separate entities. To the extent the present system and structure works efficiently, we do not want this Rule to disrupt valuable information received by borrowers or to impose inordinate costs on non-profit institutions. The Proposed Rule's draft economic impact analysis understandably does not yet analyze this specific scenario but the Association believes that its comments highlight the need to do so.

First, the Association is concerned that the Proposed Rule could inhibit the current, beneficial practice of some of its members of hiring a financial advisor to provide advice that ultimately benefits the conduit borrower. The Association believes it is critical to the cost-effectiveness of conduit financings that Authorities, who so wish, be able to continue this practice.

Second, the Association believes and requests MSRB's confirmation that there is no unmanageable conflict when there are advisors for both the municipal entity and the conduit borrower or when the conduit borrower has a municipal advisor who provides advice on the municipal financing. The Proposed Rule does not provide any clarification or guidance on these matters which could have significant impact on the current practices of the Association's members and how they assist their conduit borrowers.

Third, the Association is concerned that certain obligations owed by a municipal advisor to an obligated person client under the Proposed Rule in effect, inappropriately impose a fiduciary duty on municipal advisors providing advice to obligated persons who are not otherwise municipal entity clients. The Association respectfully submits that imposing a fiduciary duty (whether implicitly or explicitly) on a municipal advisor that provides advice to an obligated person is contrary to the specific legislative intent expressed in the Dodd-Frank Act and unnecessarily complicates a municipal advisor's role in conduit financings.

Finally, the Association proposes that it may be prudent for the MSRB to create a separate rule (or an interpretation under Rule G-17) that sets forth the duties and obligations of municipal advisors with respect to obligated persons or to revise the Proposed Rule to specifically and clearly set forth such obligations. Such a rule should be based on existing MSRB rules for other professionals involved in municipal financings concerning the level of care and fair dealing.

Overall, the objective of the Rule should be to be properly protective but to provide Authorities, borrowers and advisors with enough flexibility to achieve their objectives in conduit financings, including containing costs.

II. SINGLE FINANCIAL ADVISOR

As noted, the Association's members consist of various financing authorities that are organized as public instrumentalities of the respective states in which they are organized, or a similar type of municipal or other public entity. These state financing authorities frequently act as issuers in conduit financings on behalf of borrowers that consist of both large and small not-for-profit healthcare and educational institutions and other nonprofit entities.

Current Practice of Authority Retaining Financial Advisor. Practices among our member Authorities vary greatly. Some of the Authorities retain a financial advisor (either for a particular transaction, or on a long-term basis), that provides advice to the Authority which the Authority makes available to the borrower as well. In addition, the Authority's financial advisor sometimes provides advice directly to the conduit borrower. For certain of the Authorities, the hiring of the financial advisor is part of its efforts to meet statutory or policy directives that specifically provide that the Authority's responsibility is to assist its borrowers in obtaining the most appropriate financing. Borrowers often rely on the Authorities for guidance and assistance throughout the transaction, and may rely to a large extent on the Authority's financial advisor. This practice has been very helpful particularly for "small" borrowers, *i.e.,* those that have limited funds and limited or no access to other financing resources. Some Authorities are also able to achieve additional economies of scale by retaining a financial advisor that serves on a long-term basis with respect to all of its conduit borrowers. By doing so, the Authority is able to obtain more favorable pricing from the financial advisor, which in turn saves the borrowers money.

Concerns Raised by the Proposed Rule. The Association is concerned that the Proposed Rule, in its current form, could potentially inhibit an Authority's practice of engaging a single financial advisor who advises the Authority as well as its borrower.

The affirmative obligations imposed in sections (c) and (d)(i)-(iii) of the Proposed Rule are examples. These provisions would mandate specific agreements and discussions between the municipal advisor and the obligated person in addition to the Authority. Such discussions could be burdensome to clients and would impose additional time and other charges. The Association believes it is important that the Authorities who retain the financial advisors be able to continue to determine the scope of the municipal advisor relationship, and that they are in a position to do so effectively.

Also, the complete prohibition on principal transactions set forth in subsection (f) of the Proposed Rule could serve as a disincentive for municipal advisors to work with the Authorities and their borrowers, particularly large municipal advisory firms with many affiliates that could be acting as principals with respect to a borrower on a different transaction. The transaction costs to

determine whether any affiliates are acting as principal in other transactions not just with respect to the issuer, but also the obligated person, could be prohibitively expensive.[1]

Further, section (b)(ii) of the Proposed Rule would require advisors to disclose, not just to conduit issuers, but also to borrowers, "*any affiliate*…that provides *any* advice, service, or product to or on behalf of the client that is directly *or indirectly* related" to the services being provided [emphasis added]. This kind of open-ended directive, which is both vague and extremely broad, makes compliance exceptionally difficult — particularly when applied to conduit borrowers in addition to the Authorities.

The Association is very concerned that these and other obligations of advisors under the Proposed Rule will (i) destroy the economies of scale some Authorities have been able to create by retaining financial advisors for conduit financings in the manner described above, (ii) effectively cause financial advisors that do business with the Authorities to no longer provide such services and/or (iii) in many cases force borrowers to obtain their own financial advisors, thus duplicating costs and effort (assuming, of course, that advisors are not constrained by the operation of the Rule and cease to be available to conduit issuers as described above).

The municipal advisor engaged by an Authority already has a fiduciary responsibility to that entity and it is unnecessary to impose complicated standards on the firm simply because the conduit borrower is benefiting from the advice provided by the municipal advisor who also advises the conduit issuer. As pointed out by the SEC in its rules, it is only when the municipal entity is notified of the proposed financing by the obligated person that the municipal advisor rules become applicable to the obligated person. Also, in a conduit financing, the Authority and the conduit borrower have substantially similar interests when it comes to structuring the best financial transaction for the conduit borrower. Therefore, it would seem, there is little need to have additional duties also run to the obligated person on the same transaction.

III. Multiple Advisors in a Transaction or an Advisor Hired by the Conduit Borrower.

There are also times when a conduit borrower wishes to retain its own financial advisor in addition to the municipal entity issuer having its own advisor. In such situations, two municipal advisors may be working on the same municipal financing and could either be from different firms or the same firm. At other times, there are transactions when the conduit borrower retains the municipal advisor, and the issuer has chosen not to retain an advisor.

Since there are different levels of responsibility a municipal advisor owes to a municipal entity and obligated persons, conflicts and confusion could be created under the Proposed Rule.

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[1] The blanket prohibition on principal transactions could also be harmful to small conduit borrowers who may not have other options for the services being provided by the entity acting or purporting to act as principal.

For example, the Proposed Rule does not address whether municipal advisors from the same firm representing each of the Authority and the borrower presents an unmanageable conflict that would prohibit such an arrangement. As another example, the Proposed Rule leaves unanswered whether a municipal advisor hired by the conduit borrower, but who gives advice on the municipal financing, also has a fiduciary responsibility to the municipal entity[2] and whether the municipal advisor needs to make the required disclosures to the municipal entity even though they are initially hired by the conduit borrower.

The Association believes that the potential conflicts and confusion created by the Proposed Rule are unwarranted and do not serve the purposes of the law. The Association believes that the interests of the Authority and borrower in a conduit financing transaction are sufficiently aligned such that either (i) a single municipal advisor could provide advice to the borrower and an Authority in the same transaction, or (ii) municipal advisors from the same firm could represent each of the Authority and borrower and, in each case, still fulfill their respective duties owed to its client, so long as the advisors make appropriate conflicts disclosures and take any other necessary measures (*e.g.*, establishing a "screen" between the two advisors within the firm, if necessary).

It is important that the MSRB provide guidance on what the advisors must do in these situations and we request a confirmation that there is no unmanageable conflict or other issue in these situations that would prevent an advisor from advising both an Authority and borrower, or two advisors from the same firm from representing an Authority and borrower separately.

IV. FIDUCIARY DUTY

The Proposed Rule correctly limits a municipal advisor's explicit fiduciary duty to only municipal entity clients/issuers. We see no legal basis for any other conclusion nor did the SEC. Nonetheless, many of the obligations imposed upon a municipal advisor under the Proposed Rule as well as imposing a duty of care appear by implication to impose a fiduciary duty on municipal advisors with respect to obligated person clients.

For example, the Proposed Rule imposes upon municipal advisors who advise obligated persons a duty of care. Under traditional fiduciary law analysis, a duty of care has long been viewed as part of the fiduciary duty. The Proposed Rule further imposes general duties to disclose in detail any conflicts of interest and document the municipal advisory relationship and sets forth principal transaction prohibitions. Such obligations are typically reserved for fiduciaries holding a duty of loyalty to their principal, not obligations that are generally required of all parties. A municipal advisor should only be required to manage or mitigate such conflicts to the extent required to fulfill the municipal advisor fair dealing obligation under Rule G-17

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[2] This concern is further complicated by the fact that, in many cases, the borrower's municipal advisor is paid from bond proceeds.

Furthermore, the typical duty of care only entails requirements such as possessing the requisite knowledge and expertise.

Although the Proposed Rule does not explicitly label these obligations as part of the fiduciary duty, many of these obligations are fiduciary in nature, requiring a municipal advisor to undertake responsibilities and actions on behalf of its obligated person clients that are typically reserved for fiduciary relationships. By imposing these duties generally across all municipal advisor client relationships, the Proposed Rule arguably has, in effect, extended a fiduciary duty to a municipal advisor's relationship with its obligated person clients.

The Association respectfully submits that imposing a fiduciary duty (whether implicitly or explicitly) on municipal advisors providing advice to obligated person clients is outside of the statutory authority granted to the MSRB in the Dodd-Frank Act. Under Section 15B of the Securities Exchange Act of 1934, Congress directed that the MSRB establish rules regarding a fiduciary duty for municipal advisors only to their municipal entity clients.[3] As the SEC acknowledged in its adopting release of the final municipal advisor rules, municipal advisors do not owe a fiduciary duty to obligated persons, but rather only a fair dealing duty under MSRB Rule G-17.[4] The Proposed Rule's implicit imposition of fiduciary duties to obligated person clients is inconsistent with the MSRB's congressional directive. The duty of care and general duties in paragraphs (b) through (f) of the Proposed Rule should be revised to reflect Congress's intent that only a municipal advisor's relationship with its municipal entity clients be subject to a fiduciary duty.

If the MSRB does not believe that the obligations prescribed by the duty of care and paragraphs (b) through (f) of the proposed Rule amount to a fiduciary duty, the Association requests that the MSRB provide clarification on the legal and practical distinctions among the duty of loyalty, the duty of care and the duties owed under the other obligations imposed under Proposed Rule paragraphs (b) through (f).

For example, the Proposed Rule is unclear on whether the MSRB intends to follow the long-established precedent that alleged breaches of a duty of care are reviewed under a negligence standard, while alleged breaches of the duty of loyalty require intent. There is wording in the Proposed Rule that suggests that the MSRB intends to retain this traditional distinction, but the Proposed Rule should be revised to make clear that the duty of care imposes a negligence standard of conduct while the duty of loyalty requires intent.

Further, the distinction between the duties owed under a duty of loyalty on the one hand, and the prohibition on principal transactions and duty to disclose conflicts of interests on the other needs clarification. In requiring such similar duties of municipal advisors to all clients, it is

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3 15B U.S.C. § 78o-4(c)(1).

4 *See* Adopting Release at 156.

difficult to determine how a municipal advisor's conduct towards its municipal entity clients would differ from its conduct to all clients.

Finally, the distinction between the duties outlined under the duty of care and the recommendation obligations outlined under paragraph (d) of the Proposed Rule need clarification. Similar to the suggestion discussed above, as the Proposed Rule is currently drafted, it is difficult to assess the difference between the recommendation obligations under paragraph (d) and the obligations imposed by the duty of care.

V. PROPOSED SOLUTION

The Association strongly believes that in order for a number of its Authorities to continue to provide cost-effective and accessible financing options for conduit borrowers, it is critical that these Authorities be able to continue the practice of engaging financial advisors that can provide advice that benefits borrowers from time to time. The MSRB needs to provide guidance on the roles and responsibilities of municipal advisors when multiple advisors are involved in a transaction.

The Association suggests that the MSRB either propose a separate rule that (or a Rule G-17 interpretation) sets forth the duties and obligations of municipal advisors with respect to obligated persons (particularly in the context of conduit financings) or revise the Proposed Rule to specifically and clearly set forth such obligations. In either case, the Association respectfully submits that the disclosure and other obligations of municipal advisors with respect to private obligated persons must accurately reflect the arms-length duty of fair dealing. As discussed in Section III above, such duties and obligation should not rise to the level of the duties and obligations currently set forth in the Proposed Rule which improperly amount to a fiduciary duty.

Rather than imposing the numerous and detailed obligations currently contained in the Proposed Rule, the disclosure and other obligations municipal advisors should have with respect to private obligated persons should be simplified to clearly reflect a duty to exercise its best professional judgment and expertise in providing its services and to deal fairly with its clients rather than be held to a fiduciary duty. For example, such obligations could include the obligation (i) to deal fairly with the obligated person and not engage in any deceptive, dishonest or unfair practice; (ii) to disclose actual or potential material conflicts of interest as already contemplated in Rule G-17; (iii) to disclose its role in the financing, the fact that it owes a duty to deal fairly with both the Authority and the borrower under MSRB Rule G-17 and the fact that it owes a fiduciary duty to the Authority but not to the borrower; (iv) to disclose actual or likely conflicts arising from the form of compensation being used; (v) to discuss the material financial characteristics of a complex financings and any incentive of the advisor to recommend such a financing; and (vi) if the advisor believes the Authority or borrower lacks knowledge or experience with the financing structure being used or comes to believe that the Authority or borrower does not understand the financing structure or its key elements, to provide advice, to the extent it deems necessary and appropriate, to assist the Authority and/or borrower in

understanding the financing structure or its key elements. Except where it is absolutely critical to provide individualized disclosures (*e.g.*, with respect to conflicts), the various disclosures could be standardized.

From a conceptual standpoint, the Association suggests that the new rule or revised Proposed Rule outlined above provides Authorities, borrowers and advisors with enough flexibility to achieve their objectives in conduit financings, including containing costs by allowing them to use a single advisor or two advisors from the same firm, while still satisfying the duty of fair dealing.

VI. CONCLUSION

The Association supports the efforts of the MSRB to clarify the role and responsibilities of municipal advisors and to protect Authorities and obligated persons. The Association believes that the framework for regulation of municipal advisors as to obligated persons should accurately reflect the duty of fair dealing, adequately distinguish it from the duty of loyalty and eliminate the burdensome elements of the current Proposed Rule.

The Association appreciates the opportunity to comment on the Notice and the Proposed Rule. Please do not hesitate to contact Pamela Lenane, President of the Association at (312) 651-1340.

Respectfully Submitted by,

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March 10, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: MSRB Notice 2014-01

The National Association of Independent Public Finance Advisors ("NAIPFA") appreciates this opportunity to provide comments in connection with Municipal Securities Rulemaking Board ("MSRB") Notice 2014-01 – Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors (the "Notice").

Introduction

In general, because of the varied nature of the engagements entered into by Municipal Advisors as well as the composition of the firms themselves, NAIPFA believes that a principles-based rule rather than the prescriptive approach taken by the Notice would better serve the municipal market. In addition, the Notice puts in place a series of regulations which will place independent registered Municipal Advisors ("IRMAs")[1] at a significant competitive disadvantage to their broker-dealer counterparts, and will impose undue regulatory burdens upon small Municipal Advisor firms.

We note that it appears from the text of the Notice that the MSRB is focusing primarily on those non-solicitor Municipal Advisors who provide advice with respect to the issuance of municipal securities, rather than those Municipal Advisors who provide services related to the investment of bond proceeds. Therefore, for purposes of these comments, unless otherwise noted, NAIPFA's use of the term "Municipal Advisor" applies solely to persons who fall within the Securities Exchange Act of 1934 and its definition of "Municipal Advisor" because they provide advice with respect to the issuance of municipal securities and often throughout the period in which an issuance is outstanding.

By way of background, Municipal Advisors have served municipal entities and obligated persons for decades, typically referring to themselves as financial advisors. Although a federal fiduciary duty has been imposed upon Municipal Advisors as a result of the passage of the Dodd-Frank Act, NAIPFA member firms have for decades accepted and acted in accordance with a fiduciary duty with respect to their municipal entity clients. Illustrative of this is the fact that NAIPFA's

[1] The term "independent Municipal Advisor" as used herein refers to those Municipal Advisors who are not, and within the past two years have not been, associated with a broker-dealer.

bylaws, even before the enactment of the Dodd-Frank Act required, as a condition of initial and continued membership, that its member firms accept "a fundamental obligation to act solely in the best interests of the public entity and provide financial advice to the public entity that is not conflicted."

In this regard, we have long supported the imposition of fiduciary responsibilities upon Municipal Advisors and will continue to do so. However, NAIPFA cannot support proposed Rule G-42 to the extent that it seeks to, or may seek to, impose obligations that go beyond what is required to ensure that Municipal Advisors adhere to their fiduciary responsibility.

In addition, NAIPFA feels strongly that in terms of our provision of municipal securities issuance-related services, although Municipal Advisors may have things in common with both investment advisers and broker-dealers, the regulation of Municipal Advisors must ultimately reflect the distinctions that exist between underwriters and investment advisors. In many ways, the role of Municipal Advisors is unique and so should the corresponding regulations.

For example, Municipal Advisors have fiduciary duties just as investment advisors. However, unlike investment advisers who generally have standardized fees and scope of services, Municipal Advisors assess fees and undertake engagements that can vary widely from transaction to transaction, and some engagements may not even involve a transaction, *per se*. Similarly, in some ways Municipal Advisors are like underwriters, such as how both may provide advice to municipal entities and obligated persons with respect to matters such as the issuance of securities. However, in many key respects, Municipal Advisors are very different from underwriters. For example, unlike underwriters, Municipal Advisors are fiduciaries, they do not hold, transfer or otherwise handle client funds, and, with respect to IRMAs, generally are of a much smaller size, both in terms of employees and annual revenue. In light of the foregoing, we believe that the regulations should reflect the unique role played by Municipal Advisors. Therefore, any rules proposed and enacted should be borrowed from those of underwriters and investment advisers only when it is appropriate to do so based upon whether such regulation advances the MSRB's interest in ensuring Municipal Advisor adherence to their fiduciary duty.

Standards of Conduct – G-42(a)

Overall, NAIPFA supports the standards of conduct proposed in the Notice. As noted above, NAIPFA and its member firms have long adhered to similar standards. As such, we do not believe that the standards themselves impose an undue regulatory burden. In addition, the proposed standards accurately differentiate the role of Municipal Advisors from that of underwriters and support Municipal Advisors in effectively discharging their fiduciary duties.

Further, NAIPFA would be supportive, notwithstanding the legality of any such measure, of a rule imposing fiduciary duties upon Municipal Advisors with respect to the advice they provide to obligated persons. As with municipal entities, NAIPFA member firms who serve obligated person clients have long accepted and adhered to a fiduciary standard with respect to their

service to such clients. Thus, we do not believe that this would, in and of itself, impose an undue regulatory burden upon Municipal Advisors.

Disclosures of Conflicts of Interest and Other Information – G-42(b)

1. Text of Rule G-42(b)(viii)

> ***G-42(b)*****.** A municipal advisor must, at or prior to the inception of a municipal advisory relationship, provide the client with a document making full and fair disclosure of all material conflicts of interest, including disclosure of: ***(viii)*** the amount and scope of coverage of professional liability insurance that the municipal advisor carries (*e.g.*, coverage for errors and omissions, improper judgments, or negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage.

2. Comment

NAIPFA believes that an important aspect of supporting to fiduciary duties is requiring that any advice provided be free of material conflicts of interest which may inhibit a Municipal Advisor's ability to provide advice that is in the best interest of the client. In this regard, where a Municipal Advisor has a material conflict of interest, the Advisor should provide disclosures relating to such conflict to its client. Consequently, and as discussed more fully below, we cannot support the disclosure of those matters described within proposed Rule G-42(b)(viii) because the professional liability insurance disclosure requirement noted therein does not relate to any material conflict of interest. Moreover, and as discussed more below, this provision would place IRMAs and small Municipal Advisors at a distinct competitive disadvantage to underwriting firms and broker-dealer Municipal Advisors.

With respect to any disclosure to be mandated, the MSRB should weigh a variety of factors in determining whether a particular disclosure would be appropriate. These factors may include: whether such provision will increase Municipal Advisor adherence to fiduciary duties; the extent to which a particular provision may inhibit competition; and whether any such provision places an undue economic burden upon small Municipal Advisor firms. G-42(b)(viii) fails in all respects and should be eliminated from the MSRB's lists of mandatory disclosures. As discussed more fully below, NAIPFA would welcome a revised provision that states in effect that Municipal Advisors must truthfully disclose, upon request, information related to any professional liability insurance maintained.

NAIPFA does not believe that this disclosure furthers a Municipal Advisor's ability to adhere to its fiduciary duty. It is worth noting for comparative purposes that NAIPFA is unaware of any similar requirement imposed upon investment advisors or attorneys. As fiduciaries, Municipal Advisors must deal honestly with their clients. In addition, unlike all of the other disclosures contained within Rule G-42(b), this disclosure does not relate to any conflict of interest, material or otherwise. A Municipal Advisor's professional liability insurance policy, or lack thereof, neither creates nor eliminates any conflict of interest. However, to the extent that a client desires

to obtain information about a firm's professional liability insurance, that client should be entitled to request such information and expect that any information received will be accurate and complete. Thus, such a requirement would be appropriate in this context.

NAIPFA believes that RuleG-42(b)(viii) as written will curtail competition by, among other things, placing an undue economic burden upon small firms. Further, if firms are mandated to maintain professional liability insurance this burden will only be exacerbated. Large firms, broker-dealer and non-broker-dealer alike, will likely carry more extensive professional liability insurance policies than their smaller counterparts. Mandatory disclosures may cause municipal entities and obligated persons to focus upon this factor in selecting a Municipal Advisor, rather than relying upon the advisor's qualifications. This may, unfortunately, result in many otherwise qualified Municipal Advisors, such as the numerous solo practitioners who have been in the industry for upwards of 30 years, becoming unable to effectively compete against those firms who do possess such insurance.

In addition, because this provision may undermine the selection of potentially more qualified Municipal Advisors solely due to the larger policy limits of a competing firm's professional liability insurance, there could be an increase in litigation as the quality of advice provided declines due to this potential "brain drain;" even mandating professional liability coverage may increase litigation due to the effect that such a mandate would have on forcing otherwise qualified advisors out of the market. In either case, if litigation rates increase so too will the number of firms leaving the market, even further curtailing competition.

This provision may have a particularly significant impact on competition in certain parts of the country. After exploring a professional liability insurance pool and other options available to its members, NAIPFA discovered that there are portions of the country where professional liability insurance specific to Municipal Advisors may not be available. In these states, local Municipal Advisors may be at a significant competitive disadvantage if they are unable to obtain coverage when competing against larger, multistate companies which may be able to obtain insurance in their home state. With respect to small IRMAs, where coverage does exist, the cost can be prohibitive; the market infrastructure and understanding of the industry by insurance companies does not exist at this time in a way that will allow small Municipal Advisor firms to have a level playing field.

In light of the foregoing, and as noted previously, NAIPFA believes that a more appropriate approach to this issue would be to put in place a principles-based rule. Within the context of this provision, NAIPFA believes that it would be appropriate to require Municipal Advisors to truthfully and accurately disclose matters requested by their clients, which could include disclosures relating to the scope and extent of Municipal Advisors professional liability insurance. This would further Municipal Advisor adherence to fiduciary duties by reinforcing the notion that Municipal Advisors owe their municipal entity clients (and potentially obligated person clients) a duty of loyalty. This approach would also support the SEC's goal of placing issuers in control of their debt issuance process, and would ensure that when issuers wish to receive particular disclosures from a Municipal Advisor, that those disclosures are truthful and

accurate and complete. Finally, this approach would negate the negative competitive and economic impacts of the proposed rule.

Documentation of the Municipal Advisory Relationship – G-42(c)

1. Question Regarding The Phrase "Entered Into"

It is unclear from the Notice what the MSRB means by the phrase "entered into" with respect to the writing that a Municipal Advisor must utilize to evidence its engagement. Does this mean that the writing must be a two party agreement? In other words, must the writing be executed by both the Municipal Advisor and its client? NAIPFA respectfully requests clarification in this regard. To the extent that the MSRB intends for this writing to be executed by Municipal Advisors and their clients, NAIPFA hopes that the MSRB will consider the comments set forth below in terms of clarifying this provision.

2. Comments

In reviewing this portion of the Notice, NAIPFA again bases its analysis upon whether these provisions further Municipal Advisor adherence to their fiduciary duties or involve disclosure of material conflicts of interest, and the extent to which such provisions will inhibit competition and place an undue burden upon small Municipal Advisor firms. Overall, NAIPFA believes that the provisions of G-42(c) do not meet these criteria and should be revised accordingly.

In September, 2013, the SEC released its Final Rule on the Registration of Municipal Advisors, which contained a provision that stated, in essence, that a broker-dealers may rely upon the "Underwriter Exemption" if it is engaged by an issuer as its underwriter. In January, 2014, the SEC released its answers to a series of Frequently Asked Questions relating to the Registration of Municipal Advisors. Therein, the SEC explained the manner in which an underwriter can evidence its engagement with a municipal entity or obligated person client for purposes of availing itself of the Underwriter Exemption. In this regard, the SEC stated that a broker-dealer can demonstrate its engagement "either through a writing, such as an engagement letter […] or through other actions."

The features noted by the SEC that must be included within any such engagement letter include:

> (a) the governing body or any duly authorized official of the municipal entity responsible for municipal finance has executed, approved, or acknowledged the engagement letter in writing; (b) the engagement letter clearly related to providing underwriting services; (c) the engagement letter clearly states the role of the broker-dealer in the transaction; (d) the engagement letter relates to a particular issuance of municipal securities that the municipal entity or obligated person anticipates issuing and is not a general engagement for underwriting services that does not relate to any particular transaction; and (e) the engagement letter or a separate writing done at or before the time of the engagement provides all disclosures that are required to be made by underwriters by the time of an engagement under MSRB Rule G-17.

With the exception of (d) above, NAIPFA can find no reason why a parallel series of requirements could not be imposed upon Municipal Advisors with respect to any writing that they may be required to provide to evidence an engagement. With respect to (d) above, NAIPFA believes that because Municipal Advisors often advise on matters that are not "deal" specific, and are often engaged to provide services prior to, during and after a securities issuance, there is no reason to limit their engagement to a particular transaction. Further, unlike underwriters, nothing contained within the SEC's final Municipal Advisor registration rule or the FAQs would limit a Municipal Advisor's ability to enter into a multi-year or multi-transaction engagement. Thus, there is no reason in this instance to impose requirements on Municipal Advisors similar to those contained within (d) above. In addition, clauses (b) and (e) would need to be appropriately tailored to Municipal Advisors.

With respect to G-42(c), the currently proposed requirements do not support Municipal Advisor adherence to fiduciary duties, and G-42(c) imposes more onerous requirements upon Municipal Advisors than the SEC imposes upon broker-dealers wishing to serve as underwriters is counterintuitive. Municipal Advisors are required to act in the best interest of their clients and would breach that duty if they were to put their financial interests before their clients' interests. As a result, and because the SEC believes that it is appropriate for non-fiduciary broker-dealers to make the above-referenced disclosures, there seems to be no basis for imposing more stringent requirements upon Municipal Advisors.

The additional requirements imposed by G-42(c) on Municipal Advisors places them at a significant competitive disadvantage to their underwriting counterparts who are not, for example, required to provide an estimate of their anticipated compensation; underwriters, who have no duty to their clients other than to deal fairly, are able to determine their fee well into the course of a transaction, sometime not until they proffer a formal Bond Purchase Agreement. In addition, underwriters are not mandated to include any particular contract-related terms within their engagement letter, such as clauses relating to the termination of the relationship or their obligations relating to certain aspects of the transaction, whereas Municipal Advisors would be required to include these provisions. Conversely, Municipal Advisors will be required to provide a fee estimate early on in the transaction, well before the full scope of the engagement may be known. These disclosures like the disclosure relating to professional liability insurance will not further adherence to fiduciary duties and will simply result in a greater percentage of issuers choosing their professionals based upon cost rather than quality.

As an alternative to proposed G-42(c), NAIPFA would welcome MSRB efforts to further define the scope of a Municipal Advisor's fiduciary duty. NAIPFA would welcome a rule that states, in effect that, Municipal Advisors would be mandated to provide all of the services corresponding to their fiduciary duties absent a writing limiting the scope of the Municipal Advisor's engagement. With respect to the fee-related disclosures, NAIPFA believes that it would be appropriate to require Municipal Advisors whose compensation is transaction-based to provide a reasonable estimate of the Municipal Advisor's fee to the municipal entity (and potentially obligated person) within a reasonable time after the Advisor has been fully apprised of the scope

and nature of the transactions but in no event later than thirty (30) days prior to the initial estimated date of issuance. This would allow Municipal Advisors to fully assess the scope of their work, the amount of work required to complete the transaction, and the transaction's complexity, and would provide Municipal Advisor clients with an ample opportunity to assess the reasonableness of the Municipal Advisor's estimated fee.

Recommendations – G-42(d)

In general, we support G-42(d) as proposed. We believe that it appropriately reflects Municipal Advisor fiduciary duties. We are, however, concerned with the final portion of this provision, which states, "With respect to a client that is a municipal entity, a municipal advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest."

It is unclear to us how the determination of whether a particular transaction is in a client's best interest will be made. Conversely, in connection with the MSRB's mandate that Municipal Advisor recommendations be suitable, the MSRB provides guidance, such as the statement that the Municipal Advisor must have a "reasonable basis for believing, based on the information obtained through the reasonable diligence of the advisor, that the transaction or product is suitable for the client." In addition, because of the rapid pace at which the municipal market can move, without some criteria upon which the determination of what is in the client's best interest can be made, it seems difficult, if not impossible, to know whether a particular course of action will ultimately result in being what is in the "best interest" of the client.

Therefore, NAIPFA requests that additional guidance be provided that can assist Municipal Advisors in determining whether their recommendation is in the "best interest" of the client. In this regard, NAIPFA believes that a determination of what is in the Municipal Advisor's client's best interest must be based on the facts and circumstances in existence as of the time of the recommendation. We would also request that the MSRB Responses to Webinar Questions numbers 12.1 and 12.2 relating to its February 6 webinar be included in the provisions of the final version of G-42(d).

Review of Recommendations of Other Parties – G-42(e)

As currently written, proposed Rule G-42(e) appears to be inconsistent with SEC Rule 15Ba1-1(d)(3)(vi), the Independent Registered Municipal Advisor Exemption ("IRMA Exemption").

Rule G-42(e) seems to presuppose that a third party is providing advice to a municipal entity or obligated person without themselves being deemed a Municipal Advisor. In other words, such persons are relying upon an exemption from the definition of Municipal Advisor to provide this advice.

The SEC's rationale for creating the IRMA Exemption was that municipal entities would

> have the benefits associated with the regulation of municipal advisors. Such benefits include, but are not limited to, standards of conduct, training, testing for municipal advisors that may be required by the Commission or the MSRB, other requirements unique to municipal advisors that may be imposed by the MSRB, and *fiduciary duty*.[2]

Thus, the SEC's position appears to be that third parties can provide advice to municipal entities because the municipal entities will have the protections afforded to them by their engagement of an IRMA. In fact, the IRMA Exemption specifically requires that the municipal entity or obligated person provide a written representation indicating that they will rely upon the advice they receive from their Municipal Advisor. It seems inconsistent with the IRMA Exemption if G-42(e) were to allow Municipal Advisors to limit the scope of their engagement so as to not have an obligation to review any recommendation made by a third party pursuant to the exemption. In order for a third party to avail itself of the IRMA Exemption, the Municipal Advisor must be providing advice with respect to the same aspects of the municipal financial product or issuance of municipal securities as that of the third party to ensure that such party is receiving the benefits of having engaged a Municipal Advisor. It is, therefore, counterintuitive to believe that the SEC would have created the IRMA Exemption if Municipal Advisors could simply disclaim their obligations to review third-party recommendations.

Rule G-42(e) should therefore be amended to take into consideration the foregoing.

Although not stated, presumably G-42(e) would be equally applicable to advice provided in response to an RFP as well as to those parties relying on the IRMA Exemption. In this regard, Rule G-42(e)(i) through (iii) are potentially overly burdensome in terms of the scope of the obligations they impose. Financings simply would not be completed as Municipal Advisors would be required to devote an extensive amount of time to such analyses.

In light of the foregoing, a principles-based rule would be ideal. Such a rule could simply state that when requested and when such acts are within the Municipal Advisor's scope of engagement, a Municipal Advisor is to consider the recommendations of third parties and determine whether such recommendations are in the best interest of their municipal entity or obligated person client based on all the relevant facts and circumstances. This approach would strike the right balance by protecting the interests of municipal entities and allowing Municipal Advisors to view each recommendation within the context of their particular engagement, without having to go through potentially time consuming and unnecessary analyses.

Principals Transaction & Specific Prohibitions – G-42(f) and (g)

NAIPFA agrees with proposed Rule G-42(f) and (g). We believe that these rules are important measures that are needed to eliminate certain practices that often carry unmanageable conflicts of

[2] Securities and Exchange Commission, 17 CRF Parts 240 and 249 [Release No. 34-70462; File No. S7-45-10], at 156.

interest inconsistent with Municipal Advisor fiduciary duties. As proposed, NAIPFA believes these provisions are appropriately tailored and do not impose undue regulatory burdens.

Notwithstanding the foregoing, with respect to G-42(f), NAIPFA believes that additional guidance would be appropriate to clarify further the provision's use of the phrase "principal capacity." NAIPFA believes that it would be appropriate to specify that, for purposes of this section, the phrase "principal capacity" would include a party's activities as an underwriter of securities, remarketing agent, counterparty on swaps or other derivative transactions, or other similar capacity. In general, these kinds of relationships could conflict with the interests of municipal entities and obligated persons, and, therefore, such relationships should be prohibited in instances where the "principal" or an affiliate thereof also serves as the Municipal Advisor to such municipal entity or obligated person.

Comments to the Notice's General Questions

1. Fiduciary Duties to All Clients

As noted above, NAIPFA supports the imposition of a uniform fiduciary standard. Such a standard would further ensure the protection of the public interest.

2. Obligation to Review Official Statement

In general, NAIPFA believes that Municipal Advisors should be obligated to review the issuer's official statement. However, this review should be limited to determining whether appropriate disclosures have been made and must not obligate a Municipal Advisor to conduct an independent inquiry into the accuracy of such disclosures, unless the Municipal Advisor reasonably believes that any such disclosure is not materially accurate. In other words, absent information indicating that a disclosure may be materially inaccurate, Municipal Advisors should be permitted to conclusively rely upon the information provided by the issuer and, to the extent that the official statement is prepared by a third party, the information contained within the official statement.

3. Prohibition on Fee Splitting Arrangements

In general, NAIPFA is not opposed to prohibiting certain fee splitting arrangements. However, NAIPFA believes that a clear definition of "Fee Splitting Arrangement" should be developed prior to imposing any prohibitions. In so doing, NAIPFA urges the MSRB to recognize that a Municipal Advisor's utilization of independent contractors/subcontractors in connection with particular engagements should fall outside of any such definition.

4. Timing of Disclosures

Except as noted above with respect to a Municipal Advisor's reasonable estimate of its fee, NAIPFA believes that the timing of the provision of disclosures under the Notice is appropriate.

5. Required Acknowledgement of Conflicts

NAIPFA believes that it is appropriate to require Municipal Advisors, like underwriters and professionals possessing fiduciary duties, to obtain an acknowledgment from their clients. In this regard, we believe it would also be appropriate for such obligations to mirror those currently in place for broker-dealers under MSRB Rule G-17.

6. Disciplinary Events

To the extent that disciplinary events will be noted on any Form MA-I filed by the Municipal Advisor firm, additional disclosures seem superfluous and will place additional regulatory burdens on small Municipal Advisor firms in particular. Notably, there is no similar requirement imposed on underwriters, even though they do not possess fiduciary duties and arguably such disclosures would be more pertinent in such a case. As such, NAIPFA believes these disclosures will place Municipal Advisors at a significant competitive disadvantage.

7. Professional Liability Requirements

As discussed above, NAIPFA believes that both mandatory disclosures and mandatory professional liability insurance coverage will place IRMAs at a significant competitive disadvantage to broker-dealer firms. Such requirements will adversely impact the ability of small Municipal Advisor firms to compete for municipal advisory business. These requirements would also pose significant barriers to entry with respect to individuals and small groups of individuals wishing to form Municipal Advisor firms. In total, this will result in less competition and higher costs of issuance resulting not only from higher Municipal Advisor fees, but also from a simple lack of available advisors. In addition, municipal entities and obligated persons will be forced to rely more heavily on advice from underwriters, who do not possess fiduciary duties, thereby further increasing the costs borne by tax and rate payers.

Furthermore, it is important to note, again, that there are no similar disclosure or insurance coverage requirements in place for investment advisors or attorneys who also possess fiduciary duties. With respect to these aspects of G-42, the MSRB has determined to treat Municipal Advisors more like broker-dealers, who, for good reason, have capital requirements, than other parties who possess fiduciary duties. NAIPFA can find no rational basis for this. Therefore, neither the proposed rule's disclosure requirements nor the prospective imposition of mandatory professional liability insurance coverage are appropriate.

Finally, we anticipate that organizations representing broker-dealers will fully support the proposed rule. We also anticipate that these groups will support the imposition of mandatory liability insurance coverage. The imposition by the MSRB of mandatory professional liability insurance as discussed more fully below, or even insurance-related disclosures, may effectively eliminate small Municipal Advisor firms from the market, and we are concerned that the

underwriter community will support these requirements merely as a means of putting Municipal Advisors at a competitive disadvantage, if not out of business entirely.

8. Feasibility Study Reviews

MSRB Question #11 asks: "Should an advisor be required to review any feasibility study as a part of the information considered in its evaluation of whether a transaction it recommends is suitable for the client?"

NAIPFA believes it would be appropriate to enact a provision that requires Municipal Advisors to disclose to any client whether the scope of their engagement includes an obligation to review any feasibility study. Municipal Advisors who are engaged to review feasibility studies would have to conduct a reasonable review of any such feasibility study and make an assessment of whether the conclusions reached are in accordance with the best interests of their client. Municipal Advisors should not, however, be obligated to assess the assumptions made by a third party with respect to any conclusion made, unless such services are requested of and agreed to by the Municipal Advisor.

Comments to the Notice's Economic Analysis Questions

1. Should the MSRB Articulate the Duties or Measures to Prevent Breaches of a Municipal Advisor's Fiduciary Duty? If so, Does the Rule Address This?

NAIPFA strongly believes that the MSRB should articulate duties and prescribe means of preventing breaches of Municipal Advisor fiduciary duties. However, any duty articulated or means prescribed must be designed to prevent such breaches. As discussed above with respect to the liability insurance coverage, any disclosure that is not reasonably likely to cause Municipal Advisors to better adhere to their fiduciary duties or which relates to material conflict of interest should not be required. Where the disclosure does not reasonably relate to a Municipal Advisor's fiduciary duty, municipal entities and, if appropriate, obligated persons are not likely to receive any appreciable benefit from such disclosures. Rather, the increased burden and expense caused on Municipal Advisors by such disclosures as well as the barriers to competition erected will likely increase costs of issuance. Therefore, we would encourage the MSRB to look at any disclosure related rules primarily with respect to whether any such proposed rule will benefit municipal entities and obligated persons in terms of the quality of advice provided and whether such rule is appropriately tailored to minimize any potential increases in issuance costs resulting from such rules.

2. Questions #2 through #8

NAIPFA respectfully requests that Questions #2 through #8 be revised and resubmitted for response. We are simply not sure how to answer the questions posed. In particular, we ask that the MSRB articulate what it means by the term "baseline" within the various questions.

In general, however, NAIPFA believes that from an economic standpoint our member firms will judge the economic impacts of proposed regulations based on the two plus decades that many of these firms have been in existence. Again, during this time, our member firms have acted with fiduciary responsibilities towards their clients. The cost of their adherence to this duty has, until now, been minimal. Conversely, every regulation put in place costs Municipal Advisors money and increase costs of issuance. As such, we urge the MSRB to strongly consider this when imposing regulations.

Notwithstanding our economic concerns, we believe that appropriately tailored regulations are important. Therefore, NAIPFA proposes that rather than establish "baselines" for its economic analysis, the MSRB attempt to quantify its proposed rules in terms of dollars. The MSRB should then conduct a cost benefit analysis to determine if the potential benefits of any particular regulation outweigh the financial burden that such regulations would place upon Municipal Advisor firms, particularly, small firms, municipal issuers and obligated persons, and tax and rate payers.

3. Lower-Cost Alternatives to Requiring Disclosures of the Amount of Professional Liability Coverage

NAIPFA does not believe that this question is able to be answered effectively because it presupposes that a disclosure relating to professional liability insurance is appropriate. Notwithstanding this, NAIPFA believes that a lower cost alternative would be to require municipal advisors to provide such information as part of their annual MSRB renewal filing or upon their client's request. This would lower the overall compliance costs by decreasing the quantity of disclosures that a Municipal Advisor would otherwise be required to make on a per transaction basis. Requiring this disclosure in connection with Municipal Advisor annual MSRB renewals would also be consistent with the MSRB's goal of transitioning EMMA towards becoming a more non-industry centric platform for municipal securities related matters, including disclosure.

4. Will the New Standards Change the Quality of Advice Offered by Municipal Advisors?

These new standards will likely cause Municipal Advisors to incur additional costs due to compliance. This additional time and cost will put some strain upon small Municipal Advisor firms in particular, which could reduce competition. With respect to those firms who may be less impacted financially by these standards, NAIPFA does not anticipate that these regulations will have any appreciable benefit upon the quality of advice provided. Regardless, NAIPFA does not believe that this should be the goal of G-42. We believe that G-42 should be designed to protect the interests of Municipal Advisor clients. That being said, the advice Municipal Advisor clients have received has, for the most part, served them well. Therefore, NAIPFA believes that the MSRB should focus on ways to ensure that Municipal Advisors adhere to their fiduciary duties and to do so in as minimally burdensome of a manner as possible and not, within the context of G-42, necessarily focus on improving the quality of the advice provided but,

rather, ensuring that municipal issuers and obligated persons have access to and can accurately identify professionals who can provide high quality advice.

5. Will G-42 Affect the Willingness of Market Participants to Use Municipal Advisors?

Our member firms, as well as other Municipal Advisor firms, have acted with and advertised themselves as having fiduciary duties to their clients for many years. Municipal Advisors have also been required to act pursuant to a federal fiduciary duty to municipal entity clients since 2010. In addition, since the enactment of Dodd-Frank, NAIPFA is not aware of any law suits or regulatory actions that have been initiated relative to a breach of a Municipal Advisor's fiduciary duty. In light of the foregoing, we believe that if an increase in the use of Municipal Advisors arising from their fiduciary duties was to occur, that such an increase has likely already begun and will likely continue regardless of these rules. Therefore, we do not believe that proposed Rule G-42 will appreciably increase the use of Municipal Advisors.

6. Will G-42 Reduce Issuance Costs, Lead to Better Financing Terms, and Improve Capital Formation?

NAIPFA does not believe that these rules will achieve any of these objectives. The increased regulatory burden upon Municipal Advisors will likely lead to increased issuance costs. NAIPFA finds no reason to believe that proposed Rule G-42 will lead to better financing terms for issuers; again, Municipal Advisors have acted with a federal imposed fiduciary duty since 2010, at least with respect to municipal entity clients. Thus, capital formation, to the extent that it would have been impacted by a federal fiduciary standard, has likely already improved and will continue to improve with or without the imposition of proposed G-42, although this may be difficult to measure due to ongoing changes in market conditions.

7. Would the requirements of draft rule G-42 assist market participants in Municipal Advisor hiring decisions?

As discussed above, we believe that the disclosures that relate to material conflicts of interest will benefit municipal entity and obligated person decision making. Nonetheless, and as discussed above, some of the disclosures and other measures described within the proposed rule will not assist such decision making because such disclosures do not relate to the discharge of fiduciary duties. If municipal entities and obligated persons wish to receive information that goes beyond what is mandated by the MSRB, those municipal entities and obligated persons should be free to inquire into such other matters, and the MSRB should support this by requiring Municipal Advisors to truthfully provide such other information upon a client's request. The MSRB should be similarly supportive of contractual provisions between municipal entities and obligated person and their Municipal Advisors which extend beyond the requirements of G-42 and other MSRB rules. Again, this would strike the right balance in terms of creating effective regulation, minimizing regulatory burdens, and supporting client control over the issuance process.

8. Additional Costs Associated with Making and Preserving Books & Records

An analysis, economic-related or otherwise, with respect to any MSRB rule derived from a SEC Municipal Advisor rule is only necessary where the MSRB rule modifies the corresponding SEC rule, or where the MSRB rule relates to a matter that has not been addressed by the SEC. In all other instances, because the MSRB will be unable to vary the terms of any such rule, any exercise in an economic analysis of such rule's impact would seem to be of little value.

9. Effects on Competition, Efficiency and Capital Formation

If G-42 places a significant burden on Municipal Advisors, small Municipal Advisor firms could merge with other firms, retire or simply exist the market.[3] This will reduce competition, increase costs of issuance, and hurt capital formation, particularly in the small rural areas most in need of advice.

10. Barriers to Entry

We believe that a significant barrier to entry will be created as a result of the insurance-related disclosures. This barrier will only be exacerbated if the MSRB imposes professional liability insurance requirements upon Municipal Advisor firms. Currently, there is a lack of available insurance providers nationally who are willing/able to provide coverage for Municipal Advisors and, as of today, insurance is not readily available that will sufficiently cover the activities of Municipal Advisors. We have begun the process of identifying insurance companies which may be willing/able to cover Municipal Advisors; however, they are few in number. We have as of the date of this letter received an estimate of what this coverage may cost, which is as follows:

For a $1,000,000 aggregate claims policy for a firm of 1 to 4 professionals that carries both civil and regulatory coverage, the premium is estimated at $19,000 to $24,000 per year with a minimum deductible of $75,000; provided, however, that these terms can vary (presumably upward) depending on the risk attributed to the Municipal Advisor firm by the insurer. For small firms the premium alone may represent upwards of 10 to 15% of their annual gross revenue. Thus, if new firms were to try to enter the market, we believe coverage may be very difficult to afford or even acquire since such firms will have no operating history upon which the insurance provider could assess risk and may not have sufficient funds available.

11. Costs of Training & Compliance

The cost of training and compliance will depend upon the number of Municipal Advisor representatives each firm employs, but as the number of employees increases, so do the costs of

[3] Notwithstanding, NAIPFA is unaware of any discussions among firms regarding potential consolidations resulting from regulation. We find that it is more likely that firms, certain employees, and sole proprietors will predominantly choose to retire or not provide services as Municipal Advisors rather than attempting to carry on their work in an overly burdensome regulatory environment.

training and compliance. That being said, we believe on average that the cost of training and compliance will be approximately $2,500 to $4,500 per person, or, depending upon the firm, the equivalent of 5% to 20% of firm revenue annually.

Conclusion

NAIPFA believes that much of the Notice is acceptable. However, we also believe that revisions should be made in order to adequately regulate Municipal Advisors. Currently the proposed rules are overly broad in several key respects as noted above. The unnecessary provisions identified will place significant burdens on current and future Municipal Advisors, particularly IRMAs and even more so with respect to small firms, and will increase costs of issuance without achieving any appreciable benefit. Therefore, NAIPFA strongly urges the MSRB to consider revising G-42 in accordance with the foregoing comments.

Sincerely,

Jeanine Rodgers Caruso, CIPFA
President, National Association of Independent Public Finance Advisors

cc: The Honorable Mary Jo White, Chairman
The Honorable Kara Stein, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Michael Piwowar, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
Lynnette Kelly, Executive Director, Municipal Securities Rulemaking Board

Comments on MSRB G-42 Draft

General Matters

9. No Many of these entities will have policies in place that either require or don't require their vendors to have insurance and also specify the limits of the insurance. All of the parties to our transactions, including the buyers are represented by legal counsel.

10. Yes. For a small firm, which engages in 5-10 transactions, it would be a burden. For our firm, on every transaction, the obligated person and/or municipal entity are represented by legal counsel and the entire transaction is reviewed by a bond or note counsel. All of the investors in our transactions are banks who independently review the documents and are also represented by counsel. We are not a principal in the transaction. At $10,000 per year expense for liability insurance amounts to 2% of our gross income.

New York State Bar Association
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Business Law Section
Securities Regulation Committee

March 12, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Suite 600
Alexandria, VA 22314

Re : Regulatory Notice 2014-01
Request for Comment on Draft MSRB
Rule G-42, on Duties of Non-Solicitor
Municipal Advisors

The Securities Regulation Committee of the Business Law Section of the New York State Bar Association appreciates the invitation from the Municipal Securities Rulemaking Board ("MSRB" or "Board") in Regulatory Notice 2014-01 to comment on the MSRB's draft Rule G-42 (Duties of Non-Solicitor Municipal Advisors).

The Committee is composed of members of the New York State Bar Association, a principal part of whose practice is in securities regulation. The Committee includes lawyers in private practice and corporation law departments. A draft of this letter was reviewed by certain members of the Committee. The views expressed in this letter are generally consistent with those of the majority of members who reviewed and commented on the letter in draft form. The views set forth in this letter, however, do not necessarily reflect the views of the organizations with which its members are associated, the New York State Bar Association or its Business Law Section.

Introduction

As the SEC noted in the release adopting final rules for municipal advisors (SEC Release No. 34-70462[1])("Adopting Release"), citing the Senate report related to the Dodd-Frank Act, the

[1] www.sec.gov/rules/final/2013/34-70462.pdf.

municipal securities market has been significantly less regulated than the corporate securities market, and during the financial crisis a number of municipalities suffered losses from complex derivatives products marketed by unregulated financial intermediaries.[2] We support the efforts of Congress and the SEC to regulate those financial intermediaries as municipal advisors, and we generally support the Board's effort to impose standards of conduct on municipal advisors. However, we would like to use this opportunity to point out ways in which the proposed standards in draft Rule G-42 will have a disparate impact on different types of municipal advisors, and to suggest possible solutions.

The definition of "municipal advisor" in Section 15B(e) of the Securities Exchange Act of 1934 ("Exchange Act"), as interpreted by the Securities and Exchange Commission ("SEC"), encompasses a wide variety of persons and activities. At the core of the definition are persons that advise municipal entities on the issuance of municipal securities or act as intermediaries or finders between municipal entities and municipal underwriters.

But the definition also includes persons that advise municipal entities and obligated persons with respect to municipal financial products – municipal derivatives, guaranteed investment contracts and investment strategies. Investment strategies include plans or programs for the investment of the proceeds of municipal securities. Significantly, the SEC, in Adopting Release, announced changes to its interpretation of the term "investment strategies" such that the adviser to a collective pool that commingles proceeds of municipal securities with funds from other investors is a municipal advisor unless it is exempt as an SEC-registered investment adviser.[3] Fund advisers that will be required to register as municipal advisors if proceeds of municipal securities have been invested in their collective pools include banks and trust companies, which are excluded from the definition of investment adviser (and, therefore, not registered), state-registered investment advisers, exempt reporting advisers, foreign private advisers and advisers to real estate funds. We believe that the number of fund managers and advisers required to register as municipal advisors will be greater than the number estimated by the SEC for purposes of its Paperwork Reduction Act analysis.[4]

The definition of municipal advisor as interpreted by the SEC may also include other categories of persons who may not consider themselves to be in the business of acting as municipal advisors, including providers of guaranteed investment contracts and counterparties in municipal derivatives. If those persons provide advice about their products, in addition to selling them, they may be considered municipal advisors.

As discussed below, we believe that Rule G-42, as drafted, imposes requirements that do not comport with the businesses of some non-solicitor municipal advisors, and may conflict with or add unnecessarily to similar requirements imposed by other regulators. For that reason, we recommend that G-42 be re-proposed as a series of principles that can be applied by each municipal advisor in a manner appropriate to its business. In the alternative, if the MSRB determines to proceed with the Rule substantially as proposed, we recommend that it be revised

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2 Adopting Release text at n. 3.

3 Adopting Release, text at n. 398.

4 The SEC counted only state-registered investment advisers. See Adopting Release, n. 1621 and associated text.

to provide sufficient flexibility to allow municipal advisors to adapt the requirements of the Rule to their businesses.

Comments on Provisions of Draft Rule G-42

Duty of Care. Section (a) of the Rule imposes a duty of care on municipal advisors to clients that are either obligated persons or municipal entities. The elements of the duty of care are described in Supplementary Material .01. Among other things, a municipal advisor that is engaged by a client in connection with "a municipal financial product that is related to an issuance of municipal securities must also undertake a thorough review of the official statement for that issue, unless otherwise directed by the client and documented under subsection (c)(iv)" of the Rule.

Collective investment pools or funds may constitute investment strategies and, therefore, municipal financial products, if a municipal entity has invested proceeds of an issuance of municipal securities in the fund, even if the money invested by the municipal entity only represents a small percentage of the total amount invested in the fund by all participants. In our view, unless a municipal advisor that operates an investment fund has specifically advised a municipal entity investing in the fund with respect to a particular issuance of municipal securities included in the fund, the municipal advisor should not be required to undertake a review of the offering statement for the issuance of the municipal securities and should not be required to specifically obtain a reduction in the scope of its duties under subsection (c)(iv) for this purpose.

State and local retirement funds are significant investors in investment funds, including real estate investment funds and collective pools managed by banks or trust companies. The fund industry is awaiting advice from the SEC as to whether proceeds of municipal securities are deemed to be "spent," and thus no longer considered to be proceeds of municipal securities, when deposited in a state or local retirement fund. If proceeds of municipal securities are not deemed to be spent when they are deposited in a state or local retirement fund, then all future investments by such a retirement fund that has ever received the proceeds of municipal securities may be considered proceeds of municipal securities. We understand that some large state retirement systems also manage the money of local retirement funds. Such state systems may be unable to trace money that they have invested with privately managed investment funds to a particular issuance of municipal securities. In such circumstances, the municipal entity arguably would have no reasonable expectation that the fund manager's duty of care will include review of an offering statement. Thorough review of an offering statement should only be an element of the duty of care when the offering statement is relevant to the nature of the transaction for which the municipal advisor is providing advice.

Duty of Loyalty. Supplementary Material .02, which discusses the elements of the duty of loyalty, states: "[A] municipal advisor must investigate or consider other reasonably feasible alternatives to any recommended municipal securities transaction or municipal securities product that might also or alternatively serve the municipal client's objectives." We do not support this element of the duty of loyalty generally and as applied to specific types of businesses.

As a general matter, the duty of the municipal advisor to consider other reasonably feasible alternatives to a recommended transaction or product should apply only when it is within the explicit or implicit scope of the engagement, and not in other cases. Unlike Supplementary Material .01, Supplementary Material .02 does not permit an element of the duty to be carved out of the scope of engagement by direction of the client and documented pursuant to subsection (c)(iv). In many cases a municipal advisor's engagement may not, explicitly or implicitly, contemplate that the advisor will present to the client other reasonably feasible alternatives to a recommended transaction. Accordingly, we believe that client direction and documentation should not be required in any case where this element of the duty of loyalty is not within the explicit or implicit scope of the engagement.

The duty to consider other reasonably feasible alternatives is particularly inapposite where the municipal advisor is simply selling a product, and is not acting as advisor. Imposing a duty on a fund advisor selling a product to a municipal entity to investigate whether another fund or product would be a better alternative for the prospective investor would be inconsistent with the role of the fund advisor and with the expectations of the municipal client and would impose an unnecessary and inappropriate burden on the fund advisor. Similarly, sellers of GICs and swaps counterparties should not be required to investigate and recommend the products of other sellers or counterparties. Municipal advisors should not, of course, sell inferior or overpriced products or services to municipal entities, but that duty is different from the duty to investigate and propose to municipal clients other alternatives to their own products.

Application of Duties of Care and Loyalty to Fund Investors. Municipal advisors that manage or advise investment funds in which municipal entities have invested should not have a different or greater duty of loyalty or care to the municipal entities in the funds than their duties to other investors in the fund, in the absence of an agreement among the fund investors and the municipal advisor to the contrary.

Disclosure of Conflicts of Interest and Other Information. Section (b) of the Rule requires the municipal advisor, at or prior to the inception of the municipal advisory relationship, to provide the client with a document disclosing certain material conflicts of interest. When the municipal advisory relationship is the result of an investment by the municipal entity or obligated person in a fund managed or advised by the municipal advisor and including investments by other persons, the municipal advisor should be deemed to have satisfied this requirement by the use of an offering document provided to all investors and disclosing conflicts of interest that are relevant to fund investors generally.

We do not support a requirement that a municipal advisor with no material conflicts of interest provide written documentation to the client to that effect. In particular, we do not believe the Board should impose a requirement for a municipal advisor to list each of the categories of conflict and to state that there are none, or that there are none other than those listed. Absent any disclosable conflicts, the required disclosure would provide no meaningful information to investors. Moreover, were an advisor to provide a long, boilerplate list of potential conflicts, whether or not material, there exists a real possibility of over-disclosure and client confusion. We believe that clients are better served by a shorter list of material conflicts.

Documentation of Municipal Advisory Relationship. Section (c) requires a municipal advisor to "evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship" and prescribes what the writing must contain. In our view, a fund manager or adviser that provides offering material to investors in its fund and obtains executed subscription agreements or other organizational agreements should not be required to provide separate writings to fund investors that are municipal entities or obligated persons. Rule G-42 should permit the written documentation to contain information that is appropriate to an investor in the fund and not specific to a municipal advisory relationship.

In particular, the fund manager or adviser should not be required to (1) identify each investor in the fund that is a municipal entity or obligated person, (2) enter into a separate agreement with each municipal entity or obligated person or (3) assume obligations with respect to investors that are municipal entities or obligated persons that are different from the obligations to investors generally, except in the situation where the municipal advisor enters into a separate account relationship with a municipal entity or obligated person and recommends investment in a fund managed or advised by the municipal advisor as part of the client's overall investment strategy.

Recommendations. Section (d) discusses the suitability obligations of a municipal advisor making a recommendation to a client. We urge the Board to distinguish between a recommendation to invest in an investment fund and investment choices that are made by the adviser to the fund. The provisions of Section (d) should not apply to the investment choices made for the fund as a whole.

With respect to the decision to invest in the investment fund, the adviser to the fund should have a limited suitability obligation in cases where the municipal entity or obligated person is represented or introduced by a person with its own suitability or fiduciary obligation, such as a registered broker, a state or federally registered investment adviser or another registered municipal advisor. If the municipal entity or obligated person acknowledges in writing that it is relying on the recommendations of a qualified person and not on the recommendations of the fund adviser, the fund adviser should not be subject to the suitability requirements of section (d) or Supplementary Material .08.

Prohibition on Principal Transactions. Section (f) provides: "[e]xcept for an activity that is expressly permitted under Rule G-23, a municipal advisor, and any affiliate of a municipal advisor, is prohibited from engaging in any transaction, in a principal capacity, to which a municipal entity or obligated person client of the municipal advisor is a counterparty." We appreciate the purpose of this prohibition in situations where the municipal advisor is acting primarily in the role of adviser. However, the prohibition on principal transactions is not compatible with situations in which a person is deemed to be a municipal advisor by reason of providing a GIC or acting as a counterparty in a municipal derivative transaction. This may occur if the person's advice to the municipal entity is solely incidental to providing the product.[5] Section (f) should be amended to distinguish between situations where the municipal advisor is functioning primarily as an adviser and situations where it is acting as principal in a transaction

[5] The Rule G-23 exception does not address this issue.

with the client and providing advice only secondarily. At a minimum, the prohibition should not apply in situations where the client is advised by another municipal advisor in connection with the transaction.[6]

Specified Prohibitions – Payments to Others for Obtaining Business. Subsection (g)(v) prohibits "making payments for the purpose of obtaining or retaining municipal advisory business other than reasonable fees paid to another municipal advisor registered as such with the [SEC] and the Board for a solicitation of a municipal entity or obligated person as described in Section 15B(e)(9) of the Act." Section 15B(e)(9) by its terms does not require registration as a municipal advisor of an affiliated person that solicits on behalf of a municipal entity. In addition, in the Adopting Release, the SEC provided guidance that a broker-dealer that solicits municipal entities or obligated persons to invest in a fund advised by a municipal advisor or investment adviser is not a solicitor within the meaning of Section 15B(e)(9).[7] The exception in Subsection (g)(v) for payments to registered municipal advisors is, therefore, too narrow, because it would bar payments to broker-dealers and affiliated entities of the municipal advisor. Section (g)(v) should be amended to permit payments to (1) persons subject to a comparable regulatory regime, including banks, trust companies, broker-dealers and investment advisers and (2) affiliates of the municipal advisor, provided that, in either case, the payments are disclosed to the client.

Advantages of Principles-Based Rule

We would support a principles-based version of Rule G-42 that sets forth the requirements and prohibitions of the current draft Rule as principles rather than as prescriptive requirements, and requires municipal advisors to establish policies and procedures that address those principles in a manner that is appropriate to the municipal advisor's business. A principles-based rule would provide the flexibility to permit municipal advisors engaged in a broad range of businesses to adapt the principles in ways appropriate to those businesses.

Some registered municipal advisors are also subject to other regulatory requirements, including bank, broker-dealer and investment adviser regulation. In addition, the rules under the Employee Retirement Income Security Act (ERISA) are applicable to some registered municipal advisors -- for example, to managers or advisers to investment funds having municipal retirement systems as investors. For municipal advisors that are already subject to separate regulatory requirements that address the principles covered by Rule G-42, the Rule should deem compliance with the separate regulatory requirements to constitute compliance with the Rule, to the extent that both cover the same subject matter.

* * * * *

We are grateful for the opportunity to provide these comments on the draft Rule and for the Board's attention and consideration. We hope that our comments, observations, and

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[6] By analogy, see SEC Rule 15Ba1-1(d)(3)(vi), which excludes from the definition of municipal advisor a person engaging in municipal advisory activities in circumstances where the municipal advisor or obligated person is otherwise represented by an independent registered municipal advisor with respect to the same aspects of a municipal financial product.

[7] Adopting Release, text following n. 460.

recommendations contribute to the important work of the Board in carrying out the regulatory initiatives under the Dodd-Frank. We would be happy to discuss these comments further with the Board and its staff.

Respectfully submitted,

SECURITIES REGULATION COMMITTEE

By: /s/
Peter W. LaVigne
Chair of the Committee

Drafting Committee:

Peter W. LaVigne
Jeffrey W. Rubin

NORTHLAND SECURITIES

March 7, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Notice 2014-01 (January 9, 2014): Request for Comment on Draft MSRB Rule G-42 on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

On behalf of Northland Securities, Inc. (" Northland"), I am pleased to submit this letter in response to Municipal Securities Rulemaking Board ("MSRB") Notice 2014-01, regarding draft Rule G-42 ("Draft Rule G-42"). Let me begin by providing a brief profile of Northland Securities as context for our comments:

- Northland Securities is both a broker-dealer and registered municipal advisor.
- Northland provides debt issuance and management assistance to local governments primarily in Minnesota and Iowa. In addition, we provide a variety of other services including financial planning, economic development assistance and investment management.
- Northland serves as underwriter and placement agent working with obligated persons in the areas of housing, health care and higher education.
- We have long-term ongoing relationships with the majority of our local government clients. The nature of the relationship varies from client to client. For some clients, we act exclusively as a municipal advisor. Some clients choose to use Northland as both municipal advisor and underwriter, depending on the transaction. Finally, we also work with issuers that only use Northland as underwriter.

The remainder of this letter provides comments on specific aspects of the Draft Rule G-42.

Nature of Relationships

A critical issue for Northland is for Draft Rule G-42 (and all subsequent municipal advisor regulations) to support the transaction-based framework created by the Municipal Advisor Rule. A person acts as a municipal advisor in context of a specific transaction (issuance of municipal securities). This context defines our ability to operate within this regulatory framework. Each interaction with a client/issuer becomes one of the following:

1. Advice on the issuance of municipal securities provided as municipal advisor.
2. Advice on the issuance of municipal securities provided in the capacity other than municipal advisor pursuant to a stated exclusion in the Municipal Advisor Rule.

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Member FINRA and SIPC

3. General information (not advice) on municipal securities.

4. Other consulting services not related to advice on the issuance of municipal securities.

Framing service delivery in this manner helps to ensure that we clearly communicate our role to the issuer at the earliest opportunity and that we comply with the regulations that govern that role.

While the intent of Draft Rule G-42 appears consistent with this framework, the use of the term "relationship" blurs the practical application. Draft Rule G-42 uses relationship as a means of defining the municipal advisor activities. For example, under Documentation of Municipal Advisory Relationship, it states: "*A municipal advisor must evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship*." The practical challenge of applying the standard is that municipal advisor activities often occur within "relationships" between an issuer and an advisor that are both historical and ongoing. While the advisor's role within each transaction is defined, this is rarely thought about as a separate relationship. Draft Rule G-42 contributes to this confusion by using "maintenance of the municipal advisory relationship" under .09 Know Your Client.

An alternative would be to apply the approach for the Underwriter Exclusion in the Municipal Advisor Rule. To use the Underwriter Exclusion, a broker-dealer must be engaged as underwriter before providing advice. Applying this approach to Draft Rule G-42 would require the municipal advisor to be engaged prior to providing advice. This approach has several benefits:

- The approach fits cleanly with other aspects of the Municipal Advisor Rule. The same approach applies when that party is a municipal advisor or is acting in another capacity under the Municipal Advisor Rule.
- The issuer must make a conscious decision about the party providing advice in each instance. The disclosures required by the Draft Rule G-42, by MSRB Rule G-17 and by the Municipal Advisor Rule provide the issuer with critical information before engaging the party to provide advice. Without this distinction, the municipal advisor could claim that the relationship was not formed until after the initial advice was provided.
- This approach is consistent with the Disclosure and Documentation requirements in Draft Rule G-42. Information is required to be provided prior to or at the inception of the municipal advisory relationship. It seems desirable to require this information prior to providing advice, which is the activity that triggers the need for the disclosures in the first place.

Official Statement Review

The requirement for a thorough review of the official statement under .01 Duty of Care does not match the actual delivery of service in some market areas. The Draft Rule G-42 states that a municipal advisor "must also undertake a thorough review of the official statement for that issue, unless" the issuer limits the engagement to exclude this activity. This provision works when the official statement is prepared by a party other than the municipal advisor. In our

market, however, the standard practice is for the municipal advisor to prepare the official statement on behalf of the issuer. The requirement that a municipal advisor review its own work has little meaning.

The relevant requirement would be to extend the due diligence standards for underwriters to municipal advisors. Under the Duty of Care, a municipal advisor that prepared all or portions of an official statement would be required to attest to the due diligence used in this work. Useful guidance on this issue comes from the March 19, 2012 National Examination Risk Alert entitled "Strengthening Practices for the Underwriting of Municipal Securities". This document discusses effective practices for disclosure due diligence and supervision by broker-dealers. The same practices apply equally to municipal advisors. The Risk Alert notes that underwriters have the duty to review an official statement "with respect to accuracy and completeness of statements made in connection with an offering". A municipal advisor should be held to the same standard in both the review and preparation of official statement. Municipal advisors should also have the same supervisory obligations for disclosure review and preparation.

Recommendations

The Draft Rule G-42 proposes an appropriate standard of conduct for making recommendations about a municipal securities transaction. A municipal advisor should not recommend a transaction unless it has a reasonable basis for believing that the transaction is suitable for the client. The challenge in operating under the proposed Draft Rule is its prescriptive nature. The Draft Rule specifies items that the municipal advisor must discuss with its client including the evaluation of risks and benefits, the basis for suitability and the investigation of alternatives.

The scope of the recommendations requirement is unclear. The Draft Rule G-42 ties the requirement to entering into a municipal securities transaction or municipal financial product. There are a variety of municipal advisor activities that do not cross the threshold. An advisor may provide advice on the structure, terms and timing of an issue without recommending entering into a transaction. An advisor may provide advice on the investment of bond proceeds and material events disclosure without recommending entering into a transaction. If the intent is that the recommendations requirement applies to all recommendations, I do not think the proposed language in the Draft Rule achieves that result.

Additionally, the requirement may create areas of conflict between advisor and issuer. While the Draft Rule G-42 allows the advisor to "discuss" matters with the client, the need to document these discussions encourages the advisor to use written communications. This creates the potential for information from the advisor that conflicts with actions taken by the issuer. For example, an issuer may choose to use lease financing for a new facility when the advisor's explanation of alternatives shows that general obligation bonds produce the lowest cost debt.

An alternative approach would be the following:

"A municipal advisor must make a recommendation to a municipal entity or obligated person client related to the issuance of municipal securities or a municipal financial product unless the advisor has a reasonable basis for believing, based on the information obtained through reasonable diligence of the advisor, that the recommendation is suitable for the client."

This approach creates a standard for conduct while allowing flexibility in its application. This approach is similar to the concept of defining "advice" in the Municipal Advisor Rule. The determination would be based on the facts and circumstances of each situation.

Economic Analysis

We believe that Draft Rule G-42 should not include any exemption based on the size of a municipal advisory firm. Such an exemption would create a variety of problems. The municipal advisor registration requirements apply to all parties acting as municipal advisor. An exemption would create a class of registered advisors that are not subject to conduct, supervision and licensing requirements. Issuers would be required to distinguish municipal advisors that are registered, but not otherwise regulated. Economics is not sufficient justification to exclude a group of advisors. If issuers benefit from these regulations, then they should apply equally to all municipal advisors. Finally, an exemption would create financial inequities. Unregulated advisors would be able to charge lower fees without the overhead associated with regulatory compliance.

Liability Insurance

We agree with the proposed requirement that the municipal advisor disclose information regarding professional liability insurance (or the lack of) to the issuer. We do not, however, believe that it is appropriate or necessary for the MSRB to prescribe standards for such insurance. The issuer should have the ability to determine if liability insurance is needed and the related coverage. The MSRB may wish to consider creating issuer education material about this topic.

Thank you for the opportunity to provide these comments. Do not hesitate to contact me with any questions or the need for clarification. We look forward to continued participation in the rulemaking process.

Sincerely,

John R. Fifield, Jr.
Director of Public Finance/Senior Vice President

Comment on Notice 2014-01

from John Rodstrom, Oppenheimer & Co. Inc.

on Monday, March 10, 2014

Comment:

• The definition of “Advice” is very broad, and as such, a person or entity that proffers advice is deemed to be a Municipal Financial Advisor under Section 15B(e)(4)(A). A broker-dealer who seeks to be an Underwriter in our industry would be prohibited from soliciting a potential client with recommendations other than possibly a simple refunding recommendation. This limitation would have a “chilling” effect on our industry’s ability to seek new business. Under this broad interpretation, prospective underwriters would be severely restricted in their pitches to win new business – presentations would be solely based on the firm’s rankings, capital, experience, etc. I would propose that the definition exclude advice provided to a municipal issuer when not under an engagement. This way, governments would benefit from any idea submitted and could choose to evaluate it any way it deems appropriate. Why should government be restricted from receiving innovative structures and ideas that could save the public thousands, if not millions, of dollars?

• Municipal Financial Advisors’ compensation should not be determined on a per-bond basis. This type of compensation poses an inherent conflict because it directly incentivizes these advisors to recommend transactions, as opposed to advising against them. How can an advisor be impartial in its advice when it stands to not make any money if it recommends that a deal not be consummated? Also, an advisor would be incentivized to recommend a structure that produces a larger principal amount, since their fee would be directly tied to the issue size. Ironically, these incentives are identical to the ones characterizing underwriters, and underwriters have been forced to provide a specific disclosure pursuant to Rule G-17 stating that they are not acting in the client’s best interest because they are directly incentivized to do deals and to maximize their size. It’s completely inappropriate for a party with a fiduciary obligation to the municipality to be motivated by these same incentives

March 10, 2014

Ronald W. Smith

Corporate Secretary

Municipal Securities Rulemaking Board

1900 Duke Street

Alexandria, VA 22314

RE: MSRB Notice 2014-01- Draft MSRB Rule G-42 Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith,

Parsons Brinckerhoff Advisory Services, Inc. (PBASI) is a registered municipal advisor and appreciates the opportunity to comment on draft Rule G-42 as proposed by the Municipal Securities Rulemaking Board (MSRB). We provide these comments in response to specific questions and issues in the "General Matters" section of the proposed draft Rule G-42.

Fiduciary Duty

Draft Rule G-42 appropriately limits the application of the fiduciary duty to municipal clients. The extension of such fiduciary duty to obligated persons or all clients of a municipal advisor would exceed the scope of Dodd Frank's intent and the statutory mandate to regulate and oversee the relationship between municipal entities and their registered advisors.

Review of the Official Statement

A municipal advisor engaged by a client in connection with either an issuance of securities or a municipal financial product that is related to an issuance of municipal securities should not have a duty to review the entire official statement and should be permitted to limit the scope to those aspects of the official statement directly related to the scope of municipal advisory services.

If a requirement of review of the statement in its entirety is to be established, we request that the MSRB clarify the intended meaning of a "thorough review", as no definition or meaning has been provided and official statements include many distinct pieces of information which a municipal advisor would not independently be able to evaluate and verify. This language, without clarification, appears to create accountability for matters well beyond the scope of municipal advisory services.

Though it is often prudent for a municipal advisor to review an official statement in its entirety, the creation of a duty to perform a "thorough review" of the entire official statement would mandate work that is greatly redundant in many instances and adds no value to the client.

Disclosures of Legal and Disciplinary Events Related to Employees

A municipal advisor should not be required to disclose to a client legal and disciplinary events that relate to an individual that is employed by the municipal advisor if the individual is not a part of (or reasonably expected to be a part of) the advisor's team working for the client. With regard to any employee, forms MA and MA-I are public documents which include all such disclosures and are required to be kept up to date by all registered municipal advisors. We request that the MSRB consider that these publicly available forms should be deemed sufficient disclosure.

Liability Insurance

Coverage requirements and minimums should properly be determined and set forth by the issuer. The MSRB should not require professional liability insurance coverage be carried by municipal advisors. If such a requirement is set forth it would be inappropriate for the MSRB to specify the minimum amount and terms of such coverage. In response to the question posed by the MSRB, we do believe the cost of professional liability insurance would certainly be an undue barrier to entry for many current and potential municipal advisors.

Prohibition on Principal Transactions

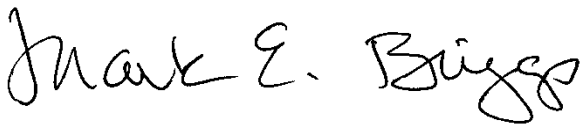
Municipal advisors and their affiliates should be permitted to engage in principal transactions with their client with full and fair disclosure and client consent. Draft Rule G-42's proposed prohibition on municipal advisor and affiliate entities engaging in principal transactions is based upon the a stated concern by the MSRB that the validity of client consent in such situations would be questionable, regardless of the amount of disclosure and potential conflicts of interests provided. We would argue that this is not the appropriate regulatory approach to principle transactions, that it is excessively paternalistic and without precedent in other fiduciary regulatory standards.

If the MSRB were nonetheless to impose such a rule on municipal advisors, it should not extend to their affiliates. To prohibit a municipal advisor's affiliates from engaging in principal transactions with a client would have the effect of shutting down advisory firms affiliated with larger companies who necessarily have to prioritize their ability to work with municipal clients in their core industry. This would have the unintended effect of reducing both competition and the diversity of expertise within the municipal advisor pool. The benefit of having created registration and regulation for municipal advisors is lost if all municipal advisors who are not strictly and solely financial advisors are pushed out of the field.

If such a burdensome prohibition against principal transactions is to be set forth, it should be limited solely to situations in which a municipal advisor is working for a municipal entity client to whom they owe a fiduciary duty.

We respectfully request your consideration of our comments and the issues addressed herein.

Sincerely,



Mark E. Briggs
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March 10, 2014

SENT VIA ELECTONIC MAIL

Mr. Ronald Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Arlington, VA 22314

Dear Mr. Smith:

I am pleased to submit this letter on behalf of Piper Jaffray in response to the MSRB's request for comment on proposed rule G-42 which specifies duties and responsibilities of municipal advisors as a follow up to the SEC's Municipal Advisor Rule.

I am responding as the Head of Public Finance for a firm that has a meaningful and varied public finance business where we serve many municipal issuers each year, including issuers of all sizes. We are among the leaders in both the number of senior managed underwritings that we complete each year as well as the number of issuers that we serve as a financial advisor. We also have significant specialty practices working with conduit borrowers including health care, senior living, higher education and other types of obligors. As a result, we bring a unique and broad perspective to the issues covered under proposed rule G-42.

General Perspective on the Proposed Rule

In general, we welcome regulation of financial advisors through the SEC's rule, particularly those who formerly were not part of any regulatory scheme, and believe that follow up with MSRB rules governing conduct standards and defining fiduciary duty is very appropriate. We would caution, however, that the SEC's approach in defining a "municipal advisor" in an activities based manner creates a level of complexity and change to what the market has historically considered a "financial advisor" which was based primarily on the role played in a transaction. As a result, we believe that the MSRB must be very careful in creating rules that govern the duties of "municipal advisors" in order to not create unintended consequences related to activities of various market participants.

Clearly what the market has considered a "financial advisor" would fit into the category of a "municipal advisor" but a "municipal advisor" includes many others as well. It could include a firm who typically seeks underwriting business who intentionally or unintentionally provides "advice" as defined under the SEC rule. It could also include a financial advisory firm who provides "advice" while seeking a financial

advisory assignment for which it is not ultimately selected. It could also include other professionals on a transaction who intentionally or unintentionally provide "advice" related to securities issuance outside the scope of their respective roles. It could also include a broker dealer who gives advice on the investment of bond proceeds but has no other connection to the issuance process. Our point is that this can get complicated and that influences some of our comments on the MSRB's proposed rule. Many of the requirements under the proposed rule only make sense for a "municipal advisor" who has actually been hired by an issuer to assist the issuer with a new issue transaction and do not make sense for a firm that has become a "municipal advisor" but is not actually engaged by or working with an issuer on a transaction.

Prohibitions on Principal Transactions

We have questions and concerns over section (f) of the proposed rule which prohibits principal transactions for a municipal advisor and its affiliates. First, it is confusing and unclear exactly what is meant by the phrase "except an activity that is expressly permitted under Rule G-23". Second, a blanket prohibition on all principal transactions for an entity and any of its affiliates is extremely broad and could include a wide variety of activities that have no connection to the matter on which advice was rendered. Third, and this gets back to the point that we made above, it makes no sense to extend any blanket prohibition of principal transactions to matters beyond the transaction where advice was rendered that made an entity a municipal advisor.

Here is an example of the confusion. Say our firm became a municipal advisor by inadvertently rendering advice related to a particular matter while seeking underwriting business (or in the alternative, say we became a municipal advisor when we rendered advice while seeking financial advisory business which we were not selected for and are not engaged on). Under the SEC's interpretive guidance, it would be inconsistent for our firm to then proceed to be an underwriter "with respect to an issuance of municipal securities" for which we gave advice and became a municipal advisor. The SEC's guidance limits our prohibition on conducting business as a result of a conflict to the particular issue on which the advice was provided and the conflict arose.

The MSRB's proposed rule potentially goes much farther which we do not believe is appropriate. And since in this example, although we gave "advice", we were never actually engaged by the issuer as a municipal advisor and there is no definitive end point under which our firm is no longer a municipal advisor to that issuer. In theory, under the MSRB's proposed rule, we could be banned forever from conducting any principal activities for this issuer who never actually engaged us. We are assuming that this is not what was intended.

We believe that a ban on principal transactions for municipal advisors only makes sense if the ban is limited to transactions on which the advice was rendered that made the firm a municipal advisor. This is consistent with the SEC's interpretive guidance and would prevent a long list of potential prohibited transactions that would unduly restrict an issuer's choice of service providers and impact any bank or broker dealer firm which provides municipal advice.

Obligated Persons

You are asking for input as to whether proposed rule G-42 should also extend the fiduciary duty of a municipal advisor "to its obligated person clients". We are not in favor of this extension for a number of reasons. Obligated persons consist of a wide range of different types of corporations, not for profits, limited liability corporations and other entities who have the ability to become obligors on municipal transactions. This potential wide base of "obligors" vary significantly in their make-up, legal structure, financial capabilities and regulatory requirements.

We believe that it becomes problematic to incorporate all of these entities into a rule for which, in our opinion, there is no particular need or, importantly, no particular want from these obligors. It also seems to be extending a potentially confusing rule beyond its legislative mandate. We have found that all of the potential obligors who we have spoken with, once informed of details of this rule and its potential consequences, are not advocates of being included in the regulatory scheme that has been created for municipal issuers. In particular, the limitations on flow of information from underwriters that would result from a fiduciary duty being placed on the activities based municipal advisor definition is problematic and would not be desired by these entities. Many of these "obligors" have complex transactional needs of which a municipal issuance approach is only one of a number of potential solutions. It would be inconsistent for an underwriter to be able to talk and give advice to an obligor related to several options for securities issuance but not be able to provide similar advice related to a municipal issuance approach.

We do not believe that it is wise to extend the fiduciary duty at this time to municipal advisors for entities who are beyond the Dodd-Frank legislative mandate (which was limited to protections for municipal issuers) and beyond the scope of the duties and outcomes created by the SEC under the Municipal Advisor Rule. At a minimum, we believe that the MSRB should consider this issue in more detail, get input from obligors and assure that all of the unintended consequences of whatever final rule is passed are determined before making any decision to extend the fiduciary duty of municipal advisors to obligors.

Documentation of a Municipal Advisory Relationship

The proposed rule calls for the documentation in writing of each municipal advisory relationship. While we have operated under Rule G-23 which requires a written agreement for a financial advisory relationship, our concern with the proposal under G-42 is that municipal advisory relationships are activity based and can be created when no on-going relationship with the municipal issuer exists. Again, consider the example of providing "advice" in the context of seeking municipal advisory business that our firm does not get selected for. In this instance, we would be deemed a "municipal advisor" to the issuer but it would make no sense to have a written agreement with the issuer. If this requirement for a written agreement is clearly limited to those instances where the issuer actually selects a firm to be its municipal advisor on a securities issuance, then we have no issue with the requirement of a written agreement and the requirements for that agreement listed in the proposed rule.

Obligations of a Municipal Advisor on Official Statements

You asked about whether a municipal advisor should have an obligation to "review thoroughly" the entire official statement for a client and whether this obligation could be limited by the scope of the advisor's engagement. On the second point, we clearly believe that a municipal advisor should be able to limit the scope of its engagement to certain activities as agreed upon with its issuer client and therefore be able to limit any obligation to assist the issuer in the review of the issuer's official statement. There will be many instances where an issuer engages its bond counsel or a disclosure counsel to assist with the review and preparation of its official statement. The issuer may simply desire to hire a municipal advisor in a limited capacity for certain elements of a transaction rather than be involved in all aspects of the issue.

We do believe however, that when a municipal advisor is engaged to have a role in assisting the issuer with the preparation or review of the official statement, then that advisor should have a duty to perform a reasonable review the official statement. This review should not rise to the level of a due diligence review of all of the content in the official statement but should be a more general review of content. The municipal advisor could be expected to have dialog with the issuer relative to assuring that the issuer understands its obligations relative to the official statement and understands what types of items the issuer should consider including as content relative to the transaction being undertaken. An advisor should not be able to contractually limit its engagement relative to the official statement but then still be the primary entity involved in assisting the issuer in the preparation of that document. It is important, however, that regardless of the role of the advisor in preparing the official statement that the issuer still have overall responsibility for the contents of that document.

Liability Insurance for Municipal Advisors

The proposed rule requires disclosure of the amount and scope of liability insurance of the municipal advisor. While we believe the ability of the municipal advisor to back its fiduciary duty with financial resources is something that an issuer should understand, we do have some comments on the rule as drafted.

As a broker dealer who has a significant amount of firm capital, we believe that disclosure for municipal advisors should start with the amount of capital that the firm has available. If a firm does not have capital or has capital below a set threshold (we would suggest $5 MM of excess net capital be the threshold level), then it should be required to disclose whether it has professional liability insurance and the amount and type of coverage.

We do believe that municipal advisory firms who lack a minimum threshold amount of capital should be required to carry some minimum amount of professional liability insurance. Issuers should clearly be aware through disclosure of the financial capacity of the firm they are engaging and should have some minimum financial protection backing the work of their advisor. We acknowledge that we do not know the costs, availability or consequences of requiring every municipal advisory firm not meeting a threshold capital requirement to purchase this insurance. It is possible that the availability and cost of this insurance could vary meaningfully over time.

Specified Prohibited Activities for Municipal Advisors

The draft rule has a list of specified prohibitions for municipal advisors. We have one technical comment and a couple of proposed additions to this section of the rule.

Under (g)(iv), there is a prohibition on "making any fee-splitting arrangements with underwriters". We agree that no municipal advisor should be able to make a fee-splitting arrangement with underwriters on any issue for which it is serving as a municipal advisor. However, our technical comment would be that this section needs to include language that limits the fee-splitting to advisory fees and does not inadvertently include any unrelated fee splitting that an underwriter would typically have as part of an underwriting agreement. We would assume that it is not your intention to prohibit our firm (a broker dealer) from serving as a financial advisor to a municipal issuer and then entering into an arrangement for another issuer (unrelated to our advisory engagement) where we are splitting fees with another underwriter. This would preclude us from being involved as an underwriter as part of any syndicate or entering into any agreement among underwriters if we are serving as a municipal advisor to any issuer. We are confident that this is not what is intended but therefore a limitation in the scope of this prohibition to the advisory fees on the transaction/engagement the advisor is serving on is required.

Additional Prohibited Activities

There are two "troublesome practices" that have concerned me over the years in our business that I believe based on the experiences that we have had should be added to the list of prohibited activities. The first is that it should be a prohibited activity for any municipal advisor to take into account whether it competes with other firms in its recommendations to an issuer about who they should hire as an underwriter.

As a broker dealer who does a meaningful volume of both underwriting and financial advisory work for issuers, we have had many instances in the past where other advisory firms have threatened us or told us directly that they would not allow their issuer clients to hire us as an underwriter because we compete with them for various advisory engagements. We had an instance recently where an advisory firm had an issuer send us a letter to drop us from their underwriting team the next day after we were hired as an advisor by another issuer who had formerly been a client of theirs. They had previously told us that they would do this if we proceeded to take on that assignment.

It should be clearly understood that this type of conduct by a municipal advisor does not meet the fiduciary standard spelled out under the duty of loyalty under the rule where the advisor must "act in the client's best interests without regard to the financial or other interests of the municipal advisor". However, because of the numerous instances that we have seen of this type of behavior and the directness with which many advisors have told us that they would consider competitive factors in advising their clients on selection of underwriters, we believe that this prohibition needs to be stated clearly in the rule as a prohibited activity.

My second request for an addition to the prohibited activities is relative to the use of the term "independent". This term has been used for a long time by many non-dealer advisors. The term

"independent" is used primarily to indicate to municipal issuers that a non-dealer advisory firm is free from conflicts. It is a term that is specifically used in an attempt to indicate that broker dealer firms who provide advisory business have an inherent conflict because they are a broker dealer and are involved in other types of activities related to the municipal market while the non-dealer advisor by not conducting these activities is purportedly free of conflicts and hence "independent".

Under the new rule G-42, the MSRB is defining the regulatory obligations of all advisors to disclose actual and potential conflicts when being engaged as a municipal advisor. We are supportive of this disclosure requirement. A broker dealer who serves as a municipal advisor may have certain "actual or potential conflicts of interest" which are required to be disclosed. Non-dealer advisors, many of whom provide a range of services to their issuer clients which could include such items as accounting services, feasibility analysis, fee-based money management products and executive search services will have to make their own determination as to which services present "actual or potential conflicts of interest".

As a result, we do not believe that it is appropriate for any firm seeking municipal advisory services to use the term "independent" in a manner that attempts to convey to potential clients that it does not have any potential conflicts of interest. Given the long history of the use of this term, we believe that a prohibited activity should be added that bans municipal advisors from using of the term "independent" in this context. In addition, the SEC municipal advisory rule creates a definition of the term "independent" for purposes of the IRMA exemption. The continued use of the term "independent" to connote freedom from conflicts would create confusion relative to the SEC definition of an independent advisor for purposes of this exemption.

Suitability

As a general matter, we are somewhat concerned about how to make suitability determinations as a municipal advisor as proposed under the rule. The language in Section .08 on "Suitability" describes an approach that appears to be focused on a municipal issue that is "product" based. There are some instances where an advisor is evaluating a particular product such as a variable rate demand bond, a SIFMA based floating rate note or a transactions that incorporates swaps where there are product characteristics that must be understood and evaluated relative to that issuer. In this context, the determination around "suitability" and the concept of assuring that the risks of a transaction structure are understood and appropriate for a particular client makes sense.

More often when serving as a municipal advisor, we find that issuer clients are not faced with a product suitability issue that is particularly complex but are faced with various issues and policy implications that may be very complex. The product that most municipal issuers utilize is a fixed rate bond issue which is typically relatively straightforward in terms of structure. However, there may be many complex policy issues that an issuer may deal with including such items as how much to borrow, how long to borrow, risks and consequences if the primary revenue source of the issue has a shortfall, and whether a project ultimately will have the benefits to the community that are expected among others. These policy determinations may make sense to the decision makers at the time of an issue but be subject to questioning after the transaction has been completed.

As an advisor we are often asked to comment on these types of items but a transaction based "suitability" determination on these types of policy issues is very difficult to make and cannot be made outside the policy directives of the issuer. We believe that the rule should either limit the requirement of a "transaction" based suitability determination or have more specificity on what it means to make this type of determination. The rule should make clear that this determination can incorporate the policy directives and decisions of the issuer at the time the issue is undertaken.

Feasibility Studies

In one of your questions you ask whether an advisor should be required to review any feasibility study that is part of a transaction. We believe that an advisor should only be required to review the feasibility study if this is part of the advisor's contractual duties as agreed to with the issuer or is necessary as part of the advisor's ability to meet the suitability determination for the issue. We do not believe that a financial advisor should generally have a duty to review every feasibility study or to become an expert on evaluating these studies particularly if the study is related to a complex project for which an expert was selected to provide the study. This would be analogous to requiring a municipal advisor to have the expertise to review and question the legal reasoning behind an opinion an issuer receives from a bond or tax counsel.

Economic Analysis

We are not completely familiar with the process for completing an economic cost benefit analysis related to proposed rule G-42 and therefore will limit our comments on this matter. We would like to comment on a statement and request that you have made relative to being sensitive to the impact of the rule on smaller municipal advisory firms. While we understand that it is not your intention to impact the competitive landscape as a result of your rulemaking, we strongly believe that smaller municipal advisory firms should not receive any exemptions from or different treatment under the rule.

While many smaller firms provide solid advice, there are a number of smaller firms or sole practitioners who do not have strong capabilities, possess limited resources and do not provide advice that meets the standards that the industry should expect and that you should require. Some of these firms and advisors and their practices were exactly what Congress was targeting when the Dodd-Frank bill was passed to regulate municipal advisors. Smaller broker dealers do not get any exemptions from rules on dealers and smaller advisors should still need to comply with all of the advisory rules.

Our other comment is relative to your assumption that any increase in municipal advisor fees would be "minimal". We believe that the added requirements of the rule, particularly the added care that advisors must take relative to recommendations and suitability determinations and the additional recordkeeping requirements, will result in added costs to issuers. While it is difficult to quantify the amount of this fee increase, we believe that this cost will be more than minimal over time.

Summary

We hope that we have provided some helpful thoughts and context relative to your request for comments on proposed Rule G-42. We strongly suggest that you consider our thoughts on these matters. In particular, you should assure that you are fully recognizing the complexities of the SEC's activity based definition of a municipal advisor when finalizing the approach to Rule G-42 so that you do not create unintended consequences relative to this new and complex SEC rule that we are still all working to fully understand.

Sincerely,

Frank Fairman
Managing Director
Head of Public Finance Services

The PFM Group
Public Financial Management, Inc.
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March 10, 2014

Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314
Attention: Ronald W. Smith, Corporate Secretary

Re: Request for Comment: MSRB Notice 2014-01

Draft MSRB Rule G-42 Duties of Non-Solicitor Municipal Advisors

Dear MSRB Board Members and Staff:

Although the Municipal Securities Rulemaking Board ("MSRB") in the captioned draft MSRB Rule G-42 ("Rule G-42") has given interested persons an opportunity to submit comments, Public Financial Management, Inc. ("PFM") believes that the implementation of Rule G-42 in its current form will substantially improve the municipal marketplace. This is realized by formalizing the issuer protections which reputable, qualified and independent Municipal Advisors provide, enhancing the clarity of the regulation supporting the role of the Municipal Advisor in municipal securities transactions, and prescribing certain conventions of the issuer - Municipal Advisor relationship. For PFM's part, unless the perfect is to be allowed to become the enemy of the good in securities regulation, Rule G-42 should be allowed to become effective.

PFM anticipates that the thousands of issuers of municipal securities present such a vast range of circumstances associated with the issuance process that the MSRB's determinations about a Municipal Advisor's satisfaction of Rule G-42 will necessarily rely on the facts associated with each issue and the Municipal Advisor's demonstrated ability to perform fiduciary responsibilities to the issuer. It is the unqualified, resource-constrained and conflict-ridden Municipal Advisor who should be very concerned about complying with Rule G-42, whereas qualified and appropriately resourced Municipal Advisors should not have such concerns and this can help strengthen the municipal marketplace.

The MSRB has asked many questions in its Request for Comment on Draft MSRB Rule G-42. PFM respectfully offers the following comments for some of the topics addressed by the MSRB's questions and the central features of the draft Rule G-42:

1. A qualified Municipal Advisor should have no hesitation in serving as a fiduciary to all of its clients, issuers and obligated persons alike.

2. It is difficult if not impossible for a Municipal Advisor to properly serve its client when advising on the issuance of municipal securities without reviewing the official statement and related or referenced transaction materials. While independent verification of all of the information in the official statement is not practical or necessary for a Municipal Advisor to fulfill its fiduciary duty to the issuer, the scope of the Municipal Advisor's engagement with the issuer needs to be sufficient to make the Municipal Advisor's review of the official statement relevant.

3. Compensation received by a Municipal Advisor and any allocation of fees among joint ventures and Municipal Advisor teams should be clearly disclosed to the issuer; there is no reason for an issuer to accept anything less than full disclosure and documentation of all fees associated with a municipal securities transaction.

4. Conflicts of interest are not always knowable at the outset of a municipal securities transaction, but once any become known, the Municipal Advisor as well as any other participant to the transaction should disclose any such actual or potential conflict(s). Principal transactions in securities should not be permitted and the prohibition should apply to Municipal Advisors with or without a fiduciary duty to the client.

5. Given the wide range of experience, capabilities and legal structures among Municipal Advisors, professional liability insurance should be required to adequately protect issuers from the mistakes of their Municipal Advisors. Reputable Municipal Advisors with the resources required to properly advise issuers and obligated persons should readily purchase such coverage and issuers should question any advisor who is unwilling to provide such protection for its client.

6. The regulation of upholding a fiduciary standard and duty of loyalty within the registered Municipal Advisor community requires increased communication, clarity and formality amongst all parties engaged in municipal security activities on behalf of an issuer. In particular, the obligation to know one's client and provide suitable advice proves paramount in facilitating an efficient and effective transaction on behalf of a client. Evidence of knowing your client's circumstances and the corresponding offering of suitable transactional advice cannot be prescribed, and should, as Rule G-42 intends, rely instead on the particular facts or circumstances and the principles of reasonable care, inquiry, and diligence.

7. Rule G-42 will itself establish, and also advocates overall for, numerous areas of compliance implementation which undoubtedly represents additional occasion for interpretation of these provisions, the internal business or external transactional implications, and the corresponding Municipal Advisor professional standards. The Municipal Advisory profession will appropriately develop in accordance with the final SEC regulations and MSRB rules with a continual focus on the best interests of their issuer clients.

As always, we would welcome the opportunity to discuss these comments or otherwise assist the MSRB in finalizing draft Rule G-42 or any other feature of the Municipal Advisor regulations that hold the promise of bringing clarity, fiduciary standards, and additional protections to municipalities and non-profit institutions.

Respectfully submitted,

John H. Bonow
Chief Executive Officer

cc: Daniel Heimowitz, Chair
Municipal Securities Rulemaking Board

Lynette Kelly, Executive Director
Municipal Securities Rulemaking Board

Ernesto Lanza, Deputy Executive Director
Municipal Securities Rulemaking Board

Gary Goldsholle, General Counsel
Municipal Securities Rulemaking Board

Michael Post, Deputy General Counsel
Municipal Securities Rulemaking Board

Kathleen Miles, Associate General Counsel
Municipal Securities Rulemaking Board

John Cross, Director of Municipal Securities Office
Securities & Exchange Commission

PRAG

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PUBLIC RESOURCES ADVISORY GROUP

March 10, 2014

Public Resources Advisory Group appreciates this opportunity to comment on draft Rule G-42 proposed by the Municipal Securities Rulemaking Board (MSRB). Our comments are included below.

1. With regard to your General Matters, Question 2, and Supplementary Material .01
   You have asked whether we agree that an advisor has an affirmative obligation to thoroughly review the entire official statement. The proposed rule sets thorough review of the official statement as a standard. While our advisory services usually include review of the official statement, from time to time clients do ask us to restrict our scope to certain prescribed tasks. Furthermore, whether or not we do review the official statement and irrespective of the level of our review, we do not always have the appropriate access to information to determine whether or not disclosure is adequate, appropriate and complete as that responsibility is with disclosure counsel or the issuer. We suggest that responsibilities with regard to the official statement be set forth in the documentation of the engagement between the advisor and the client and a thorough review should not be the presumption.
2. With regard to your General Matters, Question 4, and Section b(vi).
   The proposed rule requires specific disclosure of any conflict of interest that results from the method of compensation. In the hands of an unscrupulous advisor a conflict can result from any payment. Inclusion of this disclosure will result in the same kind of boilerplate disclosure that has characterized compliance with G-17. Disclosing the obvious does not improve disclosure.
3. With regard to your General Matters, Question 11.
   You have asked if the advisor should be required to review any feasibility study as part of the information considered in its evaluation of whether a transaction it recommends is suitable. We believe that this task should be performed if it is included in the scope of services.
4. Additional comments
   a. Section (c)(ii) of the proposed rule requires the advisor to document, in writing, the expected amount of compensation. Further language in the proposed rule requires that this written information be updated any time there is a material change in the compensation expected to be realized. With new clients, the amount of work to be performed is often unknown, and with existing clients tasks and scope can change quickly. We recognize that the language in the proposed rule includes the qualifier, "if known", but we think this language will create an undue burden with excessive amounts of time devoted to projecting expected billing amounts.
   b. Section g(i) of the proposed rule prohibits "compensation that is excessive in relation to the municipal advisory activities actually performed". As has been noted by other commenters, it is common practice for municipal entities to pay transaction based fees for services. In some circumstances the transaction fees are meant to compensate the advisor for other activities unrelated to the specific issuance or reoffering of municipal securities in connection with which the fee is being paid. Is this practice permitted?

Please let us know if we can provide additional information or clarification.

Sincerely,
Thomas Huestis

Comment on Notice 2014-01

from Lex Warmath, Raftelis Financial Consultants, Inc.

on Monday, March 10, 2014

Comment:

Please see attached.

1 file(s) uploaded successfully.

Questions for Draft MSRB Rule G-42.docx

Draft MSRB Rule G-42 on Duties of Non-Solicitor Municipal Advisors
Comments and Questions

Background Information and Context:

Our firm provides financial planning and rate consulting services primarily to government-owned water, wastewater and storm water utilities. This assistance includes developing financial planning models that provide forecasts of utility revenues and expected financial results, particularly as these results are impacted by various capital planning and debt financing strategies and alternatives. This information often includes general assumptions related to funding sources to meeting capital investment needs, including various forms of borrowing. In addition, our firm is often engaged to provide financial forecasts and supporting documentation, in the form of a financial feasibility study report, for a particular debt issue or borrowing, and these reports are typically included as a component of the Official Statement for revenue bonds, or as a component of the applications and formal documentation required for private placement loans or applications for State Revolving Fund Loans and other types of borrowing.

Our interpretation of the rules and regulations related to Municipal Advisors, both adopted and proposed, as they relate to the general financial planning and rate studies that we provide for government-owned utilities, is that this level of assistance may, or may not, fall under the regulations for a Municipal Advisor. For example, in some studies our revenue forecasts may be based on assumptions for the timing of capital expenditures, including the timing, amount and terms of future bond issues developed internally by the client, or by other advisors engaged by the client. In other studies, the forecast is more general and does not address specific borrowing assumptions and is similar to the general forecasts of demand and capital investment needs that might be developed by an engineering firm as part of a master planning engagement or similar type of study; and that are excluded from the activities that constitute Municipal Advisory services. In other cases, our scope of work may include developing assumptions as to the amount, timing and terms for future bond issues as a component of a more comprehensive financial plan, which would be more likely to fall under the definition of Municipal Advisory services.

However, for any engagement related to a specific bond issue, loan, or borrowing, we believe our services and role clearly does fall under these regulations and we have been registered as Municipal Advisor since the new guidelines and regulations were first proposed. Although we do not provide specific recommendations with respect to the structure, timing, terms and other similar matters concerning a specific financial product or loan, we do incorporate this type of information, as provided by the client's Financial Advisor or underwriter, into our models and forecasts. The resulting impacts on customers, rates, financial results and debt service coverage, as generated by our financial forecast models, may then be used by the issuer and their other financial advisors to adjust or fine-tune the terms of the loan to provide a more feasible and acceptable plan for financing the necessary capital investments. In other words, although we do not provide specific recommendations on the structure, timing, terms and other similar matters, we do participate with the other members of the financial advisory team (including the Financial

Advisor, underwriter, underwriter's counsel, bond counsel, municipal attorneys, and other members of the issuer's staff and/or governing body) to help structure the borrowing to meet a broad range of financial planning objectives. As an integral part of these types of engagements, we consider ourselves to have a clear fiduciary duty to the municipal entity, including a duty of loyalty and care.

Questions and Comments:

1) We recognize that our interpretation of the rules and regulations affecting Municipal Advisors may not be consistent with the intent of the MSRB and SEC. In particular, we are concerned that since most of our financial planning models include assumptions related to future borrowing needs, including the expected timing of the loans and assumptions related to the term and interest rates that may be applicable, that almost all of our financial planning studies might fall within the definition of Municipal Advisory services. In many cases, the assumptions used are not particularly detailed and are not represented as terms that could actually be secured for a loan, but are intended only to provide a reasonable basis for general planning and to assist in the evaluation of different capital investment plans and funding sources to address those plans. In some cases this information may never be used to support the issuance of debt. In other cases, this information may be updated to include the terms and conditions for a specific bond issue and included in a formal feasibility study, as described above, as part of a separate and distinct engagement to provide assistance with issuing a specific bond or loan. In some cases, the forecast provided by our financial planning models may be used as part of the documentation supporting a loan application without any adjustment to reflect the particular structure of a proposed loan. Since the financial planning models we develop become the property of our clients, the forecasts generated by the models may be included as part of an official statement or other loan documentation without our involvement or even our knowledge and consent. In this case, the forecast would be represented as having been prepared by the municipal entity, and not by our firm.

   In other words, we have tended to make a distinction in our interpretation of the Municipal Advisor rules that financial forecasts developed as part of a broader financial planning engagement would not fall under the regulations for a Municipal Advisory Relationship; whereas engagements related to a specific bond issue or financing involving preparation of a financial forecast as part of a bond feasibility study would fall under these regulations. Clearly, based on the guidance provided so far, there is much room for interpretation and a lot of gray areas that need clarification. Any information you can provide to help address this concern or to identify specific circumstances or conditions where the Municipal Advisor rules would apply would be useful. This determination has significant implications for the disclosure requirements and other aspect of the draft Rule G-42, as discussed below.

2) Comments related to Section (c) - Documentation of Municipal Advisory Relationship:

   If our interpretation of the Municipal Advisor regulations is appropriate, then it would not be difficult to address and comply with the requirements specified in this section. Our intention is to develop a specific document, for acknowledgement by each client, to address most of the requirements outlined in this section as part of any engagement to provide debt

issuance support or a bond feasibility study associated with a particular loan or financing. However, if it becomes evident that a Municipal Advisory Relationship is deemed to exist for a significant majority of our ongoing engagements to provide general financial planning and rate setting assistance, this requirement would become significantly burdensome. At any one time, our firm might be engaged in as many as 50 to 75 active projects that would fall into this category and reporting and updating this information would be time consuming and provide little or no value to an individual client. Requirements to provide information on the form or basis of compensation and the reasonably expected level of compensation would be problematic since the scope of work included in the various types of projects that might be included under this broader interpretation can vary significantly, with comparable variations in the level of compensation.

In comparison, active engagements to provide debt issuance support or bond feasibility studies associated with a specific loan or financing would typically include fewer than 10 engagements. These projects typically have a fairly limited and clearly defined scope of work and related costs that would be easier to document and update. To this point, we would also include language in our written documentation to define the scope and limitations of the engagement that clearly states that once the debt has been issued and all documentation for the specific financing has been completed, that our role as a Municipal Advisor would be complete and terminated (per section (c)(vi)), even if we remain actively engaged in providing other services to the same client. Only in this way will it be possible to meet the reporting and disclosure requirements outlined in this section. We believe this to be an appropriate approach since by the nature of the services we routinely provide, we always maintain a fiduciary duty to our clients, including a duty of loyalty and care, regardless of whether a Municipal Advisory Relationship is currently in effect.

Response to specific questions listed in the Regulatory Notice (pp 15-16):

1) No comment.

2) We believe that a Municipal Advisory should be allowed to limit their responsibility to review the official statement. Since our firm does not include attorneys, it would not be appropriate to opine on most of the information in an official statement. We would seek to limit our responsibility to reviewing the financial feasibility report (usually included in a separate appendix) and any sections of the official statement that addressed information relevant to the financial feasibility report, such as descriptions of the utility system; planned capital improvements; forecasts or projections of revenues, coverage, rates, customer demand and demographics; rate structure information and proposed rate adjustments; coverage requirements and the additional bonds test; comparisons of utility costs and rates to other jurisdictions; and other similar and related information.

3) Generally we believe Rule G-42(c)(vi) would have this effect and would benefit the municipal entity.

4) We agree.

5) Not applicable to our firm.

6) We agree.

7) No opinion, although it is our intention to request a written acknowledgement that addresses this issue.

8) Yes.

9) Yes, we believe professional liability insurance should be required, but the amount of that insurance should be determined by the municipal entity, not the MSRB.

10) No comment.

11) Similar to our position that it is not beneficial to the municipal entity to require all Municipal Advisors to review the entire official statement, it may not be beneficial to require all Municipal Advisors to review the feasibility study. But the same type of written acknowledgement that this was not part of a particular Municipal Advisors scope should be required.

12) Not applicable to our firm.

13) No comment.

sifma
Invested in America

March 10, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors; MSRB Regulatory Notice 2014-01

Dear Mr. Smith:

The Securities Industry and Financial Markets Association ("**SIFMA**")[1] appreciates the opportunity to provide comments on the Municipal Securities Rulemaking Board ("**MSRB**") Regulatory Notice 2014-01 (the "**Regulatory Notice**") containing a draft proposal for MSRB Rule G-42 ("**Proposed Rule G-42**") on the standards of conduct and duties of municipal advisors when engaging in municipal advisory activities other than the undertaking of solicitations.

I. Executive Summary

SIFMA supports the MSRB's efforts to develop a framework for the regulation of municipal advisors, including the establishment of standards of conduct and duties of municipal advisors. However, SIFMA has significant concerns regarding Proposed Rule G-42. In particular:

- Proposed Rule G-42 would improperly impose, in effect if not in name, a fiduciary duty on municipal advisors providing advice to obligated persons. SIFMA opposes the imposition of a fiduciary duty on this relationship between private parties. Such a duty would be contrary to Congressional intent, unnecessary for the protection of obligated persons and extremely burdensome.

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

- SIFMA also opposes the proposed blanket prohibition on principal transactions between a municipal advisor with either municipal entity or obligated person clients. The proposed prohibition, as drafted, is unworkable, unnecessarily broad and does not balance the interests of municipal entities. A fiduciary duty—which only applies in connection with advising municipal entity clients—does not necessitate a complete prohibition on transacting as principal, and such a prohibition clearly has no application to non-fiduciary advice provided to obligated persons.

- The fiduciary duty should be limited to the specific transaction or matter as to which a municipal advisor gives advice and not broadly extended to all potential dealings between the parties.

- Extending the fiduciary duty to affiliates is not necessary and is highly burdensome where affiliates engage in unrelated transactions. Many large financial institutions have investment affiliates that are completely separate from their municipal advisor, and their activities should be treated as being separate.

- The documentation and disclosure requirements under Proposed Rule G-42, in several instances, are inappropriate outside of the context of a municipal advisory relationship relating to an offering of municipal securities. However, as proposed, these obligations would apply, inappropriately, to all municipal advisory relationships, which could include, for example, incidental advice in connection with brokerage or other investment activities.

- In many cases, Proposed Rule G-42 is unnecessarily prescriptive—forcing municipal advisors to provide, and their clients to bear the cost of, services that the client may not have an interest in receiving. Rather, the MSRB should make clear that municipal advisors and their clients are free to agree to limit the services provided and duties undertaken.

- As discussed in Section II below, SIFMA believes that it would avoid confusion and promote compliance if the MSRB were to propose several separate and distinct rules that establish the duties of a municipal advisor depending upon whether the client is advising a municipal entity or an obligated person, and whether the advice is in connection with an offering of municipal securities or relates to investments (such as advice incidental to brokerage or banking services pertaining to the proceeds of a municipal securities offering).

Finally, while SIFMA applauds the MSRB's new policy on the use of economic analysis in its rulemaking, and its request for comment on its economic analysis on Proposed Rule G-42, SIFMA believes that the MSRB's draft economic analysis fails to meet the MSRB's statutory mandate and its own stated policy. Moreover, to be effective

in the specific case of Proposed Rule G-42, the MSRB's economic analysis should focus at a much more granular level on the benefits and burdens of each specific proposed requirement, as applied to the full range of covered activities and market participants. A further discussion of SIFMA's views regarding the MSRB's draft economic analysis contained in the Regulatory Notice is contained in Annex A to this letter.

II. Scope and Structure of Proposed Rule G-42

As a general matter, SIFMA has concerns regarding the manner in which, with narrow exception, Proposed Rule G-42 would create a "one-size fits all" set of duties and obligations for municipal advisors that may not (i) align with the actual legal duties that apply or (ii) be appropriately tailored to the type of advisory activity involved. As the Securities and Exchange Commission ("**SEC**") made clear in the release accompanying its adoption of final municipal advisor registration rules (the "**Final MA Rules**"),[2] a wide range of activities could potentially trigger municipal advisor status. Structuring a single rule that addresses the different duties in each different relationship and advisory assignment will ultimately be both over- and under-inclusive and not well-tailored to the activity being regulated.

Instead, SIFMA believes that the MSRB should adopt separate rules that appropriately set out the particular duties and obligations of a municipal advisor that apply in each context. As a starting point, different duties and obligations should be established depending on whether the municipal advisor is providing advice: (i) to a municipal entity in connection with a municipal securities offering; (ii) to an obligated person in connection with a municipal securities offering; (iii) to a municipal entity in connection with other activities, such as giving advice in connection with brokerage or banking services relating to the investment of the proceeds of an offering; or (iv) to an obligated person in connection with other activities, such as giving advice in connection with brokerage or banking services related to the investment of the proceeds of an offering.

In addition, the MSRB should consider applying certain of its rules somewhat differently depending on the level of sophistication of each client, including the size and complexity of the municipal entity or obligated person (*e.g.*, whether they are applied to advice given to large issuers with experienced staffs or advice given to small issuers with volunteer boards and officials). For example, an obligated person that is a sophisticated public company (*e.g.*, a publicly-traded airlines operator) should be distinguished from a significantly smaller type of obligated person (*e.g.*, an operator of a single private nursing home). We observe below several places where the MSRB might consider this approach.

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[2] *See* Registration of Municipal Advisors, Exchange Act Release No. 34-70462, *available at* https://www.sec.gov/rules/final/2013/34-70462.pdf (the "**Adopting Release**").

Many of SIFMA's concerns discussed in this letter could be addressed through a more precise rule framework that better matches the duties and obligations to the type of municipal advisory relationship to which it applies.

III. Comments on Content of Proposed Rule G-42

A. Principal Transactions

Proposed Rule G-42(f) would impose an absolute[3] prohibition on a municipal advisor or any of its affiliates engaging in any transaction in a principal capacity with a municipal entity or obligated person client whether or not the principal transactions relate to the municipal advisor relationship.

1. The Proposed Principal Transaction Prohibition Should be Clarified and Narrowed

If the MSRB determines to retain the outright prohibition on principal transactions, it should clarify and narrow its scope, including by defining when a person's involvement in a transaction is in a "principal capacity."

(a) Application to Matters Unrelated to the Municipal Advisory Engagement

Any restriction on engaging in principal transactions should be limited to the specific transaction or matter as to which the municipal advisor is providing advice, rather than applying broadly across any and all unrelated activities of the municipal entity or its affiliates. The MSRB accepted this premise in connection with its earlier proposed interpretation of a municipal advisor's fiduciary duty to municipal entity clients, where it more appropriately proposed to prohibit acting as principal *only* "in matters concerning the municipal advisory engagement."[4] Similarly, the SEC staff, in providing guidance in the form of responses to Frequently Asked Questions, indicated its expectation that any fiduciary duty (and resulting restrictions on principal transactions) would apply only "with respect to that issue" on which the municipal advisor is engaged to provide advice, not unrelated matters.[5]

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[3] While SIFMA refers to the proposed prohibition on principal transactions as "absolute," we acknowledge that Proposed Rule G-42 includes an exception for activity "expressly permitted under Rule G-23." As discussed in Section III.A.1(c) below, SIFMA requests guidance regarding what would be permissible under this exception.

[4] MSRB Notice 2011-48 (Aug. 23, 2011).

[5] *See* Final MA Rule FAQs at Question 5.2.

As drafted, the proposed prohibition is unbounded; unrelated businesses and affiliates of a financial institution would be swept into the principal transaction prohibition for unrelated transactions. Such a universal prohibition divorced from the context of the advisory relationship would not serve any useful policy objective and would deny a range of services to clients and would be unworkable in practice. If a municipal advisor and all of its affiliates were prohibited from engaging in any principal transaction with the municipal advisor's client, regardless of the nature of the transaction and connection to the advisory engagement, many multi-service financial institutions might determine that the business that must be given up in order to act as a municipal advisor could not economically justify acting as a municipal advisor. As a result, fewer firms would be willing to act as municipal advisors, reducing clients' choices and competition, particularly in markets where the availability of highly qualified municipal advisors is more limited or non-existent.

Finally, while SIFMA believes, as discussed below in Section III.A.2, that any restriction on principal transactions should not apply in the context of obligated person clients, it is worth noting the extraordinary effect not limiting the proposed restriction to matters relating to the municipal advisory engagement would have in the context of obligated persons. Private businesses, whether or not for profit, may obtain financing through conduit bonds and become obligated persons on those municipal securities. As drafted, Proposed Rule G-42 would prohibit any affiliate of the municipal advisor from engaging in any business activity, as principal, with that private enterprise.

(b) Application to Common Principal Activities

Any restriction should not apply to certain common principal activities of persons that are also municipal advisors or affiliated with municipal advisors, such as taking deposits, entering into swaps or security-based swaps that comply with applicable CFTC or SEC business conduct rules,[6] selling securities or foreign exchange products. In particular, if deposit-taking and other traditional banking services are not excluded from the prohibition, a bank should not be prohibited from acting as principal and performing these principal activities where it is the bank's separately identifiable department or division, and not the bank itself, that is the municipal advisor.

(c) Extent of G-23 Exception

Proposed Rule G-42(f) provides that the prohibition on principal transactions would not apply to "an activity that is expressly permitted under Rule G-23." The Regulatory Notice explains that in order to "avoid conflict" with another MSRB rule, the proposed rule would allow activity "expressly permitted by underwriters under Rule G-23." The extent of this exception is not entirely clear. SIFMA requests that the MSRB

[6] As noted above in Section III.A, Congress specifically considered and permitted swap dealers to provide advice to special entities and engage in those principal transactions.

confirm that this exception is intended to refer to and apply the two interpretive materials regarding Rule G-23, discussed below, rather than Rule G-23 itself.

First, under an MSRB Interpretive Notice, dated November 21, 2011,[7] the MSRB indicated that when a dealer "clearly identifies itself in writing as an underwriter and not as a financial advisor from the earliest stages of its relationship with the issuer with respect to [an] issue," then the dealer would not be prohibited from acting as an underwriter with respect to that issue. As a result, if a firm that is both a municipal securities dealer and a municipal advisor were to clearly identify itself in writing as an underwriter from the earliest stages, in accordance with Rule G-23, then even if the firm provides advice that would otherwise trigger municipal advisor status (outside of the underwriter exclusion under the Final MA Rules), then the resulting municipal advisory relationship, as a result of the exception contained in Rule G-42(f), would not be subject to a prohibition on transacting as principal.

Second, under a separate MSRB Interpretive Notice, dated May 23, 1983,[8] the MSRB clarified that Rule G-23 applies to "financial advisory services rendered to state or local governments and their agencies, as well as to municipal corporations," but not to corporate obligors.[9] As a result, a financial advisor to an obligated person is expressly permitted under interpretations of Rule G-23 to act as an underwriter with respect to the transaction. The exception from the proposed prohibition on principal transactions for activities permitted by Rule G-23 should be revised to clarify that a municipal advisor to an obligated person is not restricted from also acting as an underwriter with respect to the transactions being advised on.

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[7] *See* Guidance on the Prohibition on Underwriting Issues of Municipal Securities for which a Financial Advisory Relationship Exists Under Rule G-23 (Nov. 27, 2011), *available at* http://www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-23.aspx?tab=2#_B79A2C2C-796A-4152-BEEB-93E0C5944753.

[8] *See* Notice on Application of Board Rules to Financial Advisory Services Rendered to Corporate Obligors on Industrial Development Bonds (May 23, 1983), *available at* http://www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-23.aspx?tab=2#_42E084C9-F9D3-4CBA-97C2-2944B9A48596.

[9] *See also* Notice of Filing of Amendments to Rule G-23, on Activities of Financial Advisors, SR-MSRB-2011-03, Exchange Act Release No. 63946 (Feb. 22, 2011) (MSRB stating that "Rule G-23 does not preclude a dealer from serving as financial advisor to a conduit [private] borrower on an issuance of municipal securities and the proposed amendments [to Rule G-23] would not prohibit the dealer from providing underwriting services for such issue of the conduit issuer so long as it has not also become the financial advisor to the conduit [municipal] issuer.").

2. The Proposed Prohibition on Principal Transactions Should Not Extend To Obligated Person Clients

As discussed throughout this letter, Proposed Rule G-42 does not appropriately distinguish between the fiduciary duty owed by a municipal advisor to its municipal entity client, and its duties of care and fair dealing owed to an obligated person client. While, as discussed above, SIFMA does not believe a complete prohibition on engaging in principal transactions is appropriate in general, such a rule would be entirely misplaced as applied to obligated persons where no duty of loyalty exists.[10]

3. Application to Affiliates is Impractical

The proposed prohibition on principal transactions would purport to extend to any activities of a municipal advisor's affiliates.

To the extent that the restrictions on principal transactions are retained, the MSRB should reconsider the extent of their application to affiliates of the municipal advisor where the affiliate is not directly involved in the same municipal securities offering as the affiliated municipal advisor. Such restrictions would likely prove unworkable—particularly for large financial institutions engaged in the provision of multiple services to clients.

Large financial institutions, which may have a municipal advisor affiliate, often have thousands of other affiliates throughout the world engaged in other separately managed business activities. In order to ensure compliance with Proposed Rule G-42, a municipal advisor would first need to identify all of its affiliates, then determine whether any of its affiliates have any business relationship with the client, as well as whether there is any principal aspect to these relationships. Conducting this analysis across thousands of affiliates would be overly burdensome and would require major compliance and operational resources for such municipal advisors and their affiliates. For example, these financial institutions would need to develop systems and databases that keep track of the activities of all of their affiliates, which, as described below in the Appendix, would require costly projects to build such significant infrastructure.

Rather, any restrictions on principal transactions should apply only to the activities of the municipal advisor and affiliates directly involved in the municipal securities offering on which it advises, rather than all of its affiliates.

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[10] SIFMA notes that in this regard Proposed Rule G-42 is inconsistent with the MSRB's initial 2011 proposal interpreting the duty of care owed by a municipal entity to an obligated person under Rule G-17. Rather than restricting principal transactions in any manner, at that time the MSRB more appropriately proposed to require that a municipal advisor disclose to its obligated person client "whether the municipal advisor or an affiliate of the municipal advisor is acting as a principal in matters concerning the municipal advisory engagement." *See* MSRB Notice 2011-49.

4. The Proposed Complete Prohibition on Principal Transactions, Notwithstanding Disclosure and Consent, is Overbroad, Unprecedented, and Harmful to Clients

The proposed complete prohibition on municipal advisors transacting as principal with their clients is unprecedented and of startling breadth. While certain principal transactions may raise conflicts of interest, not all such conflicts are irreconcilable and many such conflicts can be disclosed and, at the option of the client, waived. Specifically, while SIFMA understands why the MSRB might wish to prohibit a municipal advisor advising a municipal entity on a municipal securities offering and then acting as principal in connection with the investment of the proceeds, the same conflict of interest does not arise in other forms of municipal advisory engagements.

Where a municipal advisor is engaged specifically to advise on the investment of bond proceeds or municipal escrow investments, or derivatives, rather than on a municipal securities offering, principal transactions should be permissible, so long as a municipal advisor has provided reasonable disclosure of, and obtained informed consent to, the potential conflicts associated with the principal activities. Such disclosure and informed consent should be required only when a municipal advisory relationship is established or when an account is opened between a municipal advisor and a municipal entity or obligated person and not on a transaction by transaction basis.

Even investment advisers, which have long been recognized as owing a fiduciary duty and the utmost good faith in dealings with their clients,[11] are not subject to an immutable prohibition on transacting with a client as principal. Rather, consistent with its fiduciary duty, an investment adviser and its affiliates may engage in a principal transaction with a client so long as the adviser obtains the client's consent after disclosing the capacity in which the adviser will act, any compensation the adviser will receive and any other relevant facts.[12]

In fact, throughout the Dodd-Frank Act, where Congress considered advisory relationships and the potential for principal activity, it made clear that the two were compatible with appropriate safeguards. The MSRB should interpret the duties of municipal advisors, created under the same act of Congress, consistent with how Congress viewed them. For example, the Dodd-Frank Act subjects a swap dealer and security-based swap dealer, when acting as an advisor to a "Special Entity" (which generally includes municipal entities), to a duty to act in the best interests of the Special

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[11] *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180 (1963).

[12] *See* Investment Advisers Act of 1940 § 206(3). *See also* SEC Staff Study on Investment Advisers and Broker-Dealers (Jan. 2011) at 24–26.

Entity.[13] But swap dealers and security-based swaps dealers, by their nature, transact as principal. Permitting these dealers to act as both principals and advisors, subject to the best interest standard, reflects a Congressional determination, contrary to the MSRB's proposal, that acting as both an advisor and a principal on the same transaction does not always raise such a "high potential for self-dealing"[14] that disclosure and client consent could not cure.

Similarly, Section 913 of the Dodd-Frank Act, codified at the second Section 15(k) of the Exchange Act, permits the SEC to promulgate rules subjecting broker-dealers to a fiduciary duty when providing personalized investment advice about securities to retail customers. However, Congress instructed the SEC that notwithstanding any fiduciary duty rule the SEC adopts, a broker-dealer would not be in violation of such a fiduciary duty by selling only proprietary products, although the SEC could require that the broker-dealer provides its customer with notice and obtains consent or acknowledgement.[15] So too, when a municipal advisor is providing advice on investments incidental to its brokerage activities rather than advising on a municipal securities offering, the municipal advisor and its affiliates should not be prohibited from transacting as principal, so long as the client has received full and fair disclosure and consent to the principal transaction.

Notably, a registered investment adviser is generally exempt from registration as a municipal advisor to the extent that it is providing investment advice.[16] Congress adopted this exclusion because it believed clients of registered investment advisers were adequately protected by the fiduciary duty inherent in that regulatory scheme—including the requirement that investment advisers disclose and obtain consent prior to engaging in principal transactions. It would be an anomalous result (and contrary to Congressional intent) if the MSRB were to adopt a rule that prohibited a municipal advisor from engaging in principal transactions—while the exact same transaction would be permissible for a registered investment adviser engaging in the exact same advisory activity—solely because the investment adviser may operate under an exemption from municipal advisor registration.

In addition to being unprecedented and beyond Congressional intent, the proposed absolute prohibition on principal transactions is bad policy. A prohibition that could not be cured through disclosure and consent would deprive clients of access to certain financial products, such as debt securities the municipal advisor sells in its capacity as a dealer in securities, or swaps the municipal advisor enters into in its swap dealer capacity. Moreover, restricting the municipal entity client's options could compromise the client's

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[13] *See* Commodity Exchange Act § 4s(h)(4)(B) (added by Section 731 of the Dodd-Frank Act).

[14] *See* Regulatory Notice at 13.

[15] *See* Exchange Act § 15(k)(2).

[16] *See* Exchange Act § 15B(e)(4)(C); *see also* Exchange Act Rule 15Ba1-1(d)(2)(ii).

ability to receive better pricing given that large market makers may not be able to provide certain pricing if they are not able to compete.

5. The Proposed Prohibition Would Require Large Financial Institutions to Share Confidential or Material Nonpublic Client Data Among Their Affiliated Legal Entities

In order to comply with the proposed prohibition on principal transactions, large financial institutions will be required to know whether any of its affiliated legal entities are acting as either a principal or advisor on a specific transaction with a municipal entity or obligated person. This, in turn, will require such large financial institutions to develop new, or enhance already existing, systems that would force these institutions to share confidential or material nonpublic information involving municipal entities or obligated persons across their many lines of business. However, client privacy requirements and standard business practice may prohibit or limit the ability of large financial organizations to share client data among affiliated, but separate, legal entities. This may create a situation in which it would be impossible to identify where affiliates act as principals with municipal entities or obligated persons. Moreover, these large financial organizations will necessarily need to violate their own information barrier policies and procedures, established pursuant to regulatory requirements under the Exchange Act, in order to protect against the misuse of material nonpublic information and to protect their clients' privacy.[17]

B. Municipal Advisor Standards of Conduct Generally

1. Municipal Advisors Should Not Be Subject to an Explicit or Implicit Fiduciary Duty When Advising Obligated Persons

Proposed Rule G-42(a) correctly notes that a municipal advisor is subject to different legal duties when it advises an obligated person than when it advises a municipal entity, since in the latter case, the municipal advisor is subject to a fiduciary duty. However, the distinction becomes illusory in light of the manner in which Proposed Rule G-42 would impose uniform obligations and restrictions on both relationships—effectively imposing a fiduciary duty on municipal advisors dealing with obligated persons. Many of the obligations under Proposed Rule G-42 presuppose the existence of a fiduciary duty and would be wholly inappropriate to more arms-length relationships only involving a duty of fair dealing. For example, the need to avoid or

[17] *See e.g.*, Exchange Act Section 15(g) (requiring registered broker-dealers to establish, maintain and enforce written policies and procedures reasonably designed, taking into consideration the nature of the business, to prevent the misuse of material nonpublic information by the firm or its associated persons in violation of the Exchange Act).

disclose extensive information regarding conflicts of interest, and the proposed prohibition on transacting as principal, appear to be expounding upon a duty of loyalty.[18] And, as discussed more fully in Section III.A.2 below, the imposition of a principal transaction ban on relationships with obligated persons is also an inappropriate extension of fiduciary standards to the obligated person client. By applying these requirements equally to both relationships, the MSRB would, in effect, inappropriately extend a fiduciary duty to advisory activities with obligated persons.[19]

Applying a fiduciary duty to a municipal advisor's relationship with an obligated person would be inconsistent with Congress's statutory directive to the MSRB under Section 15B of the Securities Exchange Act of 1943 (the "**Exchange Act**") (as amended by the Dodd-Frank Act) and would arguably exceed the MSRB's authority. If Congress intended for a uniform standard to apply when advising obligated persons and municipal entities, it would have assigned a statutory fiduciary duty to both relationships. Rather, as the MSRB has noted, Congress only directed that a municipal advisor have a fiduciary duty when it acts as an advisor "to [a] municipal entity,"[20] and that the MSRB adopt rules relating to this fiduciary relationship. Congress clearly had the opportunity to consider requiring municipal advisors to observe a uniform standard or duty, and specifically declined to do so. In adopting the Final MA Rules, the SEC similarly indicated its belief that separate duties would apply, with municipal advisors to obligated persons being subject to a duty of fair dealing under Rule G-17, rather than a fiduciary duty.[21]

The distinction mandated by Congress and referenced by the SEC, in fact, makes sense and should be respected and maintained by the MSRB. In adopting the provisions of the Dodd-Frank Act establishing the municipal advisor regulatory scheme, Congress was concerned regarding losses suffered by *municipal entities* who may have over-relied on the advice of unregulated municipal advisors that put their own interests ahead of their clients'.[22] In contrast, obligated persons are *private* sector entities (whether or not for-profit) with the wherewithal to evaluate any advice received; most have access to financial markets using their own credit, much like other private issuers whose interface

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[18] *See infra* Sections III.C.2 (noting that requiring non-individualized disclosures is inappropriate in a non-fiduciary context); III.C.3 (noting that the disclosure requirements appear to presuppose a duty of loyalty); III.A (noting that municipal advisors should be permitted to reasonably disclose, and obtain informed consent, of potential conflicts associated with principal activities); III.A.2 (noting that the proposed prohibition on principal transactions is inappropriate when the client is an obligated person).

[19] SIFMA notes that the MSRB specifically requested comment on whether it should, in fact, explicitly adopt a uniform fiduciary duty for municipal advisors dealing with obligated persons. As noted above, SIFMA opposes such an expansion, whether explicit or implicit.

[20] Exchange Act § 15B(c)(1).

[21] *See* Adopting Release at 156.

[22] *See* Regulatory Notice at 4.

with financial services providers is not specially protected by a fiduciary standard, but more arms-length duties of due care and fair dealing. Moreover, obligated persons generally engage in many types of activities that are wholly unrelated to the issuance of municipal securities. For example, the fact that an airline raised capital through a conduit offering to build an airport terminal should not mean that all of the transactions between the airline and an advisor on that offering should be subject to Rule G-42.

SIFMA therefore believes that, as discussed above, the MSRB should adopt separate rules with respect to the obligations of municipal advisors when advising municipal entities, on the one hand, and when advising obligated persons, on the other—as the MSRB proposed to do when it initially proposed rules relating to the duties of municipal advisors in 2011.[23] These separate rules should clearly reflect a fiduciary duty (*i.e.*, duty of care and duty of loyalty), in the case of advising municipal entities, and a duty of fair dealing, in the case of advising obligated persons. Further, any special affirmative duties that are owed to obligated persons under the duty of fair dealing should reflect the specific characteristics of the municipal securities market and the obligated person's activities in it, rather than to any special needs of the obligated person for special protective conduct standards.

2. Rule G-42 Should Not Apply to Any Transaction or Activity That Would Not Trigger Municipal Advisor Status

Where an entity is engaging in conduct that would not trigger municipal advisor registration under the Exchange Act or the Final MA Rules, the MSRB should exclude such entity or activity from Rule G-42. For example, Proposed Rule G-42 defines "municipal advisory activities" as those activities described in Section 15B(e)(4)(A) of the Exchange Act (with the exception of Section 15B(e)(4)(A)(ii)). However, the definition does not exclude the statutory exclusions from being considered a municipal advisor under Section 15B(e)(4)(c) of the Exchange Act (*e.g.*, underwriters or registered investment advisers) or the exemptions set forth in the SEC's Final MA Rules (*e.g.*, certain bank activities, certain swap dealer activities, situations where an independent registered municipal advisor is involved, responding to RFPs/RFQs). As a result, Proposed Rule G-42 could be read to apply, for example, to an underwriter whenever the underwriter provides advice regarding structuring a municipal securities transaction, even though such activity would not trigger municipal advisor status.

By excluding and exempting certain activities from municipal advisor registration, Congress and the SEC, of course, also intended the persons engaging in those activities to not be subject to the duties attendant to municipal advisor status. While expanding the application of Rule G-42 to apply to persons excluded or exempted from municipal

[23] *See* MSRB Notice 2011-48; MSRB Notice 2011-49.

advisor status might not have been the MSRB's intent, the MSRB should explicitly clarify the language of the rule to properly reflect its scope.

3. Proposed Rule G-42 Duty of Care Must be Appropriate for All Municipal Advisory Activities

If, contrary to SIFMA's proposal above,[24] the MSRB proposes to adopt a single rule applicable to all municipal advisory activities (other than solicitation activities), it must be sure that the obligations imposed under the rule are appropriate for all municipal advisory activities to which they would apply. This would include, for example, a registered municipal advisor that is a broker-dealer not involved in a municipal securities offering that provides advice in connection with a brokerage account that contains the proceeds of the offering.

It is not clear whether the application of Proposed Rule G-42 outside of the municipal securities offering context was adequately considered or appropriately limited. For example, proposed Supplementary Material .01 would require that a municipal advisor make a reasonable inquiry regarding the facts that are relevant to a client's determination to pursue a particular course of action. While this requirement may be appropriate in the context of arranging a municipal securities issuance, it could be prohibitive in the case of ordinary brokerage and related advice, given the number of trades involved, timing considerations and the general context of broker-related advice.[25]

Similarly, the obligation under Supplementary Material .02 for municipal advisors to investigate or consider reasonably feasible alternatives appears overly broad outside the context of municipal securities issuances. For example, consider a situation where a municipal entity has determined to invest the proceeds of a municipal securities offering in a particular asset class and whether or not they hired a municipal advisor to assist with selecting the investment within that class. That municipal advisor should not be obligated to consider whether an investment in another asset class would be a reasonably feasible alternative, unless actually engaged to do so.

C. Disclosure of Conflicts of Interest and Other Information

1. The MSRB Should Clarify When the Inception of a Municipal Advisory Relationship Occurs

Proposed Rule G-42(b) would require that certain disclosures are provided by a municipal advisor to its client "at or prior to the inception of a municipal advisory

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[24] *See supra* Section III.B.1.

[25] We also observe that the proceeds of municipal securities issuances are generally required to be invested in limited types of assets with limited duration and of high quality, reducing the risks raised by this type of advisory relationship.

relationship." The MSRB should clarify when the "inception" of such a relationship will be deemed to occur for purposes of the rule, in particular, outside of the municipal securities issuance context. Such a clarification should encompass the varied types of relationships that could trigger municipal advisor status, including when the disclosures must be sent when advising on an offering and when the disclosures must be sent when opening a brokerage account. In particular, when a municipal advisor gives advice in connection with brokerage or banking services relating to the investment of the proceeds of an offering, the disclosures should be limited to when an account is opened (*i.e.*, when a relationship is established) and should not be required on a trade-by trade-basis.

As discussed below,[26] a municipal advisor may have pre-engagement or other communications with a client that include informal advice, triggering municipal advisor status under the Final MA Rules. For example, a broker-dealer may provide incidental advice regarding the investment of funds in an account, only to learn that the account includes the proceeds of a municipal securities offering—triggering municipal advisor status. The parties would not have anticipated, in advance, entering into a municipal advisory relationship. As such, it would not have been possible for the broker-dealer/municipal advisor to have prepared the required disclosures. To address this, the MSRB should clarify when the "inception" of the relationship is deemed to have occurred for purposes of the disclosure requirements under Proposed Rule G-42(b), taking into account the need for a reasonable period within which to make these disclosures once the parties realize that a municipal advisory relationship has been formed.

2. Non- Individualized Disclosure Should be Permitted for Non-Fiduciary Relationships

Proposed Rule G-42(b) would require municipal advisors to provide extensive, and potentially burdensome, disclosures to clients, including disclosures regarding certain conflicts of interest. Supplementary Material .05 would further require that these disclosures include "an explanation of how the [municipal] advisor addresses or intends to manage or mitigate each conflict."

While SIFMA believes that such extensive and individualized conflicts disclosure may be appropriate in the context of fiduciary relationships, *i.e.*, where a municipal advisor is advising a municipal entity, they are unnecessarily burdensome and inappropriate in other relationships. As noted above, SIFMA believes that the MSRB should adopt separate rules relating to the duties of municipal advisors to obligated persons. In doing so, or to the extent that the MSRB determines to maintain a single rule, it should revise the proposed disclosure requirements for municipal advisors to obligated persons to a level more appropriate to satisfy a duty of care and duty of fair dealing. In

[26] *See infra* Section III.D.1 (noting that it is not practical to require municipal advisors to have a formal written engagement when providing informal advice).

particular, the MSRB should permit any conflicts disclosure to be satisfied through disclosures that are not individualized to the obligated person client. Where, in a particular circumstance, the municipal advisor determines that general disclosures would not be sufficient because there exists a conflict of interest specific to the obligated person client, the municipal advisor only then would be required to provide individually tailored disclosures.

Similarly, the proposed obligation under Supplementary Material .05, requiring individualized disclosure of how a conflict will be managed, is inappropriate in a non-fiduciary relationship where no duty of loyalty exists. Of course, once the conflict is disclosed, then, if the obligated person has concerns regarding how the municipal advisor plans to manage or mitigate a conflict, the obligated person can ask the municipal advisor directly.

3. Proposed Required Disclosure of Affiliate Products and Services is Vague and Overbroad

Proposed Rule G-42(b)(ii) would require municipal advisors to disclose (i) "any affiliate . . . that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related" to the services to be provided and (ii) any other relationships of the municipal advisor or its affiliates "that might impair the [municipal] advisor's ability to render unbiased and competent advice."

The MSRB should clarify the circumstances under which an affiliate of a municipal advisor would be providing advice or other services that are "indirectly related" to the municipal advisor's activities for purposes of Proposed Rule G-42(b)(ii). The concept of "indirectly related" advice, services or products in this context is open-ended and will be difficult or impossible to apply in practice. For example, as drafted, advice provided by an affiliate related to a deposit bank or a credit relationship with some relationship to the municipal advisory services to be performed could appear to be captured, but such ordinary course relationships should be beyond the scope of the disclosure requirements.

In addition, the broad language of the Proposed Rule G-42(b)(ii) and (vii) should be limited by materiality and knowledge standards, such that a municipal advisor is only required to disclose (i) for purposes of Proposed Rule G-42(b)(ii), advice, services, or products provided by an affiliate that are *material* in the context of the municipal advisory relationship that the municipal advisor has actual knowledge of, and (ii) for purposes of Proposed Rule G-42(b)(vii), other engagements or relationships that might *materially* impair the municipal advisor's ability to render unbiased and competent advice, and in the case of the municipal advisor's affiliates' relationships or engagements, where the municipal advisor has knowledge of such relationships or engagements. The MSRB should also clarify how a municipal advisor may comply with the proposed requirement to disclose the existence of another engagement in situations where it, or its

affiliate (as applicable), is subject to a confidentiality arrangement prohibiting such disclosure.

Further, as noted above with regard to similar proposed requirements, these disclosure requirements appear to presuppose a duty of loyalty, not mere duties of care and fair dealing. As such, they should only apply to the fiduciary relationships between a municipal advisor and a municipal entity client, rather than the duties of care and fair dealing between a municipal advisor and a private obligated person client.

4. Disclosure of Legal and Disciplinary History is Unnecessary and Burdensome

Proposed Rule G-42(b)(ix) would require a municipal advisor to disclose to clients legal or disciplinary events "material to the client's evaluation" of the municipal advisor or its integrity or otherwise disclosed on Forms MA or MA-I.

Municipal advisors should not be required to specially disclose any legal or disciplinary event that is already disclosed in the most recent Forms MA, MA-I, BD, ADV or other publicly available disclosures. Requiring such duplicate disclosure provides little, if any, benefit to municipal entities or obligated persons, while it imposes unnecessary additional burdens on municipal advisors.[27]

Further, to the extent that the MSRB retains Proposed Rule G-42(b)(ix), it should limit any disclosure to the information contained in Forms MA and applicable MA-Is, rather than further requiring disclosure of legal and disciplinary events "material" to the client's evaluation. A municipal advisor is not in the position to determine the manner in which a client evaluates potential municipal advisors or how a client may view the integrity of the advisor's personnel.

In addition, the SEC, in adopting Forms MA and MA-I, has already determined what legal and disciplinary events it believes would be material to disclose in the context of municipal advisory engagements. Requiring municipal advisors to consider whether there are other events, not disclosed on Forms MA or MA-I, that a particular client might find to be material would generally produce a null set, but still impose substantial costs and burdens on municipal advisors to investigate and make that determination.

5. Affirmative Disclosure of Lack of Conflicts is Unprecedented

Fiduciaries are generally required to disclose the extent to which they have any conflicts of interest with their client. However, the requirement under Proposed Rule G-

[27] Municipal entities and obligated persons are, of course, free to request such information specifically in RFPs or otherwise if they find it useful.

42(b) that a municipal advisor affirmatively disclose if it has concluded that it has no material conflicts of interest is rightfully unprecedented. No other SEC, FINRA or MSRB rule includes a similar requirement that forces a financial service provider, including fiduciary advisors, to affirmatively disclose that it believes no material conflicts of interest exist.

A requirement to affirmatively disclose a lack of conflicts may subject municipal advisors to increased liability, litigation, and enforcement actions. A municipal advisor that discloses its good faith determination that no material conflicts of interest exist may later be forced to explain in a subsequent litigation or enforcement action, subject to hindsight bias, why a conflict that later became a concern was viewed as immaterial in advance.

6. Municipal Advisors Should Not Have Disclosure Obligations to Investors

Supplementary Material .07 to Proposed Rule G-42 would require that, where a municipal advisor or its affiliate prepared any material that is included, in whole or part, in an official statement, the municipal advisor must provide investors with the same conflict disclosure the municipal advisor must provide its municipal entity or obligated person client under Proposed Rule G-42(b)(ii). Direct disclosure to investors would be improper for a municipal advisor, and the MSRB should eliminate this proposed requirement.

Municipal advisors have no contractual or other relationship with investors. Rather, it is the obligation of the issuer to make sure that its disclosure is materially accurate and complete. A municipal advisor may be engaged to advise and assist an issuer in connection with the preparation of the issuer's disclosure—but it remains the issuer's disclosure, not the municipal advisor's. Indeed, Proposed Rule G-42(b)(ii) would already otherwise require that municipal advisors provide this same conflict information to the issuer; with the information in the issuer's possession, the MSRB should leave it to the issuer to determine whether or not such information is material to investors and warrant disclosure.

7. Disclosure Rules, if Retained, Should be Clarified

Proposed Rule G-42(b)(i) would require disclosure of "any . . . potential conflicts of interest . . . that *might* impair" a municipal advisor's advice or its ability to act as a fiduciary. If this requirement is retained, it should be limited to conflicts "that could reasonably be anticipated to impair" such matters.

Proposed Rule G-42(b)(viii) would also require disclosure of "the amount and scope of coverage of professional liability insurance that the municipal advisor carries." The presence, absence or level of professional liability insurance is not particularly relevant and should not affect the quality of an advisor's advice. Many large firms may

self-insure due to financial considerations, not because of the level of service they provide. Those professional firms that do obtain liability coverage do so for their own benefit, not to benefit clients. Therefore, disclosure of professional liability insurance should not be required unless specifically requested by a municipal entity or obligated person.

D. Documentation of Municipal Advisory Relationship

1. Documentation Should Only Be Required in Connection with Formal Mandates

Under Proposed Rule G-42(c), municipal advisors would be required to document each municipal advisory relationship in writing prior to, or promptly after the inception of, the municipal advisory relationship. Requiring detailed documentation may be sensible in the context of formal mandates to provide advice in connection with a significant municipal securities offering, financing plans or investment plan. However, as interpreted by the SEC and its staff,[28] more informal advice—even uncompensated advice—may also trigger municipal advisor status. It is not practical to require a municipal advisor to evidence these forms of informal advice in a formal written document containing all the elements the MSRB has proposed to require.

For example, a business pitch that does not fit within the SEC's guidance for communications that are deemed not to constitute advice, providing incidental or post-issuance advice or investment advice in connection with a brokerage account containing the proceeds of a municipal securities offering, may trigger municipal advisor status. In such a context, neither party would expect there to be a formal advisory engagement in place. Requiring a formal written engagement in such circumstances would greatly impede the flow of timely communications which could be exigent in light of market conditions. Further, in the case of intermittent investment advice regarding a brokerage account, the amount of each investment in question or the frequency of the advice would typically make it impractical to enter into a formal agreement each time advice is given.[29]

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[28] *See* Adopting Release at 39-47 (defining the advice standard in general); *see also* Registration of Municipal Advisors, Frequently Asked Questions, *available at* http://www.sec.gov/info/municipal/mun-advisors-faqs.pdf ("**Final MA Rule FAQs**") at Question 1.1.

[29] Even if a written agreement were to be required in these cases, the MSRB would need to reconsider the required content. For example, it is unclear how one could satisfy the requirements concerning specifying termination triggers and material amendments outside the context of a formal advisory mandate.

2. Proposed Duties in Connection with the Official Statement are Contradictory and Confusing

Proposed Rule G-42(c)(iv) reasonably allows a municipal entity and its client to generally specify in the relationship documentation the scope of municipal advisory engagement and any limitations on that scope that the parties agree on. However, in connection with municipal advisory activities relating to a new issue or reoffering of municipal securities, Proposed Rule G-42(c)(v) requires that the engagement include that the municipal advisor will perform "the specific undertakings, if any, requested by the client" relating to the official statement—apparently limiting a municipal advisor's ability to choose to limit the scope of its engagement in this context. Similarly, Supplementary Material .01 to Proposed Rule G-42 provides a default requirement that a municipal advisor "must . . . undertake a thorough review of the official statement . . . unless otherwise directed by the client."

Instead, the MSRB should adopt a broadly applicable standard that a municipal advisor is only required to perform (and the client is only required to pay for) the services that the municipal advisor and its client mutually agree to as the scope of the engagement. This mutual agreement standard should apply to all aspects of the engagement, including review of official statements, so as to allow the municipal advisor and client, at the outset of the transaction, to exclude from the scope of the municipal advisory relationship any services the parties do not mutually wish to include within the scope of their engagement.

3. Additional Clarity is Needed on Certain Documentation Requirements

Proposed Rule G-42(c)(i) would require municipal advisors to include in their relationship documentation "the form and basis of direct and indirect compensation" for the services. SIFMA requests that the MSRB clarify what it believes would need to be included within the form and basis of "indirect" compensation. While it is customary to set out the form and basis of direct compensation in engagement documentation, it is not clear what indirect compensation would be appropriate to include. To the extent that a municipal advisor is to receive compensation from a third party in connection with the engagement, that fact would more appropriately be considered a potential conflict of interest subject to disclosure under Proposed Rule G-42(b), rather than a matter to be evidenced in engagement documentation.

Proposed Rule G-42(c)(ii) would require municipal advisors to include in their relationship documentation the reasonably expected amount of compensation in dollars (to the extent quantifiable), and to modify their relationship documents at the time of each material adjustment to their expectation. To the extent permitted, if the basis of compensation is a percentage or other mathematical function of the principal amount of an issue of bonds, there should be no need to update the math, even if the amount of the issue changes materially.

Proposed Rule G-42(c) would require that "during the term of the municipal advisory relationship" the disclosure information under paragraph (b) and the engagement documentation under paragraph (c) be promptly amended or supplemented to reflect certain changes or additions. The MSRB should confirm that, for purposes of this requirement, the term of the municipal advisory relationship is determined in the manner in which the termination has been described for purposes of the engagement documentation (as required by Proposed Rule G-42(c)(vi)).

E. Recommendations

1. The MSRB Should Not Mandate Specific Discussions

Proposed Rule G-42(d)(i) through (iii) would specifically mandate that a municipal advisor discuss with its client the municipal advisor's evaluation of material risks and benefits of a recommended transaction or product, the basis on which the municipal advisor believes the transaction is suitable and whether the municipal advisor investigated alternatives. Unless the client explicitly requests this information, these affirmative mandates go beyond what is required of fiduciaries generally and may be unworkable for municipal advisors and burdensome to clients.

In addition, if the MSRB retains this proposed requirement, it should clarify what type of documentation municipal advisors would be expected to maintain as evidence that the enumerated topics were discussed.

2. The MSRB Should Clarify the Proposed Requirement that a Municipal Advisor Only Recommend Transactions that are in the Client's Best Interest

While SIFMA supports the requirement in Proposed Rule G-42(d) that a municipal advisor only recommend municipal securities transactions or municipal financial products that are in the client's best interest, this provision is drafted in an overbroad manner. A client will often ask for a municipal advisor's recommendation regarding how to best meet a stated objective, which the municipal advisor may or may not have determined to be in the client's best interest. The MSRB should clarify that if a client has stated its objectives, the requirement to make only recommendations that are in the client's best interest does not imply that the municipal advisor must go behind the client's stated objectives, since such an inquiry may not be consistent with, or within the scope of, the engagement. The MSRB should also clarify that the obligation to make recommendations in the client's best interest does not imply that a recommended course of action must clearly be superior to other alternatives, in situations where there may be multiple alternatives, each of which has its own risks and costs, none of which may be objectively superior.

A further concern is that Proposed Rule G-42 may be read to suggest that a municipal advisor's compliance will be judged by whether a recommended transaction

actually is (or turns out to be) in the client's best interest, rather than by whether the advisor actually and reasonably believes that to be the case. Municipal advisors are not guarantors of what is in the best interest of their clients, and thus the MSRB should revise Proposed Rule G-42, or add Supplementary Material, confirming that the "best interest" standard is based upon a municipal advisor's reasonable belief, rather than an absolute standard. A reasonable belief standard of what is in the client's best interest should thus be satisfied by permitting an advisor to recommend (i) a range of possible action; (ii) multiple reasonably foreseeable alternatives; and (iii) any transaction that it reasonably believes to be in the client's best interest.

Finally, to the extent that this is retained, the requirement should only apply to engagements where a fiduciary duty applies.

3. The MSRB Should Not Mandate the Scope of Review of Third Party Recommendations

Proposed Rule G-42(e) would require that, when requested to do so by its client "and within the scope of its engagement," a municipal advisor must review recommendations by third parties and discuss specific aspects of its review and views with the client. It is unclear why such a requirement would be necessary or beneficial.

As proposed, a municipal advisor would only be required to undertake such a review to the extent that such reviews are "within the scope of its engagement" already otherwise agreed to with the client. A municipal advisor is, of course, required to perform the services that are within the scope of its engagement, whether or not specifically required by Proposed Rule G-42. Further, just as the parties were able to decide to include such a service within the engagement, they should be free to determine what the scope of such a review should be and what they deem appropriate to discuss.

F. Specified Prohibitions

1. Excessive Compensation

Proposed Rule G-42(g)(i) would prohibit a municipal advisor from receiving compensation that "is excessive in relation to the municipal advisory services actually performed." However, Proposed Rule G-42 and the Regulatory Notice provide no guidance as to where the line between reasonable and excessive lies, leaving municipal advisors at risk of this standard being set only in hindsight. Clients should be considered capable of evaluating and negotiating how much to pay for services and to go seek bids from others.

In its 2011 proposals relating to the duties of municipal advisors, the MSRB proposed to interpret a similar prohibition on excessive compensation as follows:

> The MSRB recognizes that what is considered reasonable compensation for a municipal advisor will vary according to the municipal advisor's expertise, the

> complexity of the financing, whether the fee is contingent upon the closing of the transaction, and the length of time spent on the engagement, among other factors. However, in certain cases and depending upon the specific facts and circumstances of the engagement, a municipal advisor's compensation may be so disproportionate to the nature of the municipal advisory services performed as to indicate that the municipal advisor is violating its duties to the client.[30]

The MSRB should confirm whether this proposed interpretation would apply to the similar prohibition under Proposed Rule G-42.

2. Accuracy of Invoices

Proposed Rule G-42(G)(ii) would prohibit a municipal advisor from delivering an invoice for fees or expenses that does not accurately reflect the activities actually performed or the personnel that actually performed the services. SIFMA agrees that such practices should be prohibited, however, we suggest adding materiality and knowledge qualifiers (*i.e.*, a municipal advisor may not *intentionally* deliver a *materially* inaccurate invoice), so as to avoid prohibiting immaterial or unintentional errors.

3. Payments to Obtain Business

Proposed Rule G-42(g)(v) would prohibit "payments made for the purpose of obtaining or retaining municipal advisory business" except for reasonable fees paid to another registered municipal advisor. If retained, the rule should be clarified to permit payments to affiliates or natural associated persons (who are not themselves required to register as a municipal advisor) in preparing responses to RFPs or RFQs, normal business entertainment expenses, and other unobjectionable expenditures made in the ordinary course of marketing and sales activities.

IV. General Requests for Comment

In response to certain of the MSRB's additional specific questions, below are SIFMA's views regarding certain of the MSRB's questions not otherwise addressed above. For ease of reference, each question is repeated in italics below, followed by SIFMA's comment.

Question 5:

> *Draft Rule G-42 allows fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client, but requires written full and fair disclosure of the arrangement. Should such fee-splitting*

[30] MSRB Notice 2011-48; MSRB Notice 2011-49.

arrangements be prohibited, regardless of whether they are fully and fairly disclosed?

If properly disclosed, fee-splitting arrangements should not be prohibited. There may be legitimate reasons for fee-splitting arrangements, including fee structures requested by clients. If a client receives full and fair disclosure regarding the arrangements and any conflicts of interest it may entail, the parties should be free to agree to the fee arrangement that it believes is most economical and efficient under the circumstances.

Question 7

Should a municipal advisor be required to obtain a written acknowledgment from the client of receipt of the conflicts disclosure and consent to any conflicts disclosed before proceeding with a municipal advisory engagement?

Municipal advisors should not be required to obtain a written acknowledgment of disclosures before proceeding with an engagement, so long as the disclosures are provided and not objected to. Requiring municipal advisors to obtain acknowledgement would effectively impose an obligation *on the client*, which could significantly delay the provision of services while clients determine what might be necessary to provide formal acknowledgment. In SIFMA members' experience in connection with disclosures provided under MSRB Rule G-17, issuers are often reluctant to formally acknowledge disclosures, even though they have received them and may request additional information.

Question 8

Should a municipal advisor be required to disclose legal and disciplinary events that relate to an individual that is employed by the municipal advisor even if the individual is not a part of (or reasonably expected to be part of) the advisor's team working for the client?

No. If the individual is not involved in providing services to the client, the disclosure would be unnecessary and potentially confusing. Moreover, if the municipal entity or obligated person wants such information, they can independently obtain such information on the Form MA-I for the municipal advisor.

Question 11

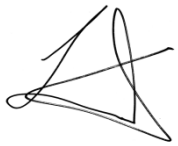
Should an advisor be required to review any feasibility study as a part of the information considered in its evaluation of whether a transaction it recommends is suitable for the client?

A municipal advisor should only be required to review a feasibility study if it is specifically engaged and agrees to do so as part of its engagement.

* * *

Please do not hesitate to contact me with any questions at (212) 313-1130, or our counsel, Lanny A. Schwartz of Davis Polk & Wardwell LLP, at (212) 450-4174.

Sincerely yours,



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Appendix: Comments on Proposed Economic Analysis

I. MSRB's Statutory Mandate

SIFMA supports the MSRB's inclusion of economic analysis in requests for comment in general, and particularly in the case of Proposed Rule G-42. Not only is an economic analysis ultimately necessary in order to meet statutory standards applicable to the approval of a self-regulatory organization's rulemaking[1] and to the MSRB's own rules,[2] but a reasoned economic analysis will inform good policy, including protection of investors, municipal entities and obligated persons, and promote a fair and robust market for the provision of financial services and prevent undue burdens on competition.

In proposing Rule G-42, the MSRB is responding to a specific statutory mandate to prescribe standards for the conduct of municipal advisors in general[3] and also to define the nature of a municipal advisor's fiduciary duty when furnishing advice to municipal entities.[4] In this context, SIFMA believes that the MSRB's economic analysis must consider the costs and benefits of Proposed Rule G-42 in light of this specific statutory directive. However, the MSRB must still evaluate the costs and benefits with respect to *each provision* of Proposed Rule G-42 in view of the differing statutory requirements applicable to municipal advisors when providing advice to municipal entities and those providing advice to obligated persons.

In light of the fact that municipal advisors are not similarly situated – particularly in regard to the range of services they and their affiliates offer – and the complexity of the corporate organizations in which they function, the MSRB should consider the costs and benefits of each proposed requirement of the proposal on each different type of municipal advisor. For example, some municipal advisors' activities (and those of their affiliates, if any, and associated persons) are limited to providing advice with respect to the issuance of municipal securities, whereas others offer underwriting, brokerage, market making, investment management and other investment services, swaps, traditional

[1] *See* Exchange Act §§ 3(f); 15B(b)(2).

[2] *See* Exchange Act § 15B(b)(2).

[3] *See* Exchange Act § 15B(b)(2)(L) (requiring the MSRB, with respect to municipal advisors, to (i) prescribe means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients; (ii) provide continuing education requirements for municipal advisors; (iii) provide professional standards; and (iv) not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud).

[4] *See* Exchange Act § 15B(c).

banking services, among others. The costs and benefits of Proposed Rule G-42 will differ across the different business models and must be considered.[5]

II. Assessing Costs and Benefits

With this framework in mind, SIFMA believes that what would be most appropriate, and most constructive, is for the MSRB to consider the benefits in terms of the protection of municipal entities, obligated persons and investors, in light of the relevant statutory standards, and the costs and competitive burdens, with respect to each proposed requirement, and as applied to the various types of municipal advisors and the variety of services offered by them.

SIFMA believes that this approach to analysis will likely facilitate more objective quantification, in particular of costs and burdens of each provision, and would help clarify for the MSRB, the SEC and market participants, the appropriateness of each provision as applied to the full range of municipal advisors and their related activities. It would also facilitate the MSRB and the SEC's evaluation of whether particular requirements are necessary or appropriate and would promote efficiency, competition, and capital formation, when applied to particular municipal advisory activities.

Concerning quantifying costs and burdens, SIFMA is concerned that the MSRB has, in direct conflict with its own policy, neglected to even attempt to do so,[6] instead asserting that cost quantification is not possible, or assuming that burdens would be minimal.[7] Moreover, there is no attempt to quantify the costs of defining the universe of relevant clients, the costs to entities in dealing with the principal transaction prohibition (including dealing with informational barriers and preventing leakage of material non-public information or the costs associated with preventing becoming a municipal advisor inadvertently). SIFMA believes that the MSRB could reasonably solicit from municipal advisors having differing profiles the expected costs of performing specified functions (*e.g.*, drafting and negotiating written agreements—which requires expenditures of time and money both for municipal advisors and their clients—preparing and providing disclosures, evaluating clients' objectives, limiting principal dealings) as well as evaluating burdens and competitive issues if the MSRB uses this analytical approach.

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[5] SIFMA notes that the MSRB has statutory authority to apply different rules to different classes of municipal advisors. *See* Exchange Act § 15B(b)(2)(A)(i) (stating that that "in connection with the definition and application of such ***standards*** the Board may appropriately classify municipal securities brokers, municipal securities dealers, and municipal advisors (taking into account relevant matters, including types of business done, nature of securities other than municipal securities sold, and character of business organization), and persons associated with municipal securities brokers, municipal securities dealers, and municipal advisors).

[6] *See* MSRB, Policy on the Use of Economic Analysis in MSRB Rulemaking, *available at* http://msrb.org/About-MSRB/Financial-and-Other-Information/Financial-Policies/Economic-Analysis-Policy.aspx (incorporating the SEC's policy that "stresses the need to attempt to quantify anticipated costs and benefits even where the available data is imperfect.").

[7] *See* Regulatory Notice at 21-24.

The MSRB's proposed economic analysis does not take into consideration the significant costs that large firms will need to bear in order to amend and/or develop their systems to comply with Proposed Rule G-42. Specifically, large firms need to consider the cost of creating information gathering that is necessary to support compliance under Proposed Rule G-42. Such large firms will also need to modify or resolve conflicts with existing information barriers that do not breach limitations of the sharing of material nonpublic information or other privacy concerns. Moreover, it is often the case that large firms have global operations, in which such firms' systems would need to be updated and/or developed on an international scale. The MSRB must therefore factor in the costs and burdens of developing such systems in relation to the size and complexity of each firm.

The MSRB must also consider the cost of certain *implied* requirements that firms necessarily will need to comply with as an incidental result of the requirements under Proposed Rule G-42. For example, municipal advisors may not be required under Proposed Rule G-42 or the proposed amendments to Rules G-8 and G-9 to keep records of all conversations relating to the relationship between a municipal advisor and its municipal entity or obligated person client. However, because Proposed Rule G-42 would require municipal advisors to undertake specific discussions, municipal advisors will, in effect, be required to maintain records that those discussions occurred in order to prove compliance with Proposed Rule G-42 during a regulatory examination.

SIFMA strongly disagrees with the MSRB's unsupported assertion that any increase in municipal advisory fees as a result of Proposed Rule G-42 "will be, in the aggregate, minimal" or that they can "be spread across the number of advisory engagements for each firm."[8] To the contrary, many of the incremental costs under Proposed Rule G-42 are not fixed overhead costs that can be spread out across all engagements. Rather, Proposed Rule G-42 would create additional costs on every single engagement, such as potentially bespoke disclosure requirements. These additional costs will need to be passed through in full, raising client's costs.

The MSRB's proposed economic analysis also fails to consider opportunity costs, which will differ depending on each and every engagement. Because of the proposed prohibition on principal transactions with clients, choosing to be engaged as a municipal advisor will mean foregoing the potential business of transacting as principal with the client. This opportunity cost will differ depending on the municipal advisor and client involved, and in some cases, need to be passed through to the client through higher advisory fees in order to justify accepting the municipal advisory engagement rather than the principal business relationship.

III. Baselines

Regarding "baselines," as suggested in the body of SIFMA's letter regarding Proposed Rule G-42, we believe that Proposed Rule G-42 as a whole should distinguish

[8] *See* Regulatory Notice at 23.

conduct standards where the municipal advisor is advising a municipal entity with respect to the issuance of municipal securities, swaps, and brokerage and dealing activities and when it is advising an obligated person (or, preferably, codify these two cases in separate rules). In the case of advising municipal entities, each requirement in the rule should be analyzed as applied to specific activities (advising with respect to the issuance of municipal securities, swaps, brokerage and dealing activities) in light of commonly understood standards of fiduciary duty in the financial services business and the specific circumstances of the municipal securities market. In the case of advising obligated persons, the baseline standard of analysis should be the fair dealing standard under MSRB Rule G-17.

IV. Consideration of Alternatives

SIFMA believes that the more granular analysis advocated above would lend itself to consideration of alternative regulatory approaches, as applied to particular requirements for particular activities—when a fiduciary standard applies and when it does not. The MSRB's proposed economic analysis does not consider alternatives at this level but instead merely considers the alternatives of (i) not adopting rules at all or (ii) adopting principles-based rules.[9] SIFMA believes that this approach is too general to be meaningful. It may be (and likely is the case) that certain *individual* requirements of Proposed Rule G-42 would, for example, be more appropriate as principles-based requirements as applied to particular activities, but others would benefit from a more prescriptive approach. The MSRB should consider these alternatives on a requirement-by-requirement basis to more meaningfully consider alternatives, rather than generalizing.

A more granular approach to evaluating costs and benefits would be particularly appropriate when considering the proposed prohibition on principal transactions, which, as noted in the body of SIFMA's comments, is overbroad. The costs and benefits of such a prohibition—and alternative approaches—should be analyzed, taking into account whether the client is a municipal entity or an obligated person, whether the transaction is one on which the municipal advisor or its affiliates are advising as a municipal advisor, the different activities (*e.g.*, investment services, swaps) that may be offered by the municipal advisor, and the practicality for compliance by a complex organization, given the impracticability of one affiliate even knowing whether another affiliate is acting as a municipal advisor on a given transaction or whether an affiliated entity or a distant trading desk may be trading as principal. Here, as elsewhere in Proposed Rule G-42, the question is not whether to have any rules at all, but how to craft the requirement so that benefits to municipal entities and obligated persons are maximized and burdens are minimized in particular contexts.

[9] In its consideration of the alternative principles-based approach, the MSRB should also discuss why a principles-based regime would be inferior to a rules-based structure, particularly given that Congress and the SEC have found a principles-based regime to be the most appropriate in the context of investment advisers—another financial advisory relationship with a statutory fiduciary duty.

V. Effect on Competition

The MSRB should expand its analysis of the effects on competition—and potential exits from the business—if MSRB rules will be applied in particular ways to particular persons, as described above. After acknowledging that the costs of Proposed Rule G-42 may lead some municipal advisors to leave the market, or others to consolidate for economies of scale, the MSRB asserts the conclusion that, nonetheless, the "market for municipal advisory services is likely to remain competitive."[10] The MSRB provides no arguments that support this conclusion, but rather cites potential offsetting benefits of Proposed Rule G-42 (*e.g.*, that clients will benefit from greater disclosure).

In fact, Proposed Rule G-42 will significantly harm competition, as many firms decide that providing municipal advisory services is not economical. For example, if, as proposed, neither a municipal advisor nor any of its affiliates is permitted to enter into any principal relationship with a client, many multiservice firms, such as firms affiliated with broker-dealers, will determine that the inability to enter into other business with the client makes the cost of providing municipal advisory services too high. As a result, the pool of firms willing to act as municipal advisors may be limited to only a smaller universe of stand-alone monoline firms. Lacking in competition, these remaining municipal advisors will increase their fees, and the quality of their service may decline, harming clients much more than they benefit from increased disclosures.

[10] *See* Regulatory Notice at 24.

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March 10, 2014

Ronald W. Smith, Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: MSRB Regulatory Notice 2014-01
Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

We are submitting this comment letter in response to Regulatory Notice 2014-01 (the "***Notice***") issued by the Municipal Securities Rulemaking Board (the "***MSRB***")[1] because of our firm's representation of a number of municipal advisors. We appreciate the opportunity to submit our comments in response to the Notice. However, as discussed below, we have a number of concerns regarding the Notice's proposal relating to MSRB Rule G-42 (the "***Proposal***").

I. OVERVIEW OF THE PROPOSAL

In 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "***Dodd-Frank Act***") to, among other things, provide for the regulation by the U.S. Securities and Exchange Commission (the "***SEC***") and the MSRB of municipal advisors. In the Notice, the MSRB notes that the Dodd-Frank Act establishes that a fiduciary duty is owed by a municipal advisor to its municipal entity clients.[2] To effectuate that end, the MSRB has proposed to define the standards of conduct and duties of non-solicitor municipal advisors. The Proposal includes, among other things:

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[1] *See Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors*, MSRB Notice 2014-01 (Jan. 9, 2014), *available at* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-01.ashx.

[2] *See* § 15B(c)(1) of the Securities Exchange Act of 1934, as amended (the "***Exchange Act***"). The Notice acknowledges, however, that the Dodd-Frank Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients.

- Disclosure requirements for municipal advisors;
- A requirement to document the terms and extent of the municipal advisor's relationship with each municipal client;
- A prohibition on recommending a municipal securities transaction or product unless the municipal advisor has a reasonable basis for believing that it is suitable for the client;
- A requirement that municipal advisors, upon request of a client, review another party's recommendation to the client;
- A prohibition of principal transactions, except in limited circumstances;
- A prohibition of specified conduct; and
- Supplementary Material containing additional guidance on the provisions of proposed Rule G-42, including Supplementary Material .10, which provides that proposed Rule G-42 would apply to municipal advisors to sponsors or trustees of 529 Plans.

As explained in further detail below, while we applaud the MSRB's goal of ensuring the protection of clients of municipal advisors, we believe that the Proposal is overly burdensome, duplicative of certain existing requirements and would lead to unintended consequences. In addition, we believe that the Notice's cost-benefit analysis does not adequately address the costs that the Proposal will create for municipal advisors.

II. COMMENTS ON THE PROPOSAL

We believe that the Proposal is overly burdensome because it (i) imposes a "one-size fits all approach" for all municipal advisors and does not account for the various business models utilized by municipal advisors, (ii) imposes substantial costs that will be passed on to the municipalities sought to be protected by the Proposal; and (iii) exceeds the scope of the fiduciary duty that was defined by Congress in the Dodd-Frank Act.

In addition, we believe that the Proposal is duplicative of existing requirements because (i) many of the proposed disclosures already are found in the publicly available disclosures municipal advisors make in Form MA, and (ii) there already exists a body of law applicable to fiduciaries, including municipal advisors.

Finally, we offer a number of miscellaneous comments relating to the Proposal.

A. The Proposal is Overly Burdensome

The Rigidity of the Proposal. Municipal advisors take a variety of forms and provide a variety of services. By imposing a single set of standards on all municipal advisors, regardless of the services provided, we believe the Proposal does not properly account for the diversity that exists in the marketplace and will, in many instances, result in the imposition of costly burdens that provide little in the way of investor protection. The Proposal appears to have been drafted with a particular municipal advisor in mind. What about the instances where an entity meets the definition of municipal advisor but is

providing a limited set of services? We believe that the Proposal is not flexible enough to accommodate the many variations that we believe exist today (as well as those that may develop in the future) because it is overly prescriptive in nature. The Proposal's rigidity is at odds with the principles-based regime of fiduciary law as developed in the common law. The Proposal's rules-based approach also is at odds with other regulatory regimes governing the provision of advice, such as the regulatory regime developed under the Investment Advisers Act of 1940, as amended the ("***Advisers Act***"). We urge the MSRB to take a principles-based approach to the regulation of municipal advisors so as to not: effectively codify a single or a limited number of business models; create winners and losers in the industry; inhibit experimentation and dynamism in the industry; limit the ability of municipal entities to contract to receive an "a la carte" set of services; or drive up the cost of compliance so as to stifle competition or to raise the costs to municipal entities of receiving municipal advisory services.

For example, in the context of state-sponsored 529 college savings plans ("***529 Plans***"), the Proposal would be impractical or unworkable in the following ways:

- Proposed Supplementary Material .01 provides that "a municipal advisor must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information." In the context of 529 Plans, municipal advisors receiving information from the trustees and sponsors of such plans would not be in a position to verify the accuracy or completeness of information provided by authorized state employees and officials.

- Proposed Supplementary Material .02 would require, among other things, that a municipal advisor "investigate and consider other reasonably feasible alternatives to any recommended municipal securities transaction or municipal financial product that might also or alternatively serve the municipal entity client's objectives." It is not clear how this requirement would apply in the context of a municipal advisor advising a 529 Plan, as the municipal advisor would be providing advice to the issuer regarding the design of the 529 Plan so as to meet stated needs and requirements of the state and complies with applicable laws governing the plan's operations. In such a context, the recommendation of another "securities transaction or municipal financial product" would not be applicable. In this respect, the quoted language above does not account for the fact that 529 Plans do not involve a particular transaction but instead are constantly being offered. It is not clear how various aspects of the Proposal apply in the context of a security that does not have a set end to the underwriting period.

- Subsection (b) of proposed Rule G-42 lists nine different disclosures that a municipal advisor must make to its client at or prior to the inception of a municipal advisory relationship, but many of these disclosures could be

inapplicable in the context of an advisory relationship with a 529 Plan.

- Proposed Supplementary Material .07 requires, among other things, the provision of written disclosure to investors of certain affiliations. As a result of the structure of 529 Plans, the services provided to 529 Plan issuers and Federal and state restrictions on the ability of financial institutions to share their customers' non-public personal information, a municipal advisor generally will not have access to information about the 529 Plan's investors or how to contact them and would therefore be unable to provide the required disclosure. In this respect, municipal advisors to 529 Plans do not generally interact with investors.

- Subsection (d) of proposed Rule G-42 imposes a suitability standard that seems unworkable in the 529 Plan context. Subsection (d), as well as Supplementary Material .08, which require consideration of such things as "the client's financial situation and needs, objectives, tax status, risk tolerance," etc., do not have much utility in the context of someone that is advising a 529 Plan issuer. In large measure, this is because Section 529 of the Internal Revenue Code and regulations thereunder dictate the relevant tax structure. Subsection (d) of proposed Rule G-42, as well as the other proposed provisions, ignore the fact that 529 Plans, unlike traditional municipal securities, do not involve a "financing" by a municipal entity. Instead, as recognized by the SEC in the municipal advisor adopting release[3] 529 Plans are funded by individual participants' contributions. In addition, a municipal advisor working with a 529 Plan issuer generally provides advice with regard to the plan's investment options that will be available to investors; in this context, the concept of suitability for the client (i.e., the state issuer) has little meaning since the municipal entity's funds will not be at risk. It is thus unclear how the suitability requirement would apply in the context of a municipal advisor advising a state on the design of a 529 Plan.

Although the stated goal of the Proposal is to provide guidance on how to apply the fiduciary duty that Congress imposed on municipal advisors, the rigidity of the Proposal creates many interpretive issues for municipal advisors that do not fit the paradigm envisioned by the Proposal; such municipal advisors will find it difficult, if not impossible, to comply with the various requirements in the Proposal. In this respect, we note that while the above examples relate to 529 Plans, the same types of issues will be faced by any municipal advisor that does not fit the traditional mold envisioned by the Proposal.

The Substantial Costs of the Proposal. As explained above, municipal advisors take many forms and will incur substantial costs when attempting to apply the Proposal's various requirements to their particular business models. These costs are likely to be

[3] *Registration of Municipal Advisors*, SEC Release No. 34-70462 (Sept. 20, 2013), *available at* http://www.sec.gov/rules/final/2013/34-70462.pdf (the "***Municipal Advisor Adopting Release***").

passed onto the clients of the municipal advisors. Furthermore, it is possible that a substantial number of municipal advisors will discontinue services that they provide to municipalities in order to avoid the Proposal's requirements or to be able to comply with the Proposal's requirements. In this respect, we believe that one of the results of the Proposal will be that municipal entities will find a more narrow menu of services and business models available to them. Accordingly, we believe the Proposal will end up harming municipalities by limiting the availability of advisory services that they need or desire. In many ways, the Proposal is rather paternalistic and assumes municipal advisors are unable to intelligently contract for advisory services. We recognize and appreciate the multitude of harms that befell various municipal entities that relied on unscrupulous or incompetent financial advisors. At the same time, we do not believe the answer to such harms lies in the prescriptive, rigid set of rules contained in the Proposal. We believe municipal entities can be protected by a broad-based set of fiduciary principles that are vigorously enforced, along with a set of complementary rules governing licensing, registration, and books and records.

The Excessive Scope of the Proposal. Although Congress imposed a fiduciary duty on municipal advisors, it did not specifically mandate any rulemaking to define the scope of such fiduciary duty. In the Notice, the MSRB justifies the Proposal by citing to Section 15B(b)(2)(L)(i) of the Exchange Act, which authorizes the MSRB to adopt rules "prescrib[ing] means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients." This grant of authority does not evidence Congress's intent for the MSRB to propose a detailed and granular set of rules defining what it means to serve as a fiduciary.

In addition, in the Notice the MSRB asks whether it should subject municipal advisors to the fiduciary duty when providing advice to obligated persons, but the MSRB has no authority for this. In fact, the Notice itself acknowledges that § 15B(c)(1) of the Exchange Act does not impose a fiduciary duty with respect to a municipal advisor's obligated person clients.

B. The Proposal is Duplicative of Existing Requirements

Disclosure of Conflicts of Interest and Other Information. Subsection (b) of Proposed Rule G-42 would require a municipal advisor to fully and fairly disclose to its clients all material conflicts of interest, and to do so at or prior to the inception of a municipal advisory relationship. We question why the disclosures that would already be made publicly available to clients through the Form MA would be insufficient, especially when the Municipal Advisor Adopting Release stated that "the information provided on Form MA and Form MA-I will expand the amount of publicly available information about municipal advisors, including conflicts of interest and disciplinary history."[4] In this respect, Form MA requires municipal advisors to disclose the following information concerning the municipal advisor's conflicts of interest:

[4] *See* Municipal Advisor Adopting Release, at p. 425 (emphasis supplied).

- Its affiliated business entities (Item 1.K.);
- Compensation arrangements, including whether the municipal advisor receives compensation from anyone other than clients in the context of its municipal advisory activities (Items 4.H. to 4.J.);
- Proprietary interests in municipal advisory client transactions, sales interests in client transactions, and investment or brokerage discretion (Item 7); and
- The municipal advisor's disciplinary history and the disciplinary history of all associated persons of the municipal advisor (Item 9).

Much of the disclosure called for by subsection (b) of proposed Rule G-42 would duplicate disclosure provided in the Form MA. For example, subsection (b)(v) of proposed Rule G-42 would require disclosure of fee-splitting arrangements, but this disclosure would already be provided pursuant to Item 4.J of Form MA. In addition, section (b)(ix) of proposed Rule G-42 would require disclosure of disciplinary events, but Item 9 of Form MA and the corollary disclosure reporting pages would already make full disclosure of these events.

Laws Applicable to Fiduciaries. The Proposal is repetitive in that there already exists a body of law applicable to fiduciaries, including municipal advisors. In addition, many municipal advisors are already subject to a fiduciary duty because of other business that they engage in, and the requirements applicable in those contexts could be sufficient to ensure that fiduciary obligations are being met.

Furthermore, because the fiduciary duty is, by its very nature, principles-based, we would suggest that the MSRB allow the fiduciary duty applicable to municipal advisors to develop organically through a principles-based approach. The SEC has adopted such an approach in developing the fiduciary duties applicable to investment advisers and that industry now has well-defined standards that are workable, practical and understandable.

C. Miscellaneous Comments

We would also offer the following miscellaneous comments regarding the Proposal:

- The Notice states, in part, that "If engaged to do so by its client, a municipal advisor also would be required to undertake a review of a recommendation made by a third party regarding a municipal securities transaction or municipal financial product." Why is this provision necessary? If engaged to provide a legal and ethical service, a municipal advisor would be obligated to do it. Why specify one out of the countless services a municipal advisor may be asked to provide?

- If a given principal transaction is truly in the best interests of a client, the client is provided full and fair written disclosure of the conflicts of interest

and costs associated with the principal transaction and the client provides prior consent to the principal transaction, then why should there be a virtual prohibition on engaging in such transactions. If the foregoing criteria are satisfied, then how it is inconsistent with a municipal advisor's fiduciary duty under Section 975 of the Dodd-Frank-Act? In this respect, we note that under the Advisers Act, investment advisers are not prohibited from engaging in principal transactions. Accordingly, the MSRB should explain why it believes "[i]t is questionable whether, given the high potential for self-dealing in such situations, a client consent following any amount of disclosure should be considered to be valid."

- In the context of 529 Plans, what does the MSRB expect from a municipal advisor in order to satisfy the proposed obligation to undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information? In the 529 Plan context it may well be that the only entity from which a municipal advisor obtains information is the issuer (or its representative) itself. Does the MSRB expect municipal advisors to obtain a representation from the issuer that the information it provides does not contain any material misstatements or omissions?

- Under the Proposal, a municipal advisor engaged by a client in connection with an issuance of municipal securities must undertake a thorough review of the official statement for that issue, unless otherwise directed by the client and so documented in writing. Why? Why is the MSRB inserting itself into the relationship between a municipal entity and a municipal advisor and requiring (unless the municipal entity expressly directs otherwise), at risk of violating an MSRB Rule, that the municipal advisor provide a service and that the municipal entity pay for such service? What is the basis for the MSRB to decide that every municipal advisor must (unless the municipal entity expressly directs otherwise), as a matter of law, provide a service prescribed by the MSRB? What is the basis for the MSRB's decision to set default contract rules for an entire industry? We note that this proposal is paternalistic, imposes, by default, costs on municipal entities and disregards the needs and desires of such entities. We believe that municipal entities should decide for themselves what services they wish to receive. We fail to see how this proposed provision supports the fiduciary duty of municipal advisors. We think it is detrimental to municipal entities, municipal advisors, and the industry and sets a dangerous precedent. Securities regulators should not be dictating contractual terms for registrants.

- Proposed Rule G-42(b) requires disclosure of the amount and scope of coverage of professional liability insurance that the municipal advisor carries (e.g., coverage for errors and omissions, improper judgments, or

negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage. We fail to understand why this is a proposed disclosure item. The MSRB needs to explain the connection between the level of insurance maintained and a municipal advisor's fiduciary duty and why such information is treated under proposed Rule G-42(b) as involving a conflict of interest.

- Under proposed Rule G-42(c), municipal advisors must evidence each of their municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship. The documentation would be required to include certain terms and conditions. Why is it necessary for the municipal advisory relationship to be reduced to a writing or to contain certain terms? We note that the Advisers Act does not require a written investment advisory agreement. What is unique about the services provided by a municipal advisor that requires a writing and that the writing contain certain designated terms? We believe that this is another example of regulatory overreaching into a relationship that should be established by the parties to the agreement.

III. THE BENEFITS VS. THE COSTS

Before proceeding with its efforts to adopt proposed Rule G-42, the MSRB should undertake a more rigorous analysis of the costs and benefits associated with the Proposal. Such an analysis would be consistent with the MSRB's recently announced *Policy on the Use of Economic Analysis in MSRB Rulemaking* (the "***Policy***") and would help ensure that any rule's costs and burdens are balanced with its expected benefits.[5] We note that the Policy establishes four elements of a proper regulatory economic analysis:

1. Identifying the need for a proposed rule and explaining how the rule will meet that need;

2. Articulating a baseline against which to measure the likely economic impact of the proposed rule;

3. Identifying and evaluating alternative regulatory approaches; and

4. Assessing the benefits and costs, both quantitative and qualitative, of the proposed rule and the main reasonable alternative regulatory approaches

[5] *See MSRB Adopts Policy for Integrating Economic Analysis into Rulemaking Process*, MSRB Press Release (Sept. 26, 2013) (announcing the MSRB's new *Policy on the Use of Economic Analysis in MSRB Rulemaking* (the "***MSRB's Economic Policy***") which is available at: http://www.msrb.org/About-MSRB/Financial-and-Other-Information/Financial-Policies/Economic-Analysis-Policy.aspx.)

The Notice is not consistent with the Policy because it does not include a discussion of the quantitative costs associated with the Proposal. The Proposal's quantitative costs must be established and compared against the expected benefits to ensure there is a legitimate basis for the Proposal.

IV. CONCLUSION

The Proposal is overly burdensome because it is inflexible, imposes costs that will be passed on to municipalities, is duplicative of existing requirements and is not supported by a rigorous cost-benefit analysis. We urge the MSRB to address these comments and to re-propose the Proposal.

I would be pleased to provide additional information or discuss these comments at your convenience.

Very truly yours,

Michael Koffler

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March 10, 2014

Via E-mail to http://www.msrb.org/CommentForm.aspx

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

RE: MSRB Notice 2014-01 Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

Wells Fargo Advisors, LLC ("WFA") appreciates the opportunity to comment on the Municipal Securities Rulemaking Board's ("MSRB" or "the Board") Draft Rule G-42, on Duties of Non-Solicitor Municipal Advisors.[1] WFA commends the Board for its effort to elaborate on the duties of municipal advisors to municipal entities and obligated persons.

WFA consists of brokerage operations that administer almost $1.4 trillion in client assets. It employs approximately 15,280 full-service financial advisors in branch offices in all 50 states and 3,328 licensed financial specialists in retail stores across the United States. [2] WFA offers a range of fixed income solutions, including municipal securities, to its clients.

Although WFA is not a municipal advisor, it offers this brief comment to express concern about the breadth of the principal trading prohibition in Draft Rule G-42.

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[1] MSRB Notice 2014-01 Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisor (January 9, 2014), http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-01.ashx?n=1

[2] WFA is a non-bank affiliate of Wells Fargo & Company ("Wells Fargo"), a diversified financial services company providing banking, insurance, investments, mortgage, and consumer and commercial finance across the United States of America and internationally. Wells Fargo has more than 264,000 team members across more than 80 businesses. Wells Fargo's brokerage affiliates also include Wells Fargo Advisors Financial Network, LLC ("WFAFN") and First Clearing, LLC, which provides clearing services to 78 correspondent clients, WFA and WFAFN. For the ease of discussion, this letter will use WFA to refer to all of those brokerage operations.

I. G-42 Should Not Prohibit Principal Transactions by Affiliates of a Municipal Advisor.

Draft Rule G-42 would prohibit municipal advisors and their affiliates from "engaging in any transaction in a principal capacity" with a municipal entity or obligated person.[3] WFA believes that a prohibition extending to affiliates is overly broad and would be unduly burdensome to municipal advisors and their affiliates.

Large financial institutions, such as Wells Fargo, may have numerous affiliates conducting business with municipal entities and obligated persons. Some such affiliates may be municipal advisors, but under Draft Rule G-42, any affiliate of a municipal advisor would be subject to a ban on principal transactions with municipal entities or obligated persons. In order for a municipal advisor to avoid a violation of the principal transaction prohibition in Draft Rule G-42, the financial institution would need to identify whether any of its affiliates has a business relationship with any of the municipal advisor affiliate's clients and scrutinize the nature of this activity to determine whether principal trading may occur. The development of systems to enable tracking and analysis of affiliate relationships with municipal advisor clients would be unduly burdensome and costly to implement. Moreover, the restriction of principal trading by affiliates would not provide tangible benefit to the municipal entity or obligated person client.

The rule could amount to an outright prohibition on a non-municipal advisor's business with a municipal entity or obligated person client if generally conducted on a principal basis. In some cases a municipal entity or obligated person may have been a long-time client of the non-municipal advisor affiliate while the entity's relationship with a municipal advisor affiliate may be short-lived or episodic. Nevertheless, by applying the principal transaction prohibition to affiliates, the municipal entity or obligated person client may be forced to move business that would not otherwise be covered by the municipal advisor scheme to an unrelated entity regardless of the client's needs and preferences.

Moreover, as drafted, Rule G-42 would prohibit any principal transactions by an affiliate with a municipal advisor client regardless of the extent of connection between the non-municipal advisor affiliate to the municipal advisor relationship. Affiliates of large financial institutions often offer substantially different services, operate with distinct governance structures and employ information barriers. If, based on such factors, a non-municipal advisor affiliate is not connected to the municipal advisor relationship, the risk of a conflict of interest in a principal transaction between a municipal advisory client and the non-municipal advisor affiliate is significantly diminished.

WFA appreciates the intent of the MSRB to protect municipal entities and obligated persons from potential conflicts of interest. However, for the reasons stated above, WFA respectfully recommends that the prohibition on principal transactions should not extend to municipal advisor affiliates. At a minimum, the prohibition should be limited to principal transactions of affiliates that are directly related to the municipal advisory relationship that the municipal advisor affiliate has with the municipal entity or obligated person.

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[3] Notice at 12.

II. Prohibition on Principal Transactions Should be Narrowed.

The provision prohibiting principal transactions covers any transaction engaged in by either the municipal advisor or an affiliate with a municipal entity or an obligated person.[4] WFA believes this standard is too strict and that some potential conflicts may be properly disclosed and waived by an informed municipal entity or obligated person client.

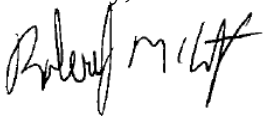
The Investment Advisers Act of 1940 recognizes that a client may give informed consent to permit a principal transaction notwithstanding a potential conflict of interest. For example, although investment advisers are subject to a fiduciary duty in dealing with their clients[5], an investment adviser may transact as principal after providing proper disclosure of the potential conflict and receiving client consent.[6] Furthermore, in contemplating a potential uniform fiduciary standard for brokers, dealers and investment advisers providing investment advice about securities to retail investors Congress made clear that a broker or dealer's practice of selling proprietary products is not a per se violation of a uniform fiduciary standard.[7] At the same time, it authorized the SEC to engage in a rulemaking to require brokers or dealers to provide notice and receive consent or acknowledgment from retail customers prior to transacting in proprietary products. By contrast, the MSRB asserts it is "questionable" municipal advisor clients could consent to any conflict presented by a principal transaction "given the high potential for self – dealing."[8]

WFA urges the Board to reconsider its strict principal transaction prohibition in light of other fiduciary standards that recognize the ability to cure a potential conflict with appropriate disclosure and client consent. Doing so would protect client access to a broader range of products offered by municipal advisors and their affiliates.

CONCLUSION

WFA appreciates the opportunity to share its views regarding the duties of non-solicitor advisors and commends the Board for its effort to elaborate on the duties of municipal advisors. For the foregoing reasons, WFA respectfully requests that MSRB reconsider the principal trading prohibition to remove the restriction for affiliates of a municipal advisor and to permit certain principal transactions with proper disclosures and consent. If you would like to further discuss WFA's position on this matter, please do not hesitate to contact me.

Sincerely,



Robert J. McCarthy
Director of Regulatory Policy

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[4] *Id.* at 12-13. The prohibition does include an exception for activities permitted by underwriters under Rule G-23.
[5] *SEC v. Capital Gains Research Bureau,* 375 U.S. 180, 194 (1963).
[6] Investment Advisers Act §206(3).
[7] Dodd-Frank Act Wall Street Reform and Consumer Protection Act, Title IX §913(g)
[8] *Id.* at 13.

March 10, 2014

VIA ELECTRONIC MAIL

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Draft Rule G-42

Dear Mr. Smith:

Thank you for providing this opportunity for us to provide the following response to the Municipal Securities Rulemaking Board's ("MSRB") proposed Rule G-42, on Duties of Non-Solicitor Municipal Advisors. Winters & Co. Advisors, LLC is responding to certain questions in the General Matters section (2, 5, 7, 9, and 11) of the proposed Rule G-42.

2. Do commenters agree that a municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities should have an obligation, unless agreed to otherwise by the advisor and client, to review thoroughly the entire Official Statement? Should a municipal advisor be permitted to limit the scope of the engagement such that the advisor is not required to review the Official Statement? If so, under what circumstances should this limitation be allowed? Should any duty to review the Official Statement be limited to any portions of the Official Statement directly related to the scope of municipal advisory services?

Response:
Winters & Co. Advisors, LLC is normally retained by clients to assist with the investment of bond proceeds. Because our role is so limited, and the scope of the official statement so broad, we believe that it makes sense to be allowed to limit our responsibility regarding review of the official statement to only those items that have an impact on our engagement. Winters & Co. Advisors will disclose in the engagement document, the specific sections of the Official Statement for which we will review.

5. Draft Rule G-42 allows fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client, but requires written full and fair disclosure of the arrangement. Should such fee splitting arrangements be prohibited, regardless of whether they are fully and fairly disclosed?

Response:
There are situations where a municipal entity or obligated person may want their municipal advisor or other professionals (including underwriters, if after the underwriting period) to receive

compensation from investment or other service providers for providing oversight and performing other services. A written full and fair disclosure of any fee splitting or fee sharing is sufficient and these arrangements should not be prohibited.

7. Should a municipal advisor be required to obtain a written acknowledgment from the client of receipt of the conflicts disclosure and consent to any conflicts disclosed before proceeding with a municipal advisory engagement?

Response:
Requiring the municipal advisor to obtain a written acknowledgement of receipt of a conflicts disclosure is unnecessary. It is often difficult to obtain these written acknowledgements from the client.

9. Should the MSRB, in furtherance of its mandate under the Dodd-Frank Act to protect municipal entities and obligated persons, require professional liability insurance by municipal advisors, and if so, should the MSRB specify the minimum amount and terms of such coverage?

Response:
On more than one occasion we have unsuccessfully attempted to obtain liability insurance. I believe liability insurance may not be available for our firm because our business does not fit into an existing liability insurer category. Therefore, we strongly feel that requiring liability insurance will be an undue barrier for existing and potential municipal advisors.

11. Should an advisor be required to review any feasibility study as part of the information considered in its evaluation of whether a transaction it recommends is suitable for the client?

Response:
A feasibility study is extraneous to the investment of the bond proceeds and therefore an advisor should only be required to review the feasibility study if it pertains to their engagement.

Winters & Co. Advisors, LLC appreciates the opportunity to respond to the MSRB, and is hopeful that the MSRB will take into consideration small municipal advisor firms when developing not only G-42, but all rules going forward relating to municipal advisors.

Sincerely,

Christopher J. Winters

WM Financial Strategies

11710 ADMINISTRATION DRIVE
SUITE 7
ST. LOUIS, MISSOURI 63146
(314) 423-2122

March 10, 2014

Municipal Securities Rulemaking Board
Attention: Ronald W. Smith
Corporate Secretary
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Request for Comments to Draft Rule G-42

Ladies and Gentlemen:

I am a sole proprietor doing business as WM Financial Strategies. I have a career devoted entirely to public finance and have been an independent financial advisor (now known as a Municipal Advisor) since 1989. In my capacity as an independent Municipal Advisor, I am writing to set forth my comments relating to the Municipal Securities Rulemaking Board's Draft Rule G-42.

1. Consider the Regulatory Burdens Imposed on Municipal Advisors as Required under the Dodd-Frank Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") mandates the Municipal Securities Rulemaking Board (the "MSRB") to establish rules relating to the conduct and qualifications of Municipal Advisors. In addition, the Dodd-Frank Act states that the MSRB may ***"not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors…"***

In establishing this provision of the Dodd-Frank Act, it is apparent that the intent was to protect small Municipal Advisors from forced regulatory exodus. Prior to the adoption of the Dodd-Frank Act, the writers met with certain Municipal Advisors and were aware that many Municipal Advisors are sole proprietors or associated with small businesses. Clearly the intent was not to reduce the number of Municipal Advisors. The existence of a large number of Municipal Advisors increases competition, thereby reducing cost, and provides Municipal Entities greater flexibility to select a Municipal Advisor best qualified for each of their particular transactions.

In Draft Rule G-42, the MSRB noted that the rules **could result in the consolidation or elimination** of Municipal Advisors. This outcome would be inconsistent with the Dodd-Frank Act and the MSRB should consider such an outcome to be unacceptable. Rules that result in a reduction of the number of Municipal Advisors or the consolidation of Municipal Advisory firms are not in the public interest and will harm Municipal Entities in the following ways:

a) Fewer Municipal Advisors equates to a loss of competition and consequently higher fees,

b) Fewer Municipal Advisors equates to fewer choices which will likely force Municipal Entities to select less experienced or less qualified Municipal Advisors for particular transactions, and

c) Fewer Municipal Advisors will result in less access whereby many Municipal Entities will be unable to engage Municipal Advisors. For example, access to Municipal Advisors in Missouri is already limited. I am the only full-time Municipal Advisor within the St. Louis metropolitan area. In addition to serving St. Louis metropolitan area issuers, I serve issuers in rural areas in Illinois and Missouri in a more than 180 mile radius of St. Louis. On the other side of the state, in the Kansas City metropolitan area, there are only a handful of Municipal Advisors and there is only one other full-time advisor in the balance of the entire state. If the number of Municipal Advisors is reduced, large numbers of Municipal Entities will not have access to Municipal Advisors and will be forced to rely on the advice of local banks or underwriters who have no fiduciary duty to Municipal Entities.

2. Definitions

For purposes of my comments, I have identified three types of Municipal Advisors:

1. "Independent Municipal Advisors" – Municipal Advisors whose primary business is assisting with the structuring and issuance of municipal securities but are not associated with any brokerage firm and are not investment advisors.

2. "Investment/Municipal Advisors" – Independent Municipal Advisors that are also investment advisors.

3. Broker-Dealer/Municipal Advisors – Individuals at brokerage firms who are registered broker-dealers, serve as underwriters and periodically serve as Municipal Advisors.

3. Liability Insurance

In the Request For Comments, the MSRB asked:

"Should the MSRB, in furtherance of its mandate under the Dodd-Frank Act to protect municipal entities and obligated persons, require professional liability insurance by municipal advisors …"

Liability insurance should not be required due to the following:

a) Numerous Municipal Advisors that can't afford insurance policies or cannot obtain insurance regardless of cost would be forced out of business.

b) An unqualified Municipal Advisor does not become a better Municipal Advisor with the acquisition of insurance. The MSRB's goal should be to enhance the qualifications of Municipal Advisors not to force Municipal Advisors out of business.

c) An insurance requirement is likely to result in the elimination of some of the most experienced and qualified Municipal Advisors in the country. Municipal Advisors with more than 35 years of public finance experience are more likely to retire than satisfy complicated disclosure rules or purchase liability insurance.

d) Based on my recent inquiries regarding the availability of insurance, it is unclear whether any insurance is available that provides coverage for the activities of Independent Municipal Advisors. (Insurance is available for Investment/Municipal Advisors and Broker-

Dealer/Municipal Advisors as it relates to their sale of securities activities but may exclude coverage for their activities relating to the structuring and issuance of securities.)

e) Insurance may not be available in every state. Based on my review of insurance to date, I have been unable to obtain professional liability issuance in Missouri regardless of cost.

f) Although no agent has been able to find a policy for me to date, I have been advised that if a policy is located, based on the terms and conditions I have requested for $1,000,000 coverage, the fees would be astronomical and would be more than 10% of my annual net income.

If the MSRB's goal is to reduce the number of Municipal Advisors in conflict with the mandate under the Dodd-Frank Act then, and only then, should liability insurance be required.

4. Disclosures Regarding Liability Insurance

In the Request For Comments, the MSRB asked:

> *"Are there lower-cost alternatives to requiring disclosure of the amount of professional liability coverage carried by the municipal advisor that would provide comparable benefits to clients of municipal advisors?"*

There is no direct cost to "requiring disclosure;" nor is there any direct benefit. The MSRB should consider the following: Have any studies been completed that show professional liability coverage benefits issuers? Are underwriters required to disclose their insurance coverage to issuers? Did the Dodd-Frank Act suggest that Municipal Advisors should make disclosures regarding insurance or did the Dodd-Frank Act require rules relating to standards of training, experience, and competence?

Based on my understanding of the foregoing, I am recommending that the MSRB omit from the Rule liability insurance coverage disclosures.

In the event the MSRB determines that disclosures are required consider the following:

Uniformity of disclosure is imperative.

Municipal Entities may assume that all of the three types of Municipal Advisors, defined above, have or could have liability insurance with comparable terms; however, as already indicated, Broker-Dealer/Municipal Advisors and Investment/Municipal Advisors may have access to insurance that Independent Municipal Advisors are not able to obtain. Furthermore, the liability insurance coverage provided for Broker-Dealer/Municipal Advisors, Investment/Municipal Advisors and Independent Municipal Advisors may be entirely different. It is important that disclosures be based on the same terms of coverage otherwise it may appear to issuers that Municipal Advisors that are Broker-Dealer/Municipal Advisors and Investment/Municipal Advisors have insurance even if they have no insurance coverage relating to the structuring and issuance of municipal securities. Stated differently, if Municipal Advisors are required to disclosure whether or not they have liability insurance, those that have insurance should be required to precisely describe the securities activities that are and are not covered.

5. Draft Rule G-42 has Unachievable Provisions

Draft Rule G-42 states that "With respect to a client that is a municipal entity, a Municipal Advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest". The requirement to **recommend the best transaction** goes well beyond traditional fiduciary duties. This provision needs to be rewritten as follows: With respect to a client that is a municipal entity, a municipal advisor may only recommend a municipal securities transaction or municipal financial product that **it reasonably believes** is in the client's best interest".

Municipal Advisors working in conjunction with their clients must make judgment calls based on current circumstances. Municipal Advisors must deal with changing regulations and changing market conditions that make it impossible to determine the "best transaction" except with twenty-twenty hindsight. The following are examples of situations that require judgment calls that will not necessarily result in the best transaction:

a) Should an issue be delayed when rates are rising?

b) For advance refunding issues, should the client proceed in a low interest rate environment or wait until a date closer to the call date?

c) When Build America Bonds ("BABs") were available, a choice had to be made whether to issue traditional tax-exempt bonds or BABs. Today, many issuers of BABS regret having issued such bonds in light of the sequestration reduction of subsidy.

Financial decisions are not black and white. The role of a Municipal Advisor should be to work with the client with the objective of achieving excellent and appropriate financial results.

6. Fees Should Not be Treated as a Conflict of Interest Requiring Disclosure

In February 2011, the MSRB proposed Rule G-36 that included APPENDIX A - "Disclosure of Conflicts of Interest With Various Forms of Compensation." APPENDIX A outlined the following fee arrangements: (i) fixed fees, (ii) hourly fees (iii) contingent fees (iv) fees paid under a retainer agreement, and (v) fees based upon the amount of the transaction. In APPENDIX A, the MSRB suggested that with the exception of fees paid under a retainer agreement (an uncommon method of compensation for Municipal Advisors) each of the other compensation arrangements has potential conflicts of interest. Recently, the MSRB released questions and answers relating to its February 6 webinar on Rule G-42 titled "MSRB Responses to Webinar Questions." In the MSRB Responses to Webinar Questions, the MSRB noted the 5 fee arrangements described above and stated that "Each of these forms of compensation has associated potential conflicts of interest."

The concept that every type of fee or that a particular fee arrangement creates a conflict of interest that requires disclosure should be eliminated from the Rule. Disclosure of fees based on "potential" conflicts of interest is inappropriate due to the following:

a) A Municipal Advisor's fiduciary duty should govern whether the particular fee arrangement is appropriate.

b) A "potential" conflict of interest attributable to a fee arrangement is not a conflict of interest and the fiduciary duty will curtail any improprieties.

c) Unnecessary disclosures are likely to confuse rather than assist Municipal Entities. The confusion is enhanced since the MSRB does not provide viable alternative fee arrangements that can be offered. Based on the MSRB's view of fee arrangements, each alternative would create a conflict requiring further disclosure.

d) Unlike underwriters that must disclose their contingent fee arrangements, a Municipal Advisor is required to act in the best interest of their clients. Accordingly good advice will prevent a fee arrangement from creating a "conflict."

e) Municipal Advisors should work to provide the best results for the client rather than attempting to mitigate problems that don't exist.

f) The MSRB rules should focus on serving the best interests of Municipal Entities rather than attempting to prevent conflicts of interest that don't exist.

Rather than disclosing potential problems with a particular fee arrangement, a Municipal Advisor should work with the client to establish a fee arrangement that best meets their needs. In the MSRB's August 2013 report for issuers titled "Financial Considerations for Hiring Municipal Advisors" the MSRB wrote that it is essential for a state or local government issuer to determine whether the proposed compensation arrangement will meet its needs. In the report, the MSRB also indicated that "Depending on the nature and extent of work to be performed by the municipal advisor, an issuer may favor one type of compensation structure over another. Consequently, the goal of Municipal Advisors should be to establish reasonable fees that meet the needs of the issuer.

For my clients, I establish fee arrangements that I believe are in their best interest based on the specific transaction under consideration. Depending on the transaction, my fee may be based on an hourly rate or a fixed fee that is (i) contingent upon the completion of a transaction or project, (ii) non-contingent, or (iii) non-contingent with a contingent component. Prior to commencement of services, I review the scope of the transaction and services to be provided and thereafter set forth the fee arrangement in writing.

The following are a few examples of the fee arrangements I utilize for specific types of transactions:

I am often engaged to structure and arrange the sale of municipal securities after a determination has already been made by the municipality to issue securities to finance a specific capital project (e.g. voters have approved a specific amount of general obligation bonds). For these municipal securities issues I generally charge a fixed fee that is contingent on the completion of the transaction. Many of my clients are small issuers with limited budgets that plan to pay costs of issuance, including financial advisory fees, from the proceeds of the securities. When capital funding is required, municipal issuers rely on the expertise of their financial advisor to develop marketable bond structures and to actively locate broker-dealers willing to underwrite the issue.

I also charge contingent fees for refunding transactions. The feasibility of these transactions is dependent upon market conditions. As part of an authorizing resolution or contract, I generally predefine the level of savings to be derived (e.g. 3% of present value savings or other generally accepted feasibility criteria). I believe this arrangement eliminates any conflict of interest by insuring that the transaction will be terminated if pre-determined savings will not be realized. Furthermore, if interest rates rise I want to advise my clients not to proceed with the transaction. I do not want to be paid and to be the only party that benefits from a terminated refunding.

Contingent fee arrangements benefit Municipal Entities by insuring that their governmental funds will not be drawn upon for payment of fees if the transaction is not completed.

For projects that require a significant amount of planning or feasibility analysis and that may be terminated as a result of my analysis or recommendations, I typically charge either a fixed fee with all or a portion of the fee being non-contingent or an hourly non-contingent fee.

In each of the situations mentioned above, the fee is intended to provide the most appropriate option for my clients. Therefore, the MSRB should not require conflict of interest disclosure of fee arrangements that do not inherently create conflicts of interest.

7. Mitigation of Fee Conflicts of Interest

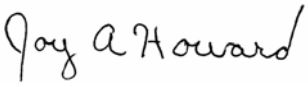
The proposed rule requires that typical fee arrangements be treated as a conflict of interest requiring disclosure. Additionally, the rule requires that "Such disclosures also must include an explanation of how the advisor addresses or intends to manage or mitigate each conflict." As noted above, there is no way to mitigate a fee conflict of interest since the MSRB has suggested that every fee arrangement creates a conflict of interest. The inability to mitigate a "fee as a conflict of interest" is further justification to eliminate treating fees as creating conflicts of interest.

8. Summary

Prior to the 1970's there were very few Municipal Advisors. While the use of Municipal Advisors has increased since that time, a substantial percentage of bond issues continue to be completed without a Municipal Advisor. As a result, many municipal transactions have higher than necessary costs of issuance, higher than necessary interest rates, and detrimental financial covenants. The MSRB must consider whether the proposed rule will result in improved Municipal Advisory activities or result in an exodus of Municipal Advisors. The MSRB must consider whether it is in the public interest to have a large pool of qualified Municipal Advisors from which issuers may make a selection. Alternatively, the MSRB can impose rules that eliminate a large number of Municipal Advisors, increase Municipal Entities' costs due to lack of competition, and encourage Municipal Entities to work solely with underwriters that have no fiduciary duty to their clients.

I respectfully request that the MSRB modify the Draft Rule G-42 as described herein.

Sincerely,



Joy A. Howard
Principal

Comment on Notice 2014-01

from Christopher Woodcock, Woodcock & Associates, Inc.

on Tuesday, January 14, 2014

Comment:

Woodcock & Associates, Inc. is a small (one person) organization that provides consulting services to municipal entities throughout the world related to the development of water and wastewater rates. Because our work sometimes involves recommendations on financing capital improvements, we sometimes provide recommendations regarding the amount and timing of municipal bond issues to finance capital programs that have been developed by others. We are not responsible for recommending actual bond issues or the types of issues - this is typically done by the municipality' Financial Advisor. Rather, we make broad recommendations on the mix of bonds and current revenues to use, and sometimes the timing of when bond proceeds may be needed.

We are also asked to provide consultant certificates on the the adequacy of (water or wastewater) revenues to meet bonded debt requirements and annual coverage on revenue bonds. We have been doing this work for 20 years and are well known and respected throughout the USA.

We have never carried any professional liability insurance. We have found that it is not necessary and far too costly for a small organization. We hope that any new rules would not require such insurance. We have no problem disclosing our lack of such insurance and have not found this to be a problem with any of our 100+ clients. The requirement to carry such insurance may lead us to suspend the tangential services that would cause such a requirement. I do not believe that the removal of independent consultants that have no direct connection to the sale or marketing of securities or the choice of kinds of securities would be in the public interest.

The services we provide (water and wastewater rate consulting and revenue projections) are highly specialized and concentrated in a few dozen experts across the country; primarily in smaller firms. It is unclear where we would receive any formal training or continuing education since those of us at the top of this field are typically the ones putting on seminars and preparing manuals of practice (published by the American Water Works Association and Water Environment Federation, for example). Requirements for CEUs in our field would provide little, in any, added value to those that provide so much of the training.

While the cost and time involved with the registration as a Municipal Advisor with the MSRB is minimal, it is an added cost to smaller organizations such as ours. Following the new rules takes us away from work for our clients. At this point, the added time and expense is not excessive. We understand the need for the registration and oversight in this market sector and expect it will improve the services received by municipalities. We hope that any new rules or requirements will not cause additional burdens that we would not be able to meet.

Thank you for the opportinity to comment.

WULFF, HANSEN & CO.
ESTABLISHED 1931
INVESTMENT BANKERS
351 CALIFORNIA STREET, SUITE 1000
SAN FRANCISCO 94104
(415) 421-8900

March 17, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Dear Mr. Smith:

Thank you for the opportunity to comment on Regulatory Notice 2014-01. Wulff, Hansen & Co. is an 80-year-old FINRA member broker/dealer and a registered municipal financial advisor active in the California market. Most of our issuer relationships are of a long-term nature, some dating back decades. With some clients we serve exclusively as municipal advisor, with others solely as an underwriter. Certain clients may retain us as either depending on the facts and circumstances of a particular project.

Our comments below address the various sections of Draft Rule G-42 individually, followed by our response to certain questions contained in the Notice.

G-42(a)

In many localities municipal advisors have long had fiduciary duties under State law and a new uniform standard applying to advisors nationwide is appropriate, creating a more level playing field across the nation.

We generally support the other concepts underlying Draft Rule G-42(a). G-42(a)(v) allows fee-splitting arrangements so long as they are properly disclosed. This should be retained as such arrangements can sometimes be efficient and beneficial to the client: An example might be when the advisor engages a specialist to perform a particular type of financial analysis and compensates him out of the advisor's fee. G-42(a)(v) should be modified to make clear that the advisor's arranging for routine purchase of services on behalf of the client in a transaction with an entity in which the advisor has an interest (e.g, purchase of services from DTCC when the advisor is also a DTCC Participant and thus part-owner) does not constitute disclosable 'fee-splitting' (or a principal transaction) for purposes of the Rule when the services in question cannot be purchased from another unrelated entity.

In addition, Supplementary Material .01, on the 'Duty of Care', raises potential difficulties. The requirement that the advisor undertake a 'thorough review' of an entire Official Statement unless specifically relieved of that duty by the client is unreflective of how things work in the real world. Of course all parts of an Official Statement require review, and that review is best conducted by subject matter experts. In actual practice, an advisor 'thoroughly reviews' those

portions of the OS which fall within its professional competence, leaving word-by-word review of technical legal documents to counsel, of engineering data to engineers, and so forth. The advisor will likely also 'review' those sections as well, but is not necessarily competent to form a judgment or be an arbiter as to whether they are properly prepared. Requiring the advisor to conduct and document a 'thorough' review of every word in every section and appendix of the OS would be duplicative and thus increase costs with no commensurate benefit. Division of labor in the review of the Official Statement is a matter best left to those most familiar with the issue: Issuer staff, the advisor, counsel(s), and other members of the team. It should not be prescribed in the Rule. In addition, the cost of thoroughly documenting such a review would be excessive and would unduly burden small issuer clients who would ultimately pay the bill.

G-42(b)

If Draft Rule G-42(a) is adopted as proposed, making municipal advisors subject to a fiduciary duty with regard to its municipal clients, Draft Rule G-42(b) may well be unnecessary and redundant. The fiduciary duty would, in our view, in and of itself require disclosure of items specified in G-42(i) through (v) as well as (vii). We believe (vi) is unnecessary, as the conflicts posed by the various means of compensation are both inherent and obvious upon even the most cursory reflection. Few issuer officials can be unaware that a person compensated solely by completion of a transaction has an incentive to ensure that the transaction takes place, or that persons paid by the hour have incentive to spend more hours on their tasks than might be the case in a fixed-price engagement. These are common-sense conflicts that all of us confront every day as we engage professionals, tradespeople, and others. That said, including (vi) would likely do no harm other than as a source of confusion and suspicion, but we think it is simply unnecessary.

We find items (viii) and (ix) to be inappropriate. In the case of (viii) we are not aware of any other industry or profession – not law, not medicine, not dentistry, not engineering, not anything - whose overseers require provision of this information. Purchase of such insurance is a business decision and says nothing about the firm or individual's professional competence. Indeed, one can argue that those who knowingly do poor work are more likely to purchase insurance than are those having strong professional qualifications and who are more careful in their conduct. Further, issuers who are concerned with this often request the information in their RFP or other proposal. Others do not, and issuers should remain free to choose what they want to know about a vendor's insurance arrangements.

In the case of (ix), this also greatly exceeds what is required of other professions. Such information is already publicly disclosed on Form MA or MA-1. We suggest as an alternative that advisors be required to provide potential clients with a link or other information directing them to the website or other place where such information can be reviewed should the client wish to do so.

The final sentence of proposed Rule G-42(b) is unnecessary and in practice redundant. Assuming that G-42(i) is adopted as written, the subject of conflicts would be adequately addressed. G-42(i) requires disclosure and thus an advisor who discloses none is effectively asserting that he has none to disclose.

G-42(c)

We support Draft Rule G-42(c) except that G-42(c)(ii) should better reflect the fact that at the beginning of an engagement, and often for a long period of time after commencement, it is not possible to know even in very round numbers what an advisor's compensation might be. The terms of compensation are laid out in the agreement, but the number of hours or the size of a financing may in the end vary by as much as an order of magnitude. Requiring hypothetical examples would likely confuse the client and at best is of small utility, and at worst could give a highly erroneous impression of the ultimate cost of services. Ensuring that the terms of compensation are clear and unambiguous is the best solution at this point in the engagement.

G-42(d)

Draft Rule G-42(d) is generally reasonable, but needs to make clear the advisor's duty in cases where the client, for political or other reasons, wishes to engage in a transaction that in the advisor's opinion is not financially or economically beneficial. Such actions are not uncommon, particularly in areas where the issuer perceives social, political or other intangible benefits associated with the project. A solar installation which costs more than its fossil-fuel equivalent would be an example. Although Supplementary Material .03 states than an advisor would not be required to resign rather than assist in such a project, additional details of his obligations and responsibilities - both those removed and those which still exist - in such circumstances should be included.

G-42(e)

Draft Rule G-42(e) is unnecessary, as the obligations it imposes are already contained in G-42(a)(i) and (ii), G-42(c) and G-42(d). They are part of standard advisory work.

G-42(f)

Draft Rule G-42(f) should specify that the sale of other additional municipal advisory or related services (the latter properly defined to protect the client) does not constitute a 'principal transaction'.

G-42(g)

We support Draft G-42(g) except that G-42(g)(ii) should be modified to apply only to inaccuracies resulting in overstatement of the fees, expenses, or activities being billed for. Advisors frequently understate or do not charge at all for incidental services provided in the context of a long-term and mutually satisfactory relationship, perhaps to help the client keep a project within budget, to avoid the appearance of 'nickel-and-diming' him, or because calculating the exact amount due for a particular small task would not be justified by the revenue involved. Allowing the advisor to understate or forgo part of an amount technically due him is good for the client and should be left to the advisor's discretion.

Supplementary Material:

Other than our comment above on Supplementary Material .01 and our requested clarification of duties and responsibilities in the circumstances to which .03 applies, the balance of the Supplementary Material is useful and we support it as proposed.

Other Questions

The Regulatory Notice asks whether advisors should be required to obtain written acknowledgment of, and consent to, their disclosures. We think not. In our experience, obtaining written acknowledgement from the proper issuer officials can be difficult and in many cases impossible. Indeed, we understand that certain issuers have been advised by counsel that they are never to sign such an acknowledgement under any circumstances. A reasonable approach would be to require that the advisor document his request for such an acknowledgement rather than mandate that he actually receive it.

The Notice asks whether advisors should be required to purchase professional liability insurance. We would oppose this idea in the strongest terms. We know of no other profession required to do so. Purchase of insurance is a business decision to be made by each advisor. Issuers who are interested in the matter can inquire, and in our experience many of them do so. Municipal advisors can purchase many other commercial services which may benefit or protect the clients such as sophisticated software, fire insurance covering its premises and the client work product stored therein, firewalls protecting confidential client information, technical consultants working on the clients' behalf, and so on. The list is endless. The purchase of business services is a business decision and not an appropriate subject for regulation. In addition, smaller firms might well find themselves priced out of the market and in poor market conditions insurers could cease offering such coverage at any price as has happened in the past with similar types of insurance.

The Notice asks if advisors should be required to review any feasibility study as part of its suitability evaluation. We do not think such a review should be mandated by Rule. Each engagement is structured in light of the facts and circumstances surrounding it, and the advisor's specific scope of work should be left to the parties. The same considerations expressed above regarding Supplementary Material .01 apply here. The advisor's role could be such as to not require this review, or the feasibility study could be of such a technical nature that review by the advisor would not be useful and were better left to a technically qualified party on the team whose opinion could then inform that of the advisor.

Thank you again for the opportunity to comment on this Regulatory Notice.

Very truly yours,

Chris Charles
President

The Yuba Group LLC

Yuba Group Advisors LLC
130 West 30th Street, Loft 12C
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T 212 518 6166
F 212 937 3872
www.yubagroup.com

March 7, 2014

Via electronic submission
Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: MSRB Notice 2014-01 Request for Comment on Draft Rule G-42, on Duties of Non-Solicitor Municipal Advisors

The Yuba Group appreciates the opportunity to provide comments in response to the Municipal Securities Rulemaking Board ("MSRB") proposed Rule G-42, on Duties of Non-Solicitor Municipal Advisors. The Yuba Group commends the MSRB's continued effort in working with and listening to market participants as new MSRB Municipal Advisor Rules are drafted.

Background

The Yuba Group is a seven-person advisory firm formed in 2010. Our work is focused solely on higher education and not-for-profit institutions. In addition to assisting with tax-exempt and taxable debt transactions, as well as interest rate swaps, we provide on-going services related to capital financing, debt policy/capacity and rating strategies.

Our clients include a range of public and private colleges and universities, as well as research, cultural and other types of not-for-profit institutions. Current clients include several Ivy League institutions and other major research universities – both public and private- as well as liberal arts schools and "niche" institutions. We do not advise any issuing authorities. Our partners and other personnel have many years of prior experience at investment banks, rating agency and other financial services and swap advisory firms.

Comments on MSRB Draft Rule G-42

General Matters

The Yuba Group offers these comments in response to certain questions in the General Matters section (1, 2 and 9) posed in the MSRB Draft Rule G-42, as follows.

1. Draft Rule G-42 follows the Dodd-Frank Act in deeming a municipal advisor to owe a fiduciary duty, for purposes of the draft Rule G-42, only to its municipal entity clients. Is carrying forward that distinction in the draft rule appropriate in light of the services a municipal advisor provides to its obligated person clients? Would having a uniform fiduciary standard applied to all of a municipal advisor's clients facilitate compliance with the draft rule or provide better protection for issuers? If so, are there any legal impediments to the MSRB extending a fiduciary duty in the draft rule to all clients of a municipal advisor?

Response:

Although the Yuba Group understands that the Dodd-Frank Act specifically requires a fiduciary duty to municipal entities and not "obligated persons," we believe there should be no distinction between these types of borrowers and a uniform fiduciary standard should apply to all municipal advisor clients. As a municipal advisor, we would not view our responsibility to our private, 501(c)3 institutions as any less than to our public university clients. In fact, we would argue that some of the smaller private institutions were more adversely affected by the heavy marketing of auction rate and swap structures than public institutions of higher education who may have access to additional resources and expertise in evaluating the benefits and risks associated with such products. It is also possible that the lower "duty of care standard" imposed on municipal advisors to 501(c)3 institutions may not provide these institutions with adequate protection.

The Yuba Group encourages the MSRB to utilize a uniform fiduciary standard for both municipal entities and "obligated persons."

Additionally, although the Yuba Group understands that the SEC has defined "obligated person" as the same meaning in section 15(B)e(10)[1], the effect of this means that there are no restrictions on providing advice to 501(c)3 institutions for future issues of debt until they have made an application to or are in negotiation with an issuing authority. By the time a borrower makes an application to an issuing authority, a bond structure has already been determined in most cases. This allows bankers, planning to act in the capacity of underwriters, to provide advice up until that point to 501(c)3 institutions. The use of the "obligated person" structure also may add a level of ambiguity since not all issuing authorities have formal applications. If the MSRB is able to broaden the application of the Rule such that an "obligated person" is not based on "per issue" basis, but rather a 501(c)3 institution who could potentially be, or intends to become, an "obligated person," that would eliminate such ambiguities and remove the status of the issuing authority application from impacting the ability to provide advice.

[1] As such, the definition in Rule 15Ba1-1(k) provides that obligated person has the same meaning as in Section 15B(e)(10)) and means "any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities."

The Yuba Group recommends that the MSRB expand the G-42 requirements for an "obligated person" so that Rule G-42 applies to municipal bond issues prior to the application of a 501(c)3 institution and prior to application to an issuing authority.

2. Do commenters agree that a municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities should have an obligation, unless agreed to otherwise by the advisor and client, to review thoroughly the entire Official Statement? Should a municipal advisor be permitted to limit the scope of the engagement such that the advisor is not required to review the Official Statement? If so, under what circumstances should this limitation be allowed? Should any duty to review the Official Statement be limited to any portions of the Official Statement directly related to the scope of municipal advisory services?

Response:
As a municipal advisor (MA) to a borrower in the municipal market, we consider the review of the Preliminary and Final Official Statement (OS) as part of our responsibilities in implementing a bond transaction and will communicate to our client any inconsistencies, inaccuracies and omissions that we may find. The Yuba Group currently documents our method of reviewing the OS within our engagement agreements. However, the draft supplementary Material .01, regarding Duty of Care indicates that "a municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or municipal financial product that is related to an issuance of municipal securities must also undertake a ***thorough*** review of the official statement for that issue."

The Yuba Group would like clarification by the MSRB to ensure this "thorough" review does not require municipal advisors to perform due diligence or engage counsel to assist in such matters. If the municipal advisor were to be formally "responsible" for reviewing the disclosure document that may require them to hire counsel to perform diligence and provide them with a 10(b)5 opinion. If so, that will have the effect of increasing fees to the borrower. Additionally, there are other parties (underwriter, underwriter's counsel, borrower's counsel) who are already responsible for performing due diligence and, in the case of counsel, provide a 10(b)5 opinion on the Official Statement. It may also make the availability and costs of Professional Liability insurance prohibitive.

The Yuba Group requests that the MSRB clarify its meaning of a "thorough" review of the Official Statement required to be performed by municipal advisors, taking into consideration other parties that have responsibility over the content of the OS. We believe that an advisor's role should be focused on the appropriateness of the financing strategy, not investor disclosure.

9. Should the MSRB, in furtherance of its mandate under the Dodd-Frank Act to protect municipal entities and obligated persons, require professional liability insurance by municipal advisors, and if so, should the MSRB specify the minimum amount and terms of such coverage?

Response:
The Yuba Group has made the decision since our formation to obtain professional liability (PL) insurance despite its hefty cost. Each year, our insurance broker re-bids our PL and general liability (GL) insurance, often with very large increases in the premiums, and we are concerned that insurers may view the new regulatory environment and the potential requirement to have PL insurance as justification for increasing such fees even further. Often, our clients have specific requirements regarding PL and general liability coverage, and it may be more appropriate for these arrangements to be discussed between MAs and their clients rather than being mandated by the MSRB.

The Yuba Group recommends that the requirement as written in the draft remain the same which does not require PL insurance, but does require a disclosure of "the amount and scope of coverage of professional liability insurance, deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage."

Economic Analysis

The Yuba Group appreciates the MSRB's effort in obtaining supporting data, studies, or other information related to our views of the economic effects of the draft rule. Additionally, the Yuba Group, as a small municipal advisor, is happy to provide feedback regarding the potential economic impact of the draft rule and draft amendments on small municipal advisors.

The Yuba Group offers these comments in response to certain questions in the Economic Analysis section (specifically 13, 21, and 22) posed in the MSRB Draft Rule G-42, as follows.

13. To the extent that draft Rule G-42 and the draft amendments to Rules G-8 and G-9 impose costs on municipal advisors, will these costs be passed on to municipal entities or obligated persons in the form of higher fees?

21. How will the requirements of draft Rule 42 affect potential municipal advisors' decisions with respect to entry into the market?

Response to 13 and 21:
The financial model of small MA firms is fairly straightforward, and to the extent that our costs increase, we either have to decrease the amount we pay our employees and ourselves or attempt to increase our fees. In order to serve our clients with the level of care and loyalty to which we are committed, there are limited numbers of clients we can take on without increasing the number of our employees. In a truly service-oriented business, there are limited "economies of scale," and we are very cognizant of our clients' sensitivities to costs as they are under continuous pressures regarding affordability. In order to be truly independent, we do not have other business lines that can supplement our income, and it is often challenging to compete with the investment banks in attracting high quality personnel. We have a number

of fixed costs that are fairly expensive that enable us to perform our role (Bloomberg terminals, DBC software, Reuters etc.) in addition to salaries of our employees, and the costs of compliance, both direct and related to the "opportunity cost" of our time are daunting.

The Yuba Group believes that the costs associated with compliance with new regulations may have many unintended consequences, including the need for advisors to increase fees to cover such expenses, with issuers reluctant to accept such increases and some who may decide against hiring an independent advisor to avoid such fees entirely. The costs may also discourage highly qualified individuals from entering the profession. Smaller firms and those more specialized, will be particularly sensitive to the increased time and costs associated with compliance, compared with larger firms who may be able to enjoy any "economies of scale."

22. What training costs would the requirement of draft Rule G-42 cause at municipal advisory firms to ensure compliance?

Response:
As stated earlier, the Yuba Group focuses solely on higher education and not-for-profit institutions. Over the past couple of months, we have had to spend a great deal of time reviewing the 778-page SEC rule, the SEC guidance, existing MSRB rules and draft Rule G-42 in addition to speaking with counsel, clients and underwriters about the existing and upcoming regulations. Since our clients need to understand how communication with their bankers may change, we have spent time developing materials to explain the new rules to them and assist in the potential provision of the independent registered municipal advisor ("IRMA") exemptions. We estimate that compliance with the current MA rules will cost us over $50,000 for the first six months of 2014, for our small firm, which includes:

- Registration fees, time allocated to training staff, issuers;
- Outside consultant assistance for new rules and advice;
- Time allocation internally to learn the rules, discuss the rules, create internal documents, and prepare registration documents; and
- Time allocation for client education.

As the MSRB continues to introduce and implement new rules for municipal advisors, it would be more efficient, particularly for small firms, for these to be done on a consolidated basis, rather than "piecemeal," if at all possible. Having to review a series of rules released over time imposes greater time demands compared with a smaller number of rules which are more comprehensive in nature.

Other Matters for the MSRB's Consideration

The Yuba Group is aware that the MSRB is planning professional tests for the municipal advisor community.

The Yuba group recommends that the MSRB take into consideration the costs of administering these tests, especially for small firms. It is the Yuba's group calculation based on the cost of the tests, time studying, and lost wages, that this will be an additional $89,000 cost to the firm. In addition to these initial fees, we expect that there will also be annual continuing education fees associated with professional standards.

The Yuba Group recommends some suggestions as the MSRB develops professional standards to minimize costs in this regard:

- Acknowledge the length of prior advisory and/or investment banking work in establishing needs for examination or other requirements. For example, the MSRB could consider allowing professionals who have provided advisory service for many years to be exempt from taking the full exams, or only require them to complete some continuing education courses, whereas someone without experience with advisory work would need to pass the exam to demonstrate a basic knowledge of the industry and market;
- Grandfather those individuals who have been in this business for several years and were registered as Series 7, 52 and/or 53 in prior positions.

We encourage the MSRB to consider the potential impact and costs of compliance on small firms as it develops professional standards and requirements.

In closing, we recognize the challenges of drafting rules that will impact advisors, bankers and issuers with varying degrees of expertise and resources, and appreciate the opportunity to respond to the MSRB. We are hopeful that the MSRB will take our comments into consideration.

Thank you.

Linda Fan
Managing Partner

ZIONS BANK®

March 10, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors: MSRB Regulatory Notice 2014-01

Dear Mr. Smith:

Zions First National Bank ("Zions Bank") appreciates this opportunity to provide comments to the Municipal Securities Rulemaking Board ("MSRB") pertaining to Proposed Rule G-42 regarding enhanced standards of conduct and duties of municipal advisors when engaged in municipal advisory activities (the "Proposed Rule"). We would like to focus our comments on the broad blanket prohibition contained in the Proposed Rule against principal transactions between municipal entities and their municipal advisors.

We believe that such a prohibition should be applied on a transaction by transaction basis, and only to those transactions for which the municipal advisor actually serves as advisor to the municipal entity. We also believe that the prohibition should continue to reflect the kinds of exceptions that have consistently been articulated by the MSRB, as well as the Securities and Exchange Commission ("SEC"), ever since these enhanced standards of conduct and duties have been under consideration, including particularly the exceptions for traditional banking activities such as those that were described by the MSRB as "bank loans" and "true loans" in its filing of proposed amendments to Rule G-23 with the SEC [SEC Release No. 34-63946 (February 22, 2011) at pp. 35-36]. Further, we note that banks providing advice with respect to traditional banking services, which include but are not limited to "Any extension of credit by a bank to a municipal entity or obligated person, including the issuance of a letter of credit, the making of a direct loan, or the purchase of a municipal security by the bank for its own account" [240 CFR Section 15Ba1-1(d)(3)(iii)(B)], are not engaged in municipal advisory activities under the SEC's municipal advisor registration rules.

As we have mentioned in previous comment letters pertaining to these enhanced standards of conduct and duties, Zions Bank and its affiliates have provided, and continue to provide, a variety of traditional banking services to municipal entities throughout the western United States including deposit accounts, checking accounts, financial advisory services, and direct loans. We have spent a great amount of time and resources establishing the expertise necessary to provide these services to our municipal customers. Municipal entities are often some of the best customers banks like ours can have.

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We believe that if a municipal entity selects a bank to provide it with banking services including financial advisory services, the municipal entity should be free to borrow from the bank, and the bank should be free to make a direct loan to the municipal entity, if the municipal entity deems it to be in its best interests to do so. Thus we believe that Proposed Rule G-42 should not be interpreted or applied in any way that would prevent a municipal entity which has hired a bank or its affiliate to provide it with financial advisory services, from borrowing moneys directly from, or receiving other traditional banking services from, that bank, and that the language of the Proposed Rule should be revised to provide an explicit exemption for these services.

It would be profoundly paradoxical to suggest that individuals can be allowed to borrow money from the same banks that also serve as their fiduciary, for example in the capacity of a trustee for a personal trust, but that municipal entities – which levy, collect, and spend hundreds of thousands, millions, hundreds of millions, and even billions of dollars that they collect from their taxpayers and ratepayers – require the protection of an absolute prohibition against principal transactions like direct loans or other traditional banking services from banks that also serve as their financial advisor.

Banks often may be the sole source of certain types of financings for smaller municipal entities. And as mentioned above, municipal entities are often some of the best borrowing customers banks can have. During the recent financial downturn, municipal loans performed better than other types of loans for many banks. In addition, many of the direct loans we make to smaller and more remote municipal entities for which we also serve as financial advisor on unrelated issuances of municipal securities, qualify for Community Reinvestment Act ("CRA") credit from our banking regulators. Many of these borrowers are so small that their access to the capital markets is quite limited, and direct bank loans may be the only source of efficient and economic solutions for their capital needs. If adopted as proposed, Rule G-42 would likely increase costs to these entities.

The CRA requirements are designed to insure that banking organizations provide sufficient services to under-served individuals and communities in three specifically targeted areas: (i) loans, (ii) investments, and (iii) financial services. A bank must provide a sufficient amount of services under each of those three categories, to under-served individuals and communities in the geographic area which is served by the bank. A failure to meet the requirements in any one of the three categories is a failure to meet CRA requirements as a whole. If a bank serves as a municipal advisor in connection with bonds issued and sold publicly by a small, remote municipal entity in an under-served area, thus providing that under-served municipal entity with services which fall under the financial services CRA category, and the bank also provides direct loans to the municipal entity and purchases municipal obligations directly from the municipal entity for the bank's own investment portfolio, thus providing the under-served municipal entity with services which fall under both the loan and the investments categories as well, it would be unfair, uncompetitive and burdensome to the municipal entity, and contrary to the clear intent of CRA, to require the municipal entity to have to choose whether to obtain either financial services, or loans and investments, but not both, from its bank. We recommend that any proposal that might have the effect of curtailing the ability of banks to make loans to their municipal customers, and of municipal entities to obtain competitive, favorable loans from their banks, including those in under-served areas, should weigh these factors very carefully.

Some of the commentaries surrounding these enhanced standards of conduct and duties of municipal advisors have focused on when a municipal obligation acquired by a bank would constitute a security, and when it would constitute a loan for these purposes. As we have mentioned in our previous comment letters on the subject, in order for a municipal entity's promise to repay a direct loan from a bank (or from anyone else) to be legally enforceable under state constitutional and statutory municipal debt limitations and restrictions, the loan documents must contain the same basic provisions that conform to such limitations and restrictions as do the municipal bonds which have been designed to fit the particular type of municipal financial transaction that is involved. Thus, municipal loan and bond documents must of legal necessity often look essentially the same.

Nevertheless, it should be easy to differentiate between a municipal security and a direct loan for the purposes discussed in this letter. A simple test, consistent with established law, would be to determine whether a municipal obligation has been acquired by a bank with or without an intent to distribute it. If a bank acquires a municipal obligation directly from a municipality with the intent to distribute it, the obligation should be treated as a security. However, if a bank acquires a municipal obligation directly from a municipality for its own portfolio and investment, with no intent to distribute it, the obligation should be treated as a direct loan, even if the obligation is booked as a security on the bank's books. In addition to being consistent with established law, this test is simple to apply because any pattern of distribution in contravention of a stated intent not to distribute could easily be detected and dealt with appropriately. In this regard it should be remembered that banks are highly regulated and audited entities.

To our knowledge, Zions Bank has never transferred to a third party any municipal obligation it has purchased directly from a municipality for its own portfolio and investment. Even if the Bank later wanted to transfer it, there is usually a strong accounting disincentive to do so. When Zions Bank purchases municipal obligations directly for its own portfolio, the vast majority of such obligations are immediately received into, and must be maintained in, a "held-to-maturity" ("HTM") account. Zions Bank routinely holds upwards of $1 billion or so of municipal obligations in its HTM accounts. If the Bank were to transfer any municipal obligation out of an HTM account, that transfer alone could vitiate treatment as held-to-maturity for all obligations held in that account (not just the one being transferred), which would subject all such obligations to mark-to-market requirements that could pose significant financial disadvantages to the Bank. So in addition to Zions Bank's having no intent to distribute municipal obligations it purchases directly from municipalities for its own portfolio, there are also significant accounting and financial disincentives to distributing, selling, or otherwise transferring any such municipal obligation from its HTM portfolio.

In conclusion, as a national banking organization serving a wide variety of municipal customers throughout the western United States for over a hundred years, we believe that our extensive knowledge and experience in helping municipal customers to meet all of their financial needs gives us the broad range of expertise that is necessary to provide them with adequate and complete financial advisory services. We wonder whether entities with less capital and resources have the expertise necessary to provide comparable services.

We believe our position on this matter is correct and would welcome an opportunity to discuss this issue further. We hope our comments will provide additional context and insight into an important and challenging issue.

We participated in the development of the American Bankers Association's comments to you on the Proposed Rule [letter from Cristeena G. Naser, dated March 4, 2014] and wish to express our support for and endorsement of those comments.

Because they may be interested in the final outcome of these issues, in addition to forwarding a copy of this letter to the SEC, we have also forwarded copies to the primary regulators of our banking affiliates – the Board of Governors of the Federal Reserve System ("Federal Reserve") in the case of our bank holding company, the Office of the Comptroller of the Currency ("OCC") in the case of our national banks, and the Federal Deposit Insurance Corporation ("FDIC") in the case of our state chartered banks.

If you have any questions concerning this letter or would like to discuss these observations further, please feel free to contact Gary Hansen at Zions First National Bank, Investment Division, One South Main, 17th Floor, Salt Lake City, Utah 84133; Telephone: 801-844-7762; E-Mail: Gary.Hansen@zionsbank.com. Given our broad background in municipal finance, we have many examples we could describe in detail that would reflect our actual experience, and the importance to our municipal customers of the comprehensive banking services we provide to them. We would welcome the opportunity to talk with you.

Very truly yours,

ZIONS FIRST NATIONAL BANK

By _____
W. David Hemingway
Executive Vice President

cc: Lynnette Kelly, Executive Director, MSRB
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MSRB
Municipal Securities Rulemaking Board

Regulatory Notice

2014-12

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Stakeholders
Municipal Advisors, Issuers, General Public

Notice Type
Request for Comment

Comment Deadline
August 25, 2014

Category
Fair Practice

Affected Rules
Rule G-8; Rule G-9

Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Overview

The Municipal Securities Rulemaking Board (MSRB) is seeking comment on a revised draft MSRB Rule G-42 on standards of conduct and duties of municipal advisors when engaging in municipal advisory activities other than the undertaking of solicitations, and on associated revised draft amendments to MSRB Rules G-8, on books and records, and G-9, on the preservation of records (Revised Draft Rules). The MSRB previously sought comment on an initial draft Rule G-42 and initial draft amendments to Rules G-8 and G-9 (Initial Draft Rules). The Revised Draft Rules reflect the modifications made to the Initial Draft Rules after consideration of the comments received.

Comments should be submitted no later than August 25, 2014, and may be submitted in electronic or paper form. Comments may be submitted electronically by clicking here. Comments submitted in paper form should be sent to Ronald W. Smith, Corporate Secretary, Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314. All comments will be available for public inspection on the MSRB's website.[1]

Questions about this notice should be directed to Michael L. Post, Deputy General Counsel, at 703-797-6600.

[1] Comments are posted on the MSRB website without change. Personal identifying information such as name, address, telephone number, or email address will not be edited from submissions. Therefore, commenters should only submit information that they wish to make available publicly.

Initial Draft Rules

Following the financial crisis of 2008, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).[2] The Dodd-Frank Act establishes a federal regulatory regime requiring municipal advisors to register with the SEC, deeming them to owe a fiduciary duty to their municipal entity clients and granting the MSRB rulemaking authority over them. The MSRB, in the exercise of that authority, is currently developing a regulatory framework for municipal advisors.

On January 9, 2014, the MSRB requested comment on a cornerstone of that regulatory framework, the Initial Draft Rules.[3] Draft Rule G-42 (Duties of Non-Solicitor Municipal Advisors) (the Draft Rule or Initial Draft Rule) addressed the subjects of the core standards of conduct and duties of municipal advisors, other than when soliciting a municipal entity or obligated person.[4] The draft amendments to Rules G-8 and G-9 addressed the subject of the records required to be made and kept by municipal advisors, including provisions specifically related to municipal advisors' compliance with draft Rule G-42.[5] The sections below summarize the provisions of the Initial Draft Rules that are modified in the Revised Draft Rules. For more detail regarding the background of this rulemaking initiative and a complete description of the Initial Draft Rules, the Initial Request for Comment should be consulted.

Standards of Conduct

Draft Rule G-42(a) provided that each municipal advisor in the conduct of its municipal advisory activities for an obligated person client is subject to a duty of care. It also provided that each municipal advisor in the conduct of its municipal advisory activities on behalf of a municipal entity client is subject

[2] Pub. Law No. 111-203, 124 Stat. 1376 (2010) (Dodd-Frank Act).

[3] *See* MSRB Notice 2014-01, *Request for Comment of Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors* (Jan. 9, 2014) (Initial Request for Comment).

[4] As explained in the initial request for comment, Rule G-42 is not intended to address the duties of a municipal advisor when undertaking a solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Exchange Act and the rules and regulations thereunder. The MSRB plans a separate rulemaking with regard to solicitation activities, which may raise issues particular to those activities, at a later date. Municipal advisors engaged in such activities are subject to the MSRB's fundamental fair-practice rule, Rule G-17, which applies to all municipal advisors as well as to brokers, dealers and municipal securities dealers.

[5] Exchange Act Release No. 34-70462, (Sept. 20, 2013), 78 FR 67468 (Nov. 12, 2013) and Exchange Act Release No. 34-71288 (Jan. 13, 2014), 79 FR 2777 (Jan. 16, 2014) (SEC Final Rule).

to a fiduciary duty, which includes, without limitation, a duty of care and a duty of loyalty.

The Supplementary Material in Draft Rule G-42 provided guidance on the meaning of the duty of care and the duty of loyalty (paragraph .01 of the Supplementary Material, on the duty of care and paragraph .02 , on the duty of loyalty). Paragraph .06 of the Supplementary Material clarified that the duties created by the Draft Rule are in addition to any state-law or other duties, including fiduciary duties.

Disclosure of Conflicts of Interest and Other Information

Draft Rule G-42(b) provided that a municipal advisor must fully and fairly disclose to its client in writing all material conflicts of interest, and to do so at or prior to the inception of a municipal advisory relationship. These included any actual or potential conflict of interest that might impair the advisor's ability to render unbiased and competent advice to or on behalf of the client. Draft Rule G-42(b) included a non-exhaustive list of specific items requiring disclosure.

Paragraph .05 of the Supplementary Material of the Draft Rule provided that the conflicts disclosures must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict and must also include an explanation of how the advisor addresses or intends to manage or mitigate each conflict.

Paragraph .07 of the Supplementary Material required the municipal advisor to provide written disclosure to investors of any affiliation that meets the requirements of subsection (b)(ii) of the Draft Rule (paragraph (b)(i)(B) of the Revised Draft Rule), if a document prepared by the municipal advisor or the affiliate is included in an official statement for an issue of municipal securities. This requirement would be satisfied if the municipal advisor's affiliate were to provide written disclosure of the affiliation to investors.

Documentation of the Municipal Advisory Relationship

Draft Rule G-42(c) provided that municipal advisors must evidence each of their municipal advisory relationships by a writing entered into prior to, upon or promptly after the inception of the municipal advisory relationship. The documentation was required to include, at a minimum, certain key terms and disclosures and it was required to be amended as necessary.

Paragraph .04 of the Supplementary Material of the Draft Rule provided that a municipal advisor and its client may limit the scope of the municipal advisory relationship to certain specified activities or services. The municipal

advisor, however, was not permitted to alter the standards of conduct or duties imposed by the Draft Rule with respect to that limited scope.

Advisor Recommendations and Review of Recommendations of Other Parties

Draft Rule G-42(d) provided that a municipal advisor must not recommend that its client enter into any municipal securities transaction or municipal financial product unless the advisor has a reasonable basis for believing that the transaction or product is suitable for the client. The advisor was also required to discuss with its client its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product; the basis upon which the advisor reasonably believes the recommended transaction or product is suitable for the client; as well as whether the municipal advisor has investigated or considered other reasonably feasible alternatives. With respect to a municipal entity client, the Draft Rule provided that an advisor must only recommend a transaction or product that is in the client's best interests.

Paragraph .08 of the Supplementary Material of the Draft Rule provided guidance related to an advisor's suitability obligations. The Draft Rule provided that a municipal advisor's determination of whether a municipal securities transaction or municipal financial product is suitable for the client must be based on factors specified in the guidance.

Paragraph .09 of the Supplementary Material included a "Know Your Client" obligation, which required the advisor to use reasonable diligence to know and maintain essential facts concerning the client and in support of the advisor's fulfillment of its suitability obligations. The facts "essential" to "knowing your client" were specified.

Draft Rule G-42 (e) required a municipal advisor, if requested to do so and if the review of others' recommendations is within the scope of the engagement, to discuss with its client its evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product. The advisor was also required to discuss with the client whether the advisor reasonably believes that the recommended transaction or product is suitable for the client and the basis for such belief, as well as whether the municipal advisor has investigated or considered other reasonably feasible alternatives.

Principal Transactions
Draft Rule G-42 (f) prohibited a municipal advisor, and any affiliate of a municipal advisor, from engaging in any transaction in a principal capacity to which the municipal entity or obligated person client of the municipal advisor is a counterparty. To avoid a potential conflict with MSRB Rule G-23, an exception was allowed for activity that is expressly permitted by underwriters under Rule G-23.

Specified Prohibitions
Draft Rule G-42(g) specifically prohibited five types of activities by a municipal advisor. The topics addressed by the prohibitions included compensation, misleading representations related to expertise of the municipal advisor, fee-splitting and payments made to obtain or retain business.

Applicability to Municipal Fund Securities
The regulation of municipal advisors, as the SEC has recognized, [6] is relevant to municipal fund securities.[7] Paragraph .10 of the Supplementary Material of the Draft Rule highlighted the rule's application to municipal advisors whose municipal advisory clients are sponsors or trustees of municipal fund securities.

Books and Records
The Initial Draft Rules included provisions on record keeping to amend Rules G-8 and G-9 to address the books and records that must be made and preserved by municipal advisors registered or required to be registered with the SEC. The SEC Final Rule established a comprehensive record-keeping and preservation regime for municipal advisors.

Draft Rules G-8(h) and G-9 (h), (i), and (j) incorporated by reference all of the record-keeping provisions of the SEC Final Rule. The draft amendments, in addition, included requirements that correspond to certain specific requirements of Draft Rule G-42 that are not necessarily covered by the SEC Final Rule. This included keeping a copy of any document created by a

[6] SEC Final Rule at pages 20-21.

[7] The term "municipal fund security" refers to, among other things, interests in governmentally sponsored 529 college savings plans and local government investment pools and is defined in MSRB Rule D-12 to mean "a municipal security issued by an issuer that, but for the application of Section 2(b) of the Investment Company Act of 1940, would constitute an investment company within the meaning of Section 3 of the Investment Company Act of 1940."

municipal advisor that was material to its review of a recommendation made by another party. This also included the keeping of any document that memorializes the basis for any conclusions of the municipal advisor as to suitability. Finally, this included, unless it is included in the official statement for an issue of municipal securities, a copy of any disclosure provided by the municipal advisor, or any affiliate, to investors as required by paragraph .07 of the Supplementary Material.

The draft amendments to Rule G-9 required records to be preserved for not less than five years—the same period required by the SEC Final Rule.

Economic Analysis

The Initial Request for Comment incorporated the MSRB's preliminary economic analysis, as guided by MSRB's policy on economic analysis in rulemaking. The analysis addressed: the need for the draft rule and how the draft rule would meet that need; the relevant baselines against which the likely economic impact of the elements of the draft rule could be considered; reasonable alternative regulatory approaches; and the potential benefits and costs of the draft rule and the main alternative regulatory approaches. The initial request for comment specifically invited comment on the preliminary economic analysis, in addition to comment on all other aspects of the Initial Draft Rules.

Summary of Revised Draft Rule G-42 and Revised Draft Amendments to Rules G-8 and G-9

The MSRB received 44 comments on the Initial Draft Rules.[8] After careful consideration of the comments, the MSRB has determined to make significant modifications as reflected the Revised Draft Rules and request additional comment on the modifications. The significant modifications to the Initial Draft Rules are summarized below, with discussion of related matters raised by commenters.

Standards of Conduct

The Initial Draft Rule did not deem municipal advisors to owe a fiduciary duty to obligated persons, and specifically invited comment on whether the rule should do so and, if so, on any legal impediments to doing so. Commenters generally opposed the existence of a fiduciary duty on the part of municipal advisors to obligated persons under MSRB rules. After carefully considering the comments, Revised Draft Rule G-42(a), on standards of conduct, has not

[8] The comments received by the MSRB on the Initial Draft Rules are available here.

been modified in this regard and follows the Dodd-Frank Act in deeming a municipal advisor to owe a fiduciary duty, for purposes of the rule, only to its municipal entity clients.

Several commenters expressed the view that Draft Rule G-42 implicitly and inappropriately imposed fiduciary duty obligations on municipal advisors whose clients are obligated persons, without a demonstrated need for a more robust regulatory framework than that adopted by Congress or the SEC. The MSRB disagrees and has retained the duty of care as the standard of conduct that would apply to municipal advisors whose clients are obligated persons. Importantly, the MSRB has authority under the Exchange Act to, subject to SEC oversight, adopt rules (with respect to municipal advisory activities) designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

Many commenters expressed the view that Draft Rule G-42 is overly prescriptive. They suggested that the rule could benefit from a more principles-based approach that would articulate broad principles and standards that could be more readily applied to the multifaceted activities of a wide array of types of municipal advisory firms.

In response to the comments, Supplementary Material .01, which describes the duty of care, is revised to remove the requirement to undertake a thorough review of the official statement. Supplementary Material .02, which describes the duty of loyalty, is also revised to remove the requirement to investigate or consider other reasonably feasible alternatives to any recommended municipal securities transaction or financial product that might also or alternatively serve the municipal entity client's objectives. These changes have been made primarily based on the overarching principle that the client should be empowered to determine the scope of services and control the engagement with the municipal advisor. Supplementary Material .02 has also been revised to articulate the principle that the duty of loyalty precludes a municipal advisor from engaging in municipal advisory activities with a municipal entity client if it cannot manage or mitigate its conflicts in a manner that will permit it to act in the municipal entity's best interests.

Disclosure of Conflicts of Interest and Other Information

Draft Rule G-42(b) required disclosure of all material conflicts of interest, including any fee-splitting arrangements with any provider of investments or services to the client and conflicts that may arise from the use of the form of compensation under consideration or selected by the client. Draft Rule G-42(b) also required disclosure of the amount and scope of coverage of

professional liability insurance that the municipal advisor carries (*e.g.*, coverage for errors and omissions, improper judgments, or negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage. Draft Rule G-42(b) further required disclosure of any legal or disciplinary event that is (a) material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel; (b) disclosed by the municipal advisor on the most recent Form MA filed with the SEC; or (c) disclosed by the municipal advisor on the most recent Form MA-I filed with the SEC regarding any individual actually engaging in or reasonably expected to engage in municipal advisory activities in the course of the engagement. Finally, Draft Rule G-42(b) provided that, if a municipal advisor concludes that it has no material conflicts of interest, the advisor must provide written documentation to the client to that effect.

The MSRB received comment objecting to a specified requirement to disclose conflicts related to the form of compensation and stating that it might confuse the client and not serve any useful purpose.

In response to the comments, Revised Draft Rule G-42(b)(i)(F) has been modified to specifically require disclosure of material conflicts of interest arising from compensation for municipal advisory activities to be performed only where the compensation is contingent on the size or closing of a transaction as to which the municipal advisor is providing advice.

A commenter objected to the requirement to affirmatively state if the advisor has concluded that it has no material conflicts and stated that if an undisclosed conflict is only later discovered, it would be in violation of the requirement to disclose.

After consideration of the comments, Revised Draft Rule G-42(b) requires an advisor to affirmatively disclose in written documentation that it has "no known" material conflicts of interest based on the exercise of reasonable diligence by the advisor (if that is the case) rather than a more categorical statement.

Some commenters expressed concerns that professional liability insurance is costly, especially for smaller municipal advisors. They stated that the cost of professional liability insurance creates a significant barrier to entry, particularly for smaller firms seeking to enter the municipal advisory industry. One commenter stated that the requirement to disclose the amount and scope of professional liability insurance coverage does not relate to a conflict of interest, material or otherwise, and that, while disclosure may have an

impact on hiring decisions, it does not relate to a municipal advisor's qualifications and does not increase adherence to fiduciary duties. A few commenters described the complications associated with full and fair disclosure of the terms and limitations of policy coverage. In response to the comments, the requirement to disclose the amount and scope of coverage of professional liability insurance that the municipal advisor carries has been removed, though such information may be provided voluntarily or in response to requests from clients or prospective clients.

Some commenters objected to the draft provisions on the disclosure of legal and disciplinary history and suggested that there is ample and detailed disclosure provided about the advisory firm, compensation arrangements, proprietary interests in municipal advisor client transactions, affiliated business entities and disciplinary history of the advisory firm and its associated persons in Forms MA and MA-I that are required to be filed with the SEC.

In response to the comments, the Initial Draft Rule has been revised, and subsection (b)(ii) of the Revised Draft Rule expresses a principle that the municipal advisor must disclose any legal or disciplinary event that is material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel. Additionally, Revised Draft Rule G-42(c)(iii) requires the documentation of the advisory relationship to include a description of the type of information regarding legal events and disciplinary history requested by the SEC on Form MA and Form MA-I and information identifying where the client may electronically access the advisor's most recent Form MA and each most recent Form MA-I filed with the SEC. According to Revised Draft Rule G-42(c)(iv), the documentation must also include the date of the last material change to a legal or disciplinary event disclosure on any Form MA or Form MA-I filed with the SEC by the municipal advisor, which will alert the client to any material changes that have occurred to the information previously provided to the SEC and that may have been previously reviewed by the client.

Some commenters expressed the view that Draft Rule G-42 failed to address adequately issues associated with the provision of inadvertent or incidental advice which may cause a firm to be considered to be a municipal advisor under the SEC Final Rule. Commenters stated that, in other cases, if advice was provided to a company that was not identified as an obligated person, the party that provided the advice may unknowingly cause itself to be considered a municipal advisor. Similarly, commenters observed that a firm could render advice and trigger the application of certain provisions of the Initial Draft Rule absent a decision by the firm and the prospective client to

enter into a client relationship. This could implicate the application of requirements to disclose conflicts of interest and requirements for the documentation of the municipal advisory relationship.

In response to the comments and because disclosure and documentation requirements in certain circumstances would be impractical and unwarranted, a new provision is added, Supplementary Material .06. It addresses the steps that may be taken if the party inadvertently engaged in municipal advisory activities does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship and elects to seek a safe harbor from the requirements of sections (b) and (c) of Revised Draft Rule G-42 relating to disclosure of conflicts of interest and documentation of the municipal advisory relationship.

The Revised Draft Rule provides that the client must be promptly provided with a document that is dated and includes: a disclaimer that the advisor did not intend to provide advice and that, effective immediately, it has ceased engaging in municipal advisory activities; a notification that such municipal entity or obligated person should be aware that the disclosure of material conflicts of interest and other information as required by the rule has not been provided; a representation by the advisor that it, in good faith, has undertaken reasonable efforts to identify the advice that was inadvertently provided; and a request that the municipal entity or obligated person acknowledge receipt of the documentation. The advisor utilizing this alternative is also required to conduct a review of its supervisory and compliance policies and procedures for the purpose of ensuring that they are reasonably designed to prevent the provision of inadvertent advice to municipal entities and obligated persons.

Documentation of the Municipal Advisory Relationship

Under Draft Rule G-42(c), the documentation of the municipal advisory relationship was required to include provisions relating to compensation; the scope of municipal advisory activities to be performed and any limitations on the scope of the engagement; the specific undertakings, if any, requested by the client to be performed by the advisor relating to the preparation or finalization of the official statement or similar disclosure document; and the termination of the municipal advisory relationship. Draft Rule G-42(c) also required that the municipal advisor amend or supplement the writing during the term of the municipal advisory relationship as necessary to reflect changes in or additions to the terms or information required to be disclosed by section (b) or (c), except changes in the reasonably expected amount of compensation were only required to be updated if the change was material. The amendment and supplementation requirement in Draft Rule G-42(c)

applied to any changes and additions that were discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor.

A commenter suggested that the materiality standard should apply for all updates related to disclosures required in the documentation of the municipal advisory relationship, not just those relating to compensation. Another commenter supported acknowledgment of conflicts of interest disclosure and yet another commenter supported the concept of informed consent, confirmed in writing, and said that the acknowledgment does not need to be a separate, stand-alone document; it could be in the form of a writing evidencing the engagement, so long as it was after the disclosure of conflicts of interest. One commenter stated that a municipal advisor should be permitted to proceed with a municipal advisory engagement in the absence of receipt of a written acknowledgment of the conflicts disclosure and consent, if the municipal advisor has a reasonable belief that such information has been received.

One commenter stated that, as with other fiduciary standards, the rule should provide for the withdrawal from, and termination of, municipal advisory relationships. The commenter also stated that the rule should ensure that any withdrawal or termination of the advisory relationship complies with fiduciary standards. The commenter suggested that the rule, or guidance, should state that, when a municipal advisory relationship is no longer in existence, the advisor no longer owes duties to its former client. Another commenter stated that the rule should provide when and how municipal advisors withdraw or terminate the advisory relationship.

In response to the comments, the Revised Draft Rule simplifies the documentation of compensation and requires that the documentation include only the form and basis of any direct and indirect compensation. Though no longer required by the Revised Draft Rule, the parties may agree to document the reasonably expected amount of compensation and may agree to state such amount in dollars to the extent it can be quantified. Also removed from the Revised Draft Rule is the requirement to detail, in the case of municipal advisory activities relating to a new issue or reoffering of municipal securities, the specific undertakings, if any, requested by the client to be performed by the advisor relating to the preparation or finalization of the official statement or similar disclosure document. Additionally, the Revised Draft Rule provides that the documentation of the advisory relationship is required to include any terms relating to withdrawal from the relationship and must be amended and supplemented only if there are material changes or additions.

Recommendations and the Review of Recommendations of Others

The Initial Draft Rule provided that an advisor must not recommend that its client enter into any transaction or financial product unless the advisor had a reasonable basis for believing the transaction or financial product was suitable for the client. One commenter suggested that because a municipal advisory relationship could, just like the attorney-client relationship, include a wide spectrum of activities, the terms of the engagement should govern the tasks that a municipal advisor must perform in providing its advice. This commenter believed that a municipal advisor should be free to recommend a transaction based on facts given to it by its client, without exercising any diligence to check the facts, if consistent with the engagement, and that a municipal advisor also should be free to provide advice regarding, or otherwise recommend, a pricing of a transaction even if it does not believe that the transaction is preferable to other possible transactions. In addition, this commenter stated that a municipal advisor should be permitted to recommend a range of transactions that would be in the client's interests, even though only one could be in the client's best interests.

The Initial Draft Rule required a municipal advisor, when requested to do so by its client and within the scope of the engagement, to undertake a thorough review of another party's recommendation. The Initial Draft Rule further required that certain matters be "discussed" with the client in the course of the review. One commenter stated that this would require excessive recordkeeping associated with defensive documentation in order to show compliance with the provisions of the Initial Draft Rule.

After carefully considering the comments, the provisions of the Revised Draft Rule relating to recommendations made by the advisor and the advisor's review of recommendations of other parties are merged. The merged provisions retain the diligence standard in connection with each kind of undertaking. The merged provisions, however, clarify that the client (with the agreement of the municipal advisor) will control the scope of the engagement. Revised Draft Rule G-42(d) provides that, if a municipal advisor makes a recommendation of a municipal securities transaction or municipal financial product, or if the review of a recommendation of another party is requested by the municipal entity or obligated person client and within the scope of the engagement, the municipal advisor must determine, based on the information obtained through reasonable diligence, whether a recommended transaction or financial product is suitable for the client. Revised Draft Rule G-44(d) allows the advisor to inform the client of certain matters rather than retaining the provisions of the Initial Draft Rule that required the topics to be "discussed." A municipal advisor is allowed to

choose the appropriate method by which to communicate its evaluation of the material risks and benefits attendant to the recommendation.

Principal Transactions

Draft Rule G-42(f) prohibited a municipal advisor, and any affiliate of a municipal advisor, from engaging in any transaction in a principal capacity to which the municipal entity or obligated person client of the municipal advisor is a counterparty. In the initial request for comment, the MSRB specifically sought comments on whether a prohibition of principal transactions by municipal advisors was the appropriate regulatory approach. The initial request asked, for example, whether an advisor (or its affiliate) should be permitted to engage in certain types of principal transactions with its client, with full and fair disclosure and written client consent. And the initial request asked, if so, what types of principal transactions should be allowed. The initial request also asked whether the treatment of principal transactions should differ based upon whether or not a municipal advisor owes a fiduciary duty to the client.

In response to the Initial Request for Comment, many commenters expressed concerns with respect to the proposed prohibition of principal transactions by municipal advisors with their clients. Several commenters interpreted the prohibition as covering activities and transactions that are unrelated to the municipal advisory relationship. Other commenters viewed the application of the prohibition to transactions with obligated persons as overreaching because it, according to the commenters, inappropriately treats them as benefitting from a fiduciary duty. Many commenters stated that other fiduciary regimes do not completely prohibit principal transactions, and the ban should be significantly narrowed and should not apply in any event to affiliates. One commenter objected to the ban extending to affiliates regardless of the extent of the connection of the principal transaction between the non-municipal advisor and the municipal advisory relationship. The commenter stated that the risk of conflicts of interest is significantly diminished because affiliates provide different services or have different governance structures and information barriers. Other commenters expressed concerns related to regulating conduct of affiliates of municipal advisors, specifically the imposition of compliance burdens on the affiliates and possible unintended consequences to clients if certain products and services offered by affiliates of the municipal advisor were no longer available to clients. Finally, many commenters sought clarification of the definition of principal transaction or “principal capacity.”

After carefully considering the comments, the MSRB has, in the Revised Draft Rule, clarified and significantly narrowed the scope of the proposed

prohibition of principal transactions. Revised Draft Rule G-42(e)(ii)[9] prohibits a municipal advisor (and its affiliate) to a municipal entity client from "engaging in a principal transaction" directly related to the same municipal transaction or financial product as to which the municipal advisor is providing advice. It provides that a municipal advisor to a municipal entity client is prohibited from certain principal transactions, but there is no specific prohibition or disclosure-and-consent requirement in the Revised Draft Rule for a municipal advisor to an obligated person client. Importantly, municipal advisors are subject to the MSRB's fundamental fair-practice rule, Rule G-17, which applies to the conduct of all of their municipal advisory activities. The exception in the Revised Draft Rule to the prohibition on principal transactions that is included to avoid a possible conflict with Rule G-23 is located in Supplementary Material .07, and is clarified through the use of terminology from Rule G-23 rather than solely through a cross-reference.

Also in response to comments, Revised Draft Rule G-42(f)((i) adds, for purposes of the Revised Draft Rule, a definition of the term "engaging in a principal transaction" – "when acting as a principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client." This definition draws on the statutory language that addresses principal transactions in the Investment Advisers Act.[10] These modifications are designed to exclude many of the transactions that some commenters read as potentially covered by the Initial Draft Rule, including the taking of a cash deposit or the payment by a client solely for professional services.

Specified Prohibitions

Draft Rule G-42(g) included provisions that specifically prohibited an advisor from receiving excessive compensation and making or participating in any fee-splitting arrangements with underwriters.

One commenter was not opposed to the prohibition on fee-splitting but requested a clear definition of "fee-splitting arrangements" that would recognize that a municipal advisor's utilization of independent contractors and subcontractors in connection with particular engagements would fall outside of any such definition. One commenter stated that allowing an investment provider to pay fees related to the solicitation of the investment by the municipal advisor, and that are within the permitted limits of the

[9] The prohibition of certain principal transactions is provided in Revised Draft Rule G-42(e)(ii) as one of the "specified prohibitions."

[10] Section 206(3) of the Investment Advisers Act, 15 U.S.C. 80b-6(3).

Internal Revenue Service rules, should be acceptable so long as they are disclosed to the issuer and each investment provider on the bid list. Two commenters stated that fee-splitting should be disclosed but not prohibited and provided one example of fee-splitting with a structuring agent to provide specific quantitative services on a transaction and another example of a situation where a municipal entity or obligated person may want its municipal advisor or other professionals (including underwriters, if after the underwriting period) to receive compensation from investment providers or other service providers for providing oversight and performing other services. The commenter stated that in the case of the latter example, this should not be prohibited if there is written full and fair disclosure of any fee-splitting or fee-sharing arrangements.

One commenter recommended that the MSRB clarify that the prohibition on fee-splitting with underwriters applied "on any issue for which it is serving as municipal advisor" because the failure to link the prohibition to the actual advisory engagement many lead to unintended consequences. The MSRB agrees with this commenter and, in response, the Revised Draft Rule clarifies that the prohibition applies to fee-splitting with underwriters on any municipal securities transaction for which it is acting as municipal advisor.

One commenter questioned the standard that would be used to evaluate whether compensation was excessive. Another commenter stated that in some circumstances certain transaction fees are meant to compensate the advisor for other activities unrelated to the specific issuance or reoffering of municipal securities in connection with which the fee is being paid and asked whether this practice was permitted.

In response to the comments, Revised Draft Rule G-42 includes paragraph .11 of the Supplementary Material to provide guidance on factors that may be relevant to whether a municipal advisor's compensation is excessive, including: the municipal advisor's expertise, the complexity of the municipal securities transaction or the financial product, whether the fee is contingent upon the closing of the transaction or financial product, the length of time spent on the engagement and whether the advisor is paying any other relevant costs related to the transaction or financial product. Regarding the other commenter's question, the Revised Draft Rule, like the Initial Draft Rule, prohibits receiving compensation that is excessive in relation to the municipal advisory activities actually performed and also prohibits invoices that do not accurately reflect the services actually performed. Depending on the facts and circumstances, either or both of these provisions could apply to a scenario like that posited by the commenter. The Revised Draft Rule,

however, does not speak to the client's decision regarding the source of funds for the payment of fees for services rendered by the municipal advisor.

Another commenter stated that the specific prohibition against inaccurate invoices (subsection (g)(ii) of the Initial Draft Rule) should be modified to apply only to inaccuracies resulting in an *overstatement* of fees, expenses, etc., to allow an advisor to *understate* or forgo part of an amount (in the advisor's discretion). Revised Draft Rule G-42(e)(i)(B) is unchanged from the Initial Draft Rule, and prohibits delivering an invoice for fees or expenses for municipal advisory activities that does not accurately reflect the activities actually performed or personnel that actually performed those services--it does not prohibit an advisor from offering a payment discount for services actually performed. The MSRB believes an advisor would be free to accurately disclose on its invoice the amount of any discount.

Definitions

Many commenters stated that the Initial Draft Rule should be harmonized with the SEC Final Rule and should state clearly that it does not apply to activities that have been excluded or exempted under either the Dodd-Frank Act or the SEC Final Rule. The references in the Initial Draft Rule to the Exchange Act and the rules and regulations thereunder encompassed the statutory exclusions and the rule-based exemptions. Nevertheless, each of the definitions of "advice," "municipal advisor," "municipal entity" and "obligated person" has been modified in Revised Draft Rule G-42(f)(ii), (iv), (vii) and (viii) and now specifically reference the applicable provisions of the SEC Final Rule to address commenters' concerns.

Finally, Revised Draft Rule G-42(f)(vi) includes language that clarifies when the municipal advisory relationship begins and ends. This clarification is important given, among other reasons, that an advisor is required to evidence each of its municipal advisory relationships in a writing that must be promptly amended to reflect any material changes or additions.

Application to Other Types of Municipal Securities

Some commenters stated that the Initial Draft Rule may be unworkable when applied to advisors advising municipal entities regarding municipal fund securities (such as local government investment pools or 529 college savings plans), advisors to certain state and local funds (such as state and local retirement funds or any state and local fund investing bond proceeds) or

advisors to other investment funds (such as real estate funds) that may from time-to-time comingle bond proceeds with funds from other investors.[11]

One commenter stated that a fund manager or adviser that provides offering materials to investors in its fund and obtains executed subscription agreements or other organizational agreements should not be required to provide separate "writings" to fund investors who are municipal entities or obligated persons. The MSRB, at this juncture, does not intend to create an exemption for these types of advisors and believes that it is appropriate to require them to either create a separate writing or adapt the subscription agreement language or other written materials to conform to the requirements of Revised Draft Rule G-42.

One commenter recommended that the MSRB provide that a municipal advisor is not required to investigate whether information is materially inaccurate or complete if it was provided by persons who are authorized by a municipal entity client to act on behalf of a state's 529 college savings plan. Another commenter stated that in the context of 529 plans, municipal advisors receiving information from the trustees and sponsors of such plans would not be in a position to verify the accuracy or completeness of information provided by authorized state employees and officials.

Paragraph .01 of the Supplementary Material of the Revised Draft Rule provides, as a core general standard, that a municipal advisor must make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client and it also provides that an advisor must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. The Revised Draft Rule does not provide an exception for information that is provided to the advisor by the client. In addition, the MSRB believes that in some circumstances the information may be provided to the advisor by the client in connection with the preparation of the official statement. Paragraph .01 of the Supplementary Material of the Revised Draft Rule provides that a municipal advisor must have a reasonable basis for any information provided by the advisor to the client or other parties involved in the municipal securities transaction in connection with the preparation of an official

[11] To help address various general concerns about the scope of municipal advisory activities, the SEC has provided transitional guidance for identifying proceeds of municipal securities for market participants who prior to July 1, 2014 have deposited proceeds of municipal securities in existing accounts and invested such proceeds in existing investments held by certain market participants. *See* SEC FAQ 11.1 (updated May 19, 2014).

statement. The MSRB believes at this juncture that the provisions of the Revised Draft Rule are appropriate and does not believe that advisors to 529 plans should be relieved from an obligation to inquire as to material provided by it to its client or other parties in connection with the preparation of an official statement.

Two commenters stated that Supplementary Material .07 required, among other things, the provision of written disclosure to investors of certain affiliations and that a municipal advisor generally will not have access to information about the 529 plan's investors or how to contact them and would therefore be unable to provide the required disclosure. One of the commenters stated the advisor may have no control over the content of the official statement used by the plan or its underwriter, so it would be unable to require the plan or its underwriter to include the required disclosure in such document. Notably, this requirement, according to the last sentence of Supplementary Material .08, would be satisfied if the advisor's affiliate were to provide written disclosure of the affiliation to investors. The purpose of these disclosures would be to alert investors to the affiliation.

One commenter stated that many of the disclosures included in Draft Rule G-42(b) could be inapplicable in the context of an advisory relationship with a 529 plan. The MSRB believes that application of section (b) is warranted because advisors to 529 plans may have material conflicts of interest including those that may arise in connection with affiliates of an advisor that may be registered investment companies that are included in one or more of the investment options in the 529 plan to or on behalf of which the advisor is providing advice.

Books and Records

The Initial Draft Rules included provisions on record keeping to amend Rules G-8 and G-9 to address the books and records that must be made and preserved by municipal advisors registered or required to be registered with the SEC.[12] One commenter expressed concerns that, in order to maintain proper books and records of any evaluations and recommendations made by a municipal advisor, a number of discussions that typically occur verbally

[12] The Initial Draft Rules included fundamental books and records provisions intended to become effective with the first major municipal advisor rule since the SEC's adoption on September 18, 2013, of the SEC Final Rule. Because the MSRB is requesting additional comment and then will be reviewing the comments received on the Revised Draft Rules, these provisions are removed and the MSRB plans to include them in a separate rulemaking initiative. These provisions of the Initial Draft Rules would have added Rule G-8(h)(i) and Rule G-9(i), (j) and (k), and amended Rule G-9(e) and (f).

between an issuer and its advisor would need to be memorialized in writing, which may be of concern to issuers and impractical for advisors. The commenter stated that, if these discussions and alternatives are memorialized, this may affect the decision-making process and how much information an issuer may be willing to disclose to its advisor. The commenter stated that the MSRB should describe in more detail exactly what records a municipal advisor will need to retain and asked if a municipal advisor needs to know whether it should retain records or copies of all the proposals it receives, only those it receives and reviews at the specific request of the issuer, or only those it receives, reviews and recommends to the issuer.

Draft Rule G-8(h)(ii)(A) did not require a municipal advisor to make and keep a copy of any document unless the municipal advisor already has created the document. It required a municipal advisor to make and keep current a "copy of any document created by the municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any conclusions as to suitability." In addition, the Draft Rule did not require that a record be created of an advisor's evaluations or recommendations.[13] The Initial Draft Rules left the determinations regarding record creation in this respect to the municipal advisor in its professional and business judgment, and then required the preservation of copies of documents that the municipal advisor determined to create.

One commenter requested that the MSRB provide a draft of a prototype baseline policies and procedures guide that smaller municipal advisor firms can adopt or modify, as needed, to assist firms with this type of endeavor. The MSRB has declined at this time to do so in part because it may be impracticable for the MSRB to develop policies and procedures that would appropriately address the scope and diversity of business models and particular practices of the numerous municipal advisor firms.

One commenter requested that the MSRB clarify that maintenance of documents and emails on a firm's email site or through its internet service provider will comply with the record retention requirements. The draft amendments to Rule G-9 contain relatively principles-based requirements for retention, including that records be available for ready retrieval, inspection and production of copies. The draft amendments to Rule G-9 do not

[13] SEC Rule 15Ba1-8 requires an advisor to keep records of all written communications received and sent by such advisor relating to municipal advisory activities and a copy of any document created by the advisor that was material to making a recommendation to a municipal entity or obligated person or that memorializes the basis for that recommendation.

prescribe the specific details of how or where electronic records must be preserved. Additionally, if a municipal advisor would prefer to comply with the SEC's electronic record retention requirements (SEC Rule 15Ba1-8(d)), as interpreted by the SEC, the draft amendments to Rule G-9 provide that alternative.

Economic Considerations

As noted above, the initial request for comment incorporated the MSRB's preliminary economic analysis, as guided by MSRB's policy on economic analysis in rulemaking. This analysis examined likely benefits and costs of the Draft Rule, relative to appropriate baselines and reasonable alternatives. As summarized below, much of that preliminary analysis applies to the Revised Draft Rules, and the MSRB believes that, overall, the significant modifications made likely will reduce costs as compared with the Initial Draft Rules.

Benefits.

The MSRB believes that the Revised Draft Rule will provide several likely benefits by enhancing protections to municipal bond issuers and investors and by providing guidance to municipal advisors for complying with the requirements of the Dodd-Frank Act.

First, The MSRB believes the Revised Draft Rule will enhance municipal entity and obligated person protections by ensuring that these entities have available to them sufficient information to make meaningful choices about engaging a municipal advisor. These protections would also be enhanced as a result of the Revised Draft Rule's guidance for municipal advisors that may assist these advisors in complying with, or help prevent breeches of, their fiduciary and fair dealing duties. To the extent that this guidance increases the likelihood of compliance by municipal advisors, municipal entities and obligated persons will benefit. Investors in municipal bond offerings should also benefit from the Revised Draft Rule to the extent that a municipal entity issuing bonds that uses a municipal advisor is more likely to receive services that reflect a higher ethical and professional standard than otherwise would be the case.

Second, the Revised Draft Rule provides needed guidance and clarification with respect to the standards of conduct and duties of a municipal advisor that would meet the purposes of the Dodd-Frank Act and the SEC Final Rule. The Revised Draft Rule also prescribes for municipal advisors means that will prevent breaches of these duties. Therefore, this guidance provides a benefit to municipal advisors who could otherwise face greater uncertainty about the standards of conduct and duties required to meet certain of the requirements

of the Dodd-Frank Act, particularly given the regulatory framework for municipal securities regulation involving multiple enforcement organizations.

Third, the MSRB believes that a benefit of the Revised Draft Rule may follow from the increased level of information disclosed to clients by municipal advisors relative to the baseline, which may lead to an improvement in the selection of municipal advisors. As a result of the information disclosed through the Revised Draft Rule, municipal entities and obligated persons may be able to more easily establish objective criteria to use in selecting municipal advisors and may increase the likelihood that municipal advisors are hired because of their qualifications as opposed to other reasons.

Fourth, the Revised Draft Rule should also result in improved quality-based competition among municipal advisors to the extent that the clients of municipal advisors rely on this disclosed information in the municipal advisor selection process.

Costs.
The Board recognizes that municipal advisors would incur costs, relative to the baseline state, to meet the standards of conduct and duties contained in Revised Draft Rule and the revised amendments to Rules G-8 and G-9. These costs may include additional compliance costs and additional record-keeping costs.

First, to ensure compliance with disclosure obligations of the Revised Draft Rule, municipal advisors may incur costs by seeking advice from legal and compliance professionals when preparing disclosures to clients. However, the Board believes that some of these costs are accounted for in the baseline requirements of the SEC final municipal advisor rules which require disclosure of at least some similar information, such as the disclosure of disciplinary history. Revised Draft Rule G-42 may impose additional costs on municipal advisors as it requires disclosure of additional information and requires that information be disclosed directly to clients rather than through submissions to a regulator. The magnitude of these additional costs, however, is not quantifiable using available data.

Second, municipal advisors may incur additional record-keeping costs as a result of the Revised Draft Rule. The Board considers existing requirements in the SEC's municipal advisor rules on record keeping and record preservation to serve as a baseline. As the SEC recognized in its economic analysis of its recordkeeping requirements, municipal advisors should already be maintaining books and records as part of their day-to-day operations. In addition, municipal advisors who are also registered as broker-dealers or

investment advisors are currently subject to the record-keeping requirements of those regulatory frameworks. Against these baselines, the Board believes that the costs associated with the few additional record-keeping requirements associated with Revised Draft Rule G-42 will not be significant.

The Initial Request for Comment specifically invited comment on the preliminary economic analysis. Commenters cited four features of the rule they believed were potentially costly and burdensome and therefore deserving of careful consideration by the MSRB.

First, many commenters expressed concerns about the potential breadth of the draft prohibition of principal transactions by municipal advisors with their clients. As noted, the MSRB has clarified and significantly narrowed the scope of this prohibition in the Revised Draft Rule.

Second, commenters expressed concerns about the cost for a firm to document whether any of its affiliates has a business relationship with any of the municipal advisor affiliate's clients. These costs arise from developing and implementing systems to enable tracking of affiliate relationships with municipal advisor clients. Commenters asserted that these costs were incurred without any tangible benefit to municipal entity or obligated person clients.

Third, commenters cited professional liability insurance as costly, especially for smaller municipal advisors. Commenters asserted that the cost of professional liability insurance created a significant barrier to entry, particularly for smaller firms seeking to enter the municipal advisory arena. As noted, the MSRB has deleted the specific disclosure requirement related to professional liability insurance from the Revised Draft Rule.

Fourth, commenters believed that a portion of the costs associated with the Initial Draft Rule would be passed along to municipal entity and obligated person clients in the form of higher fees. The MSRB believes that any increase in municipal advisory fees attributable to the additional costs of the Revised Draft Rule compared with the baseline state will be, in the aggregate, low and that the cost per municipal advisory firm will be spread across the number of advisory engagements for each firm. The MSRB recognizes, however, that for smaller municipal advisors with fewer clients, the cost of compliance with the Revised Draft Rule's standards of conduct and duties may represent a greater percentage of annual revenues, and thus, such advisors may be more likely to pass those costs along to their advisory clients

The MSRB recognizes that, as a result of these costs, some municipal advisors may decide to exit the market, curtail their activities, consolidate with other firms, or pass the costs on to municipal entities and obligated persons in the form of higher fees. While the Board recognizes that some municipal advisors may exit the market as a result of the costs associated with the Revised Draft Rule relative to the baseline, the Board believes municipal advisors may exit the market for a number of reasons, including business reasons separate from reasons involving the costs associated with the Revised Draft Rule. The Board believes that municipal advisors that have been subject to past disciplinary actions may decide to exit the market rather than disclose that information directly to clients, which could improve the quality of the market for municipal advisory services and, therefore, benefit municipal entities and obligated persons. The Board recognizes that some of the municipal advisors that may exit the market could be small entity municipal advisors that exit the market for financial reasons and that such exits from the market may lead to a reduced pool of municipal advisors.

The MSRB has also considered the possibility that some compliance costs could be greater in the absence of the Revised Draft Rule. By articulating the duties and obligations of municipal advisors and by prescribing means that will prevent breaches of these duties, the Revised Draft Rule may reduce possible confusion and uncertainty about what is required in order to comply with relevant provisions of the Dodd-Frank Act. Therefore, the Revised Draft Rule may reduce certain costs of compliance that might have otherwise been incurred by allowing municipal advisors to more quickly and accurately determine compliance requirements.

Request for Comment

The MSRB requests comments on Revised Draft Rule G-42 and the revised draft amendments to Rules G-8 and G-9. In addition to any other subject that commenters wish to address related to the Revised Draft Rules, the MSRB particularly welcomes any statistical, empirical and other data from commenters that may support their views and/or support or refute the views or assumptions contained in this request for comment.

July 23, 2014

* * * * *

Text of Proposed Amendments[14]

Rule G-42: Duties of Non-Solicitor Municipal Advisors

(a) *Standards of Conduct.*

(i) A municipal advisor to an obligated person client shall, in the conduct of all municipal advisory activities for that client, be subject to a duty of care.

(ii) A municipal advisor to a municipal entity client shall, in the conduct of all municipal advisory activities for that client, be subject to a fiduciary duty that includes a duty of loyalty and a duty of care.

(b) *Disclosure of Conflicts of Interest and Other Information*. A municipal advisor must, ~~at~~upon or prior to ~~the inception of a~~engaging in municipal advisory ~~relationship~~activities, provide ~~the~~to the municipal entity or obligated person client ~~with a document making~~ full and fair disclosure in writing of:

(i) all material conflicts of interest, including ~~disclosure of~~:

~~(i)~~(A) any actual or potential conflicts of interest of which it is aware after reasonable inquiry that might impair its ability either to render unbiased and competent advice to or on behalf of the obligated person client or to fulfill its fiduciary duty to the municipal entity client, as applicable;

~~(ii)~~(B) any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor;

~~(iii)~~(C) any payments made by the municipal advisor, directly or indirectly, to obtain or retain the client's municipal advisory business;

~~(iv)~~(D) any payments received by the municipal advisor from third parties to enlist the municipal advisor's recommendation to the client of its services, any municipal securities transaction or any municipal financial product;

~~(v)~~(E) any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client;

[14] The proposed amendments to Draft Rule G-42 as indicated here include markings to show changes from the text of the proposed amendments that were contained in the Initial Request for Comment, MSRB Notice 2014-01. The proposed amendments to Draft Rules G-8 and G-9 are indicated here through comparison with the existing text of the MSRB Rule Book. Underlining indicates new language; strikethrough denotes deletions.

~~(vi)~~(F) any conflicts of interest ~~that may arise~~arising from ~~the use of the form of~~ compensation ~~under consideration or selected by the client for the~~for municipal advisory activities to be performed~~;~~ that is contingent on the size or closing of any transaction as to which the municipal advisor is providing advice; and

~~(vii)~~(G) any other engagements or relationships ~~of the municipal advisor or any affiliate~~ of the municipal advisor that might impair the advisor's ability either to render unbiased and competent advice to or on behalf of the obligated person client or to fulfill its fiduciary duty to the municipal entity client, as applicable~~;~~.

~~(viii) the amount and scope of coverage of professional liability insurance that the municipal advisor carries (*e.g.*, coverage for errors and omissions, improper judgments, or negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage; and~~

If a municipal advisor concludes that it has no known material conflicts of interest based on the exercise of reasonable diligence by the advisor, the municipal advisor must provide written documentation to the client to that effect.

~~(ix)~~(ii) any legal or disciplinary event that is ~~(a)~~ material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel~~; (b) disclosed by the municipal advisor on the most recent Form MA filed with the Commission; or (c) disclosed by the municipal advisor on the most recent Form MA-I filed with the Commission regarding any individual actually engaging in or reasonably expected to engage in municipal advisory activities in the course of the engagement. If a municipal advisor has disclosed a legal or disciplinary event on any form referenced in section (b) or (c) of this rule, the advisor must provide the client with a copy of the relevant sections of the form or forms~~.

~~If a municipal advisor concludes that it has no material conflicts of interest, the municipal advisor must provide written documentation to the client to that effect.~~

(c) *Documentation of Municipal Advisory Relationship*. A municipal advisor must evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the ~~inception~~establishment of the municipal advisory relationship. The writing must be dated and include, at a minimum,

(i) the form and basis of direct or indirect compensation, if any, for the municipal advisory activities to be performed;

(ii) ~~the reasonably expected amount of any such compensation (stated in dollars to the extent it can be quantified);~~

~~(iii)~~ the information ~~regarding conflicts of interest and other matters that is~~ required to be disclosed by section (b) of this rule;

(iii) a description of the type of information regarding legal events and disciplinary history requested by the Commission on Form MA and Form MA-I, which includes information about any criminal actions, regulatory actions, investigations, terminations, judgments, liens, civil judicial actions, customer complaints, arbitrations and civil litigation, and information identifying where the client may electronically access the municipal advisor's most recent Form MA and each most recent Form MA-I filed with the Commission;

(iv) the date of the last material change to a legal or disciplinary event disclosure on any Form MA or Form MA-I filed with the Commission by the municipal advisor;

~~(iv)~~(v) the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement;

~~(v) in the case of municipal advisory activities relating to a new issue or reoffering of municipal securities, the specific undertakings, if any, requested by the client to be performed by the municipal advisor with respect to the preparation and finalization of an official statement or similar disclosure document; and~~

(vi) the date, triggering event, or means for the termination of the municipal advisory relationship, or, if none, a statement that there is none~~.~~; and

(vii) any terms relating to withdrawal from the municipal advisory relationship.

During the term of the municipal advisory relationship, the writing must be promptly amended or supplemented to reflect any material changes ~~in~~ or additions ~~to the terms or information required by section (b) or this section (c)~~, and the revised writing must be promptly delivered to the client~~, provided that this requirement applies with respect to subsection(c)(ii) of this rule only if the change in the amount of reasonably expected compensation is material~~. This amendment and supplementation requirement applies to any changes and additions that are discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor.

(d) *Recommendations and Review of Recommendations of Other Parties*. ~~A~~ If a municipal advisor ~~must not recommend that its municipal entity or obligated person client enter into any~~makes a recommendation of a municipal securities transaction or municipal financial product ~~unless~~, or if the ~~advisor has a reasonable basis for believing~~review of a recommendation of another party is requested by the municipal entity or obligated person client and within the scope of the engagement, the municipal advisor must determine, based on the information obtained through the reasonable diligence of ~~the~~such advisor, ~~that the~~whether a municipal securities transaction or municipal financial product is suitable for the client. ~~-~~In addition, the municipal advisor must ~~discuss with its~~inform the client of:

(i) the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product;

(ii) the basis upon which the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is, or is not, suitable for the client; and

(iii) whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives.

~~With respect to a client that is a municipal entity, a municipal advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest.~~

~~(e) *Review of Recommendations of Other Parties.* When requested to do so by its municipal entity or obligated person client and within the scope of its engagement, a municipal advisor must undertake a thorough review of any recommendation made by any third party regarding a municipal securities transaction or municipal financial product. In addition, the municipal advisor must discuss with its client:~~

~~(i) the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product;~~

~~(ii) whether the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is suitable for the client, and the basis for such belief; and~~

~~(iii) whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives.~~

~~(f) *Principal Transactions.* Except for an activity that is expressly permitted under Rule G-23, a municipal advisor, and any affiliate of a municipal advisor, is prohibited from engaging in any transaction, in a principal capacity, to which a municipal entity or obligated person client of the municipal advisor is a counterparty.~~

~~(g)~~(e) *Specified Prohibitions.*

(i) A municipal advisor is prohibited from:

~~(i)~~(A) receiving compensation that is excessive in relation to the municipal advisory activities actually performed;

~~(ii)~~(B) delivering an invoice for fees or expenses for municipal advisory activities that do not accurately reflect the activities actually performed or the personnel that actually performed those services;

~~(iii)~~(C) making any representation or the submission of any information about the capacity, resources or knowledge of the municipal advisor, in response to requests for proposals or

qualifications or in oral presentations to a client or prospective client, for the purpose of obtaining or retaining municipal advisory business that the advisor knows or should know is materially false or misleading;

~~(iv)~~(D) making, or participating in, any fee-splitting arrangements with underwriters on any municipal securities transaction for which it is acting as municipal advisor, and any undisclosed fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client of the municipal advisor; and

~~(v)~~(E) making payments for the purpose of obtaining or retaining municipal advisory business other than reasonable fees paid to another municipal advisor registered as such with the Commission and the Board for a solicitation of a municipal entity or obligated person as described in Section 15B(e)(9) of the Act.

(ii) A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice.

~~(h)~~(f) *Definitions*.

(i) "Engaging in a principal transaction" shall mean, for purposes of this rule, when acting as principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client.

(ii) "Advice" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(4)(A)(i) of the Act, 17 CFR 240.15Ba1-1(d)(1)(ii) and ~~the~~other rules and regulations thereunder.

~~(ii)~~(iii) "Affiliate of the municipal advisor" shall mean, for purposes of this rule, any person directly or indirectly controlling, controlled by, or under common control with such municipal advisor.

~~(iii)~~(iv) "Municipal advisor" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(4) of the Act ~~and the~~, 17 CFR 240.15Ba1-1(d)(1)-(4) and other rules and regulations thereunder; provided that it shall exclude a person that is otherwise a municipal advisor solely with respect to either activities within the meaning of Section 15B(e)(4)(A)(ii) or any solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Act.

~~(iv)~~(v) "Municipal advisory activities" shall, for purposes of this rule, ~~have the same meaning as the~~mean those activities ~~specified in Section 15B(e)(4)(A) of the Act and the rules and regulations thereunder, provided~~ that ~~they shall exclude the activities within the meaning of Section 15B(e)(4)(A)(ii) of the Act and the rules and regulations thereunder and any solicitation of~~would cause a person to be a municipal ~~entity or obligated person within the meaning of Section 15B(e)(9) of the Act and the rules and regulations thereunder~~advisor as defined in section (f)(iv) hereof.

~~(v)~~(vi) A "municipal advisory relationship" shall, for purposes of this rule, be deemed to exist when a municipal advisor ~~engages in or~~ enters into an agreement to engage in municipal advisory activities for or on behalf of a municipal entity or obligated person ~~client~~. The municipal advisory relationship shall be deemed to have ended on the date which is the earlier of (i) the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship required in section (c) hereof or (ii) the date on which the municipal advisor withdraws from the municipal advisory relationship.

~~(vi) "Municipal advisory business" shall mean, for purposes of this rule, the provision of advice to or on behalf of a municipal entity or an obligated person with respect to the issuance of municipal securities or municipal financial products by a municipal advisor whether for compensation or otherwise.~~

(vii) "Municipal entity" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(8) of the Act, 17 CFR 240.15Ba1-1(g) and ~~the~~other rules and regulations thereunder.

(viii) "Obligated person" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(10) of the Act, 17 CFR 240.15Ba1-1(k) and ~~the~~other rules and regulations thereunder.

(ix) "Official statement" shall, for purposes of this rule, have the same meaning as in Rule G-32(d)(vii).

---Supplementary Material:

.01 Duty of Care. Municipal advisors must exercise due care in performing their municipal advisory activities. The duty of care includes, but is not limited to, the obligations discussed in this section. A municipal advisor must possess the degree of knowledge and expertise needed to provide the municipal entity or obligated person client with informed advice. A municipal advisor also must make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client. ~~A municipal advisor that is engaged by a client in connection with either an issuance of municipal securities or a municipal financial product that is related to an issuance of municipal securities must also undertake a thorough review of the official statement for that issue, unless otherwise directed by the client and documented under subsection (c)(iv) of this rule.~~ A municipal advisor must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. Among other matters, a municipal advisor must have a reasonable basis for:

(a) any advice provided to or on behalf of a client;

(b) any representations made in a certificate that it signs that will be reasonably foreseeably relied upon by the client, any other party involved in the municipal securities transaction or municipal financial product, or investors in the municipal entity client's securities or securities secured by payments from an obligated person client; and

(c) any information provided to the client or other parties involved in the municipal securities transaction ~~when participating~~ in connection with the preparation of an official statement for any issue of municipal securities with respect to which the advisor is advising.

.02 Duty of Loyalty. Municipal advisors must fulfill a duty of loyalty in performing their municipal advisory activities for municipal entity clients. The duty of loyalty includes, but is not limited to, the obligations discussed in this section. A municipal advisor must deal honestly and with the utmost good faith with a municipal entity client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. A municipal advisor to a municipal entity client must either eliminate or provide full and fair disclosure to the client about each of its material conflicts of interest. A municipal advisor must ~~investigate or consider other reasonably feasible alternatives to any recommended~~not engage in municipal ~~securities transaction or municipal financial product~~advisory activities with a municipal entity client if it cannot manage or mitigate its conflicts in a manner that ~~might also or alternatively serve~~will permit it to act in the municipal ~~entity client's objectives.~~entity's best interests.

.03 Action Independent of or Contrary to Advice. If a municipal entity or obligated person client of a municipal advisor elects a course of action that is independent of or contrary to advice provided by the advisor, the advisor is not required on that basis to disengage from the municipal advisory relationship.

.04 Limitations on the Scope of the Engagement. Nothing contained in this rule shall be construed to permit the municipal advisor to alter the standards of conduct or impose limitations on any of the duties prescribed herein. If requested or consented to by the municipal entity or obligated person client, however, a municipal advisor may limit the scope of the municipal advisory ~~relationship~~activities to certain specified activities or services. If the municipal advisor engages in a course of conduct that is inconsistent with any such agreed upon limitations, it may result in negating the effectiveness of such limitations.

.05 Conflicts of Interest. Disclosures of conflicts of interest by a municipal advisor to its municipal entity or obligated person client must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict. Such disclosures also must include an explanation of how the advisor addresses or intends to manage or mitigate each conflict.

.06 Inadvertent Advice. A municipal advisor is not required to comply with sections (b) and (c) of this rule if the advisor meets all of the following requirements. In the event that a municipal advisor inadvertently engages in municipal advisory activities for or on behalf of a municipal entity or obligated person and does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship, the municipal advisor must, as promptly as possible, provide a document to such municipal entity or obligated person that is dated and includes:

(A) a disclaimer that the advisor did not intend to provide advice and that, effective immediately, it has ceased engaging in municipal advisory activities;

(B) a notification that such municipal entity or obligated person should be aware that the disclosure of material conflicts of interest and other information required by section (b) of this rule has not been provided;

(C) a representation by the advisor that it, in good faith, has undertaken reasonable efforts to identify the advice that was inadvertently provided; and

(D) a request that the municipal entity or obligated person acknowledge receipt.

A municipal advisor utilizing this alternative must promptly conduct a review of its written supervisory and compliance policies and procedures to ensure they are reasonably designed to prevent the provision of inadvertent advice to municipal entities and obligated persons.

.07 Applicability of State or Other Laws and Rules. Municipal advisors may be subject to fiduciary or other duties under state or other laws. Nothing contained in this rule shall be deemed to supersede any more restrictive provision of state or other laws applicable to the activities of municipal advisors. In addition, the specific prohibition in section (e)(ii) of this rule shall not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities, provided that the municipal advisor complies with all of the provisions of Rule G-23.

~~.07~~.08 Disclosure to Investors. If all or a portion of a document prepared by a municipal advisor or any of its affiliates is included in an official statement for any issue of municipal securities by or on behalf of its municipal entity or obligated person client, the municipal advisor must provide written disclosure to investors, which disclosure may be provided in the official statement, of any affiliation that meets the criteria of subsection ~~(b)(ii)~~ (b)(i)(B) of this rule. This disclosure requirement shall be deemed satisfied if the relevant affiliate provides the required written disclosure to investors.

~~.08~~.09 Suitability. A determination of whether a municipal securities transaction or municipal financial product is suitable must be based on the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued in the municipal securities transaction are reasonably expected to be outstanding and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry.

~~.09~~.10 Know Your Client. A municipal advisor must use reasonable diligence, in regard to the maintenance of the municipal advisory relationship, to know and retain the essential facts concerning the client and concerning the authority of each person acting on behalf of such client. The facts "essential" to "knowing a client" include those required to:

(a) effectively service the municipal advisory relationship with the client;

(b) act in accordance with any special directions from the client;

(c) understand the authority of each person acting on behalf of the client; and

(d) comply with applicable laws, regulations and rules.

~~.10~~**.11 Excessive Compensation.** Depending on the specific facts and circumstances of the engagement, a municipal advisor's compensation may be so disproportionate to the nature of the municipal advisory services performed as to constitute an unfair practice in violation of Rule G-17. Among the factors relevant to whether a municipal advisor's compensation is disproportionate to the nature of the municipal advisory services performed are the municipal advisor's expertise, the complexity of the municipal securities transaction or municipal financial product, whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product, the length of time spent on the engagement and whether the municipal advisor is paying any other relevant costs related to the municipal securities transaction or municipal financial product.

.12 529 College Savings Plans and Other Municipal Fund Securities. This rule applies equally to municipal advisors to sponsors or trustees of 529 college savings plans and other municipal fund securities. All references in this rule to an "official statement" include the plan disclosure document for a 529 college savings plan and the investment circular or information statement for a local government investment pool.

* * * * *

Rule G-8: Books and Records to be Made by Brokers, Dealers, Municipal Securities Dealers, and Municipal Advisors[15]

(a) - (g) No change.

(h) *Municipal Advisor Records*. Every municipal advisor that is registered or required to be registered under Section 15B of the Act and the rules and regulations thereunder shall make and keep current the following books and records:

(i) ~~*General Business Records.* All books and records described in Rule 15Ba1-8(a)(1)-(8) under the Act.~~Reserved.

(ii) Reserved.

(iii) Reserved.

[15] The MSRB has multiple rulemaking initiatives currently pending that would revise Rules G-8 and G-9. The revised draft amendments to Rules G-8 and G-9 reflect the substance that is related to revised draft Rule G-42, and technical or non-substantive changes will be made as necessary depending on the progress of this and the other rulemaking initiatives.

(iv) *Records Concerning Duties of Non-Solicitor Municipal Advisors pursuant to Rule G-42.*

(A) A copy of any document created by a municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any conclusions as to suitability; and

(B) Unless included in the official statement for an issue of municipal securities, a copy of any disclosure provided by the municipal advisor or any affiliate of the municipal advisor to investors, as required by the provisions of Rule G-42 Supplementary Material 08.

(v) Reserved.

* * * * *

Rule G-9: Preservation of Records

(a) - (g) No change.

(h) *Municipal Advisor Records*. Every municipal advisor shall preserve the books and records described in Rule G-8(h) for a period of not less than five years.

Alphabetical List of Comment Letters on Notice 2014-12 (July 23, 2014)

1. American Bankers Association: Letter from Cristeena Naser, Vice President, Center for Securities, Trust & Investments, dated August 25, 2014

2. American Council of Engineering Companies: Letter from David A. Raymond, President and CEO, dated August 25, 2014

3. Bart Leary: E-mail dated July 23, 2014

4. Bond Dealers of America: Letter from Michael Nicholas, Chief Executive Officer, dated August 25, 2014

5. Columbia Capital Management, LLC: Letter from Jeff White, Principal, dated August 25, 2014

6. Dave A. Sanchez: Letter dated August 25, 2014

7. Financial Services Roundtable: Letter from Richard Foster, Vice President and Senior Counsel for Regulatory and Legal Affairs, dated August 25, 2014

8. Florida Division of Bond Finance: Letter from J. Ben Watkins III, Director, dated August 22, 2014

9. Government Finance Officers Association: Letter from Dustin McDonald, Director, Federal Liaison Center, dated September 2, 2014

10. Investment Company Institute: Letter from Tamara K. Salmon, Senior Associate Counsel, dated August 19, 2014

11. Lewis Young Robertson & Burningham, Inc.: Letter from Laura D. Lewis, Principal, dated August 25, 2014

12. National Association of Independent Public Finance Advisors: Letter from Jeanine Rodgers Caruso, President, dated August 25, 2014

13. New York State Bar Association, Business Law Section, Securities Regulation Committee: Letter from Peter W. LaVigne, Chair of the Committee, dated August 27, 2014

14. Piper Jaffray: Letter from Frank Fairman, Managing Director, Head of Public Finance Services, dated August 25, 2014

15. Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated August 25, 2014

16. Southern Municipal Advisors, Inc.: Letter from Michael C. Cawley, Senior Consultant, dated August 25, 2014

17. Wells Fargo Advisors, LLC: Letter from Robert J. McCarthy, Director of Regulatory Policy, dated August 25, 2014

18. WM Financial Strategies: Letter from Joy A. Howard, Principal, dated August 25, 2014

19. Zions First National Bank: Letter from W. David Hemingway, Executive Vice President, dated August 25, 2014

American Bankers Association

Cristeena Naser
Vice President
Center for Securities, Trust & Investments
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BY ELECTRONIC MAIL

August 25, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: ***MSRB Regulatory Notice 2014-12***
Request for Comment on Revised Draft MSRB Rule G-42
Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith,

The American Bankers Association (ABA)[1] appreciates this opportunity to comment on Regulatory Notice 2014-12 issued by the Municipal Securities Rulemaking Board (MSRB). This Regulatory Notice revises MSRB Draft Rule G-42 on the standards of conduct and duties of municipal advisors engaging in municipal advisory activities other than solicitation.

ABA is most appreciative of the MSRB's responsiveness to the comments received on its first draft of Rule G-42. We believe the re-proposal significantly increases the ability of banks to continue to provide services to municipal entities within the scope of the new municipal advisor regulatory regime. We strongly support the MSRB's determination that neither the proposed fiduciary duty nor the prohibition on principal transactions should be extended to obligated persons. We are particularly appreciative that the scope of the prohibition on principal transactions has been better tailored. Our comments in this letter address clarification of the scope of Revised Draft Rule G-42, the principal transactions provision, and an appropriate effective date.

Clarification of the Scope of Revised Draft Rule G-42
In the definitions section of the preamble,[2] the MSRB noted commenters' requests that Rule G-42 "should state clearly that it does not apply to activities that have been excluded or exempted under either the Dodd-Frank act or the SEC Final Rule."[3] The preamble further states that "[t]he references in the initial Draft Rule to the Exchange Act and the rules and regulations thereunder encompassed the statutory exclusions and the rule-based exemptions." In Revised Draft Rule G-42, the MSRB has in paragraph (f)(v) defined the term "municipal advisory activities" for purposes of this rule to be those that would cause a person to be a municipal advisor as defined in the final rule issued by the Securities and Exchange Commission.

[1] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $14 trillion banking industry and its 2 million employees. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities. Learn more at www.aba.com.
[2] MSRB Regulatory Notice 2014-12 at 16.
[3] Securities Exchange Act of 1934, Section 15B(e)(4), 17 CFR 240.15Ba1-1(d)(1)-(4).

Nonetheless, given the desire of banking organizations for clear guidance, we urge the MSRB to state explicitly that the ban on principal transactions does *not* apply to any activity (including excluded or exempted activities) that does not require registration as a municipal advisor under the SEC's final rule. This is particularly critical in the case of bank loans to municipal entities in cases where the loan appears to be a security and thus may appear nominally to come within the ambit of the definition of "principal transaction" as formulated in Revised Draft Rule G-42.

Prohibition on Principal Transactions
As re-proposed, the prohibition would apply to principal transactions by the municipal advisor or its affiliate that are directly related to the advised transaction. The MSRB has further defined the term "engaging in a principal transaction" to encompass only those transactions in which the municipal advisor or its affiliate is acting as a principal:

- Selling to or purchasing from a municipal entity any securities; or
- Entering into any derivative, guaranteed investment contract or similar financial product with the municipal entity.

These two critical revisions are most welcome and go far to make workable the fiduciary duty. However, we are concerned that in large complex multi-entity, geographically dispersed banking organizations, there remains a distinct possibility that an affiliate of a municipal advisor (or another unit within the same bank that has established a municipal advisor in a separately identifiable department or division (SIDD)) may be unaware of the scope of an advisory relationship and unknowingly engage in a transaction that is related to the advised transaction. We believe such an inadvertent situation could occur even if a large banking organization incurred the cost of investing in the extensive monitoring necessary and prudently supervised its activities to detect all potential "affiliated" principal transactions. Moreover, banking organizations often impose internal "Chinese Walls" to prevent the improper disclosure of material information, ensure privacy, and/or ensure that client information does not extend beyond general "need to know" parameters, a system that could inappropriately be undermined by a monitoring system intended to address "affiliated" transactions. However, rigorous application of such a Chinese Wall could make it difficult for an institution to recognize a transaction of concern.

We recognize that the purpose of imposing a fiduciary duty on municipal advisors is to ensure that municipal entities receive disinterested advice. In the case of an affiliate (including another unit within the same bank which has established a municipal advisor SIDD) without knowledge of the municipal advisory engagement or its scope, we suggest that this objective of the MSRB could be achieved if the municipal advisor did not advise the municipal entity to engage in such transaction.

In addition, we urge the MSRB to clarify that the prohibition on principal transactions applies only in the case of advice provided pursuant to a municipal advisory relationship. Paragraph (e)(ii) should be revised to read as follows:

> (ii) A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice *pursuant to a municipal advisory relationship*.

Finally, we believe that the new sentence of Supplementary Material .07 concerning the inapplicability of the principal prohibition to the exemption in MSRB Rule G-23 is unneeded. Rule G-23 applies in any event. Should the MSRB determine to retain this language, the proviso at the end should be revised to read: *provided that such a transaction is not prohibited by the provisions of Rule G-23.*

We strongly urge the MSRB to adopt these further limited amendments to the prohibition on principal transactions in Revised Draft Rule G-42.

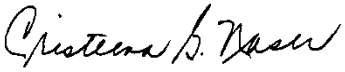
Transition Period
We urge the MSRB to provide a transitional provision in Revised Draft Rule G-42 to permit advisors to honor their existing financial advisory agreements with advised clients. Many financial advisory firms have a large number of existing financial advisory agreements, many of which are multi-year contracts. A significant amount of time and expense would be required to supplement or amend these agreements with the additional content and disclosures required by paragraph (c) of Revised Draft Rule G-42. Importantly, municipal entities may conclude under the particular state and/or local procurement laws applicable to them that an amendment to an existing municipal advisory agreement made to comply with provisions of the Revised Draft Rule might require the reopening of the request for proposal process for issuers to hire municipal advisors. Such a process could require a significant amount of time, effort, and expense for municipal advisors and their clients to implement, sometimes requiring publication of public notices and public hearings. Moreover, we cannot assume that municipal advisors would be able to compel their municipal entity and obligated person clients to revise existing contracts in accordance with the new MSRB requirements.

Accordingly, we ask the MSRB to allow firms to continue to operate under existing advisory agreements until they expire and then enter into new agreements that meet all of the G-42 requirements. However, as part of such a transition, we believe it would be appropriate for municipal advisors to provide to their advisory clients within 60 days of the effective date of a final rule the disclosures required by Revised Draft Rule G-42(b) of material conflicts and disciplinary actions. Other than these disclosures, we believe that contracts in place on the effective date of a final rule should be honored and allowed to run their course until termination in accordance with their terms. Upon such termination, the required contractual provisions of a final rule would be required to be included in new municipal advisory agreements between the parties.

Conclusion
ABA greatly appreciates the MSRB's responsiveness to the concerns we raised in our previous comment letter. However, as discussed above, we believe that additional changes are merited with respect to the scope of the prohibition on principal transactions to address the concerns of banking organizations. In addition to concerns about unknowing violations of this prohibition, we believe it is important for the MSRB to state explicitly that the prohibition does not apply to activities that are excluded or exempted under the SEC final rule. We believe also that a transition period to allow existing contracts to expire according to their terms is warranted so long as appropriate disclosures are provided to advisory clients within 60 days of the effective date of a final rule.

If you have questions about any of the issues raised in this letter, please do not hesitate to contact me.

Sincerely,



Cristeena G. Naser
Vice President
Center for Securities, Trust & Investment

ACEC
American Council of Engineering Companies
100 Years of Excellence

David A. Raymond
President & CEO

August 25, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314

Re: MSRB Revised Draft Rule G-42

Dear Mr. Smith:

On behalf of the American Council of Engineering Companies (ACEC) – the national voice of America's engineering industry – I appreciate the opportunity to comment on the Municipal Securities Rulemaking Board's (MSRB's) Revised Draft Rule G-42 regarding the duties of non-solicitor municipal advisors.

ACEC members – numbering more than 5,000 firms representing hundreds of thousands of engineers and other specialists throughout the country – are engaged in a wide range of engineering works that propel the nation's economy, and enhance and safeguard America's quality of life. Many of our member firms work with municipal clients and could potentially be affected by the municipal advisor registration rule and related regulations.

We would like to begin by expressing our appreciation that the MSRB addressed several issues we raised in our comment letter of March 7, 2014, on the initial version of Draft Rule G-42. In particular, we agree with the MSRB's decision to limit the application of fiduciary duty to a municipal advisor's municipal entity clients. In addition, we believe removing the requirement that municipal advisors disclose details pertaining to professional liability insurance was the correct decision. Finally, we appreciate the MSRB's acknowledgement that at least some portion of compliance costs will be passed on to municipal entity clients.

We are, however, disappointed that the MSRB did not address the primary concern we raised. As we previously highlighted, the fiduciary duty of a municipal advisor to act in the interest of a client required by Revised Draft Rule G-42 could come into direct conflict with the engineer's professional and ethical responsibilities to the public at large.

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Engineering is a profession that is heavily regulated by state boards of engineering, and is founded on professional credentials and personal integrity as a condition of licensure. The regulations of the various state licensing boards for professional engineers delineate the ethical duty of the engineer to uphold the safety, health, and welfare of the public. For example, the Commonwealth of Virginia's Board for Architects, Professional Engineers, Land Surveyors, Certified Interior Designers, and Landscape Architects' current regulations, which have the force and effect of law, provide as follows:

> *The primary obligation of the professional is to the public. The professional shall recognize that the health, safety, and welfare of the public are dependent upon professional judgments, decisions, and practices. If the professional judgment of the professional is overruled under circumstances when the health, safety, and welfare, or any combination thereof, of the public are endangered, the professional shall inform the employer and client of the possible consequences and notify appropriate authorities.*

The same obligation is reflected in the codes of ethics of private professional associations such as ACEC and the National Society of Professional Engineers (NSPE), as well as related professional associations such as the American Institute of Architects (AIA).

In the course of providing professional engineering services to a client, circumstances could arise in which the engineer would find himself or herself facing a conflict between breaching the fiduciary obligations of a municipal advisor and violating the ethical obligations imposed upon the engineer under applicable state licensing board regulations and/or one or more professional associations. This is a conflict that must be resolved, with priority given to the engineer's role in protecting health and safety.

For the purposes of illustrating our concern, consider the following hypothetical set of facts and circumstances, which are loosely based on a story related to ACEC staff by a representative of one of ACEC's member firms. A municipal entity client engages an engineer "to prepare revenue projections to support the structure of an issuance of municipal securities," which services are "outside the scope of the engineering exclusion" and constitute "municipal advisory activity." (See page 229 of the SEC's final rule.) In the course of performing its services, the engineer undertakes a ridership study of the municipal entity's public transportation system. In the course of performing field work in support of this study, the engineer suspects the presence of noxious fumes emanating from the ground beneath one of the transportation system's stations. While for the most part the station is not enclosed, the station does have a large roof structure providing protection for system users. The engineer is concerned about the possibility of these suspected noxious fumes being trapped beneath the roof structure and, over time, accumulating to a level that could potentially be harmful to people. The engineer voices his concerns to his municipal entity client. Concerned over the possible negative consequences such information might have on ridership at this station, the municipal entity client instructs the engineer not speak to anyone else regarding this matter. In such a circumstance, the engineer faces a conflict between his ethical duties as an engineer to

advise his client to address his concerns or the appropriate authorities will be notified, and his fiduciary duty to his client.

Our understanding of Revised Draft Rule G-42 is that the fiduciary duties imposed upon one who provides municipal advisory services will apply only to those services. However, we are concerned that there might not be a bright line between municipal advisory services and non-municipal advisory services in all circumstances. In its final rule, the SEC wrote, in pertinent part, as follows: "While the Commission believes that the determination of whether a person provides advice to or on behalf of a municipal entity or obligated person depends on all the relevant facts and circumstances, the Commission also believes that additional guidance on the advice standard for purposes of the municipal advisor definition will provide greater clarity regarding the applicability of the municipal advisor registration requirement."

We had hoped for greater clarity from the MSRB with respect to the issue of potential conflicts of interest for engineers in performance of serving their municipal clients. Respectfully, we urge the MSRB to address this conflict before finalizing Revised Draft Rule G-42.

Thank you for your consideration of our comments, and we look forward to working with the MSRB as the rulemaking process moves forward.

Sincerely,

David A. Raymond
President & CEO

Comment on Notice 2014-12

from Bart Leary,

on Wednesday, July 23, 2014

Comment:

So does that mean a person can give Municipal advice to an obligated person and not need to be registered with the SEC or MSRB? Is a Multifamily developer an obligated person?

BDA Bond Dealers of America

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202.204.7900
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August 25, 2014

VIA ELECTRONIC MAIL

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: MSRB Notice 2014-12 (July 23, 2014) – Request for Comment on Revised MSRB Rule G-42

Dear Mr. Smith:

On behalf of the Bond Dealers of America ("BDA"), I am pleased to submit this letter in response to Municipal Securities Rulemaking Board ("MSRB") Notice 2014-12 ("Notice") seeking comment on revised draft MSRB Rule G-42 (the "Revised Draft") on duties of non-solicitor municipal advisors. BDA is the only DC-based group representing the interests of middle-market securities dealers and banks focused on the U.S. fixed income markets. Accordingly, we believe that we uniquely offer insight into how the Revised Draft would impact middle-market securities dealers.

Principal Transactions. The BDA supports the MSRB's approach in the Revised Draft with respect to when municipal advisors are prohibited from engaging in a principal transaction with a client. We believe that it is very important that any such prohibition operate on a transaction-by-transaction basis rather than more broadly restricting a person from acting as a principal on a transaction that is unrelated to the municipal advisory relationship. In that light, section (e)(ii) seems to create confusion relative to this principal when it states, "A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction **directly related to** [emphasis added] the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice." We feel the term "directly related to" is vague and open to interpretation. It is not clear to us exactly what transactions would be considered "directly related to" other transactions. For example, would selling securities, as a principal after winning a competitive bid for an open market refunding escrow, on a refunding bond issue for which the firm was a municipal advisor be "directly related to" the bond issue? Would acting as a municipal advisor for a swap while acting as the underwriter on a related series of variable rate bonds be too "directly related"? Would underwriting a refunding issue years after serving as a municipal advisor for the initial issue be a transaction that is considered "directly related to" the initial issue?

We would propose that the MSRB use the following language instead:

"A municipal advisor, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction with a municipal entity client if the

> structure, timing or terms of such principal transaction was established on the advice of the municipal advisor in connection with a municipal advisory relationship with such municipal entity client."

We believe that this re-phrased language addresses the core concern of the MSRB, which is to prohibit situations in which a municipal advisor structures a transaction and then creates a potential conflict of interest by participating as a principal in that transaction or a related transaction on which it has rendered advice.

Review of Recommendations. Under paragraph (d) of the Revised Draft, in any recommendation by a municipal advisor or a review by a municipal advisor of a recommendation of another party, the municipal advisor is required to determine that the related municipal securities transaction or municipal financial product is suitable for the client. In addition, the municipal advisor is required to inform the client of the matters described in subparagraphs (i) through (iii) of paragraph (d). While the BDA supports these requirements, our members have been reading these requirements with a view to future FINRA examinations and do not understand exactly how examiners will test a dealer's compliance with these requirements when serving as a municipal advisor. The BDA would propose that the MSRB provide specific language within Rule G-42 that permits municipal advisors to develop reasonable policies and procedures regarding when and how they communicate any of the requirements of paragraph (d) to clients orally or in writing.

Reference to Rule G-23. In note .07 under supplemental materials, the Revised Draft includes a new, second sentence. The last clause of that sentence reads, "provided, that the municipal advisor complies with all of the provisions of Rule G-23." The new language makes it no clearer than the language in the original proposed regulation, which mentioned Rule G-23, as to when it is possible for a municipal advisor to act as a principal on the same transaction on which they are providing advice.

Acting as Underwriter for Conduit Issuer and Municipal Advisor for Obligated Person. The Revised Draft does not explicitly address a fact pattern that occurs in the municipal market. The BDA believes that there is (and should be) no prohibition on a dealer serving as an underwriter for a conduit issuer and a municipal advisor for an obligated person, even with respect to related matters. We would propose that the MSRB add a clarification in note .07 under the supplemental materials that there is nothing in Rule G-42 that prevents a dealer from acting as an underwriter for the conduit issuer and as a municipal advisor for an obligated person.

Thank you for the opportunity to submit these comments on the Revised Draft.

Sincerely,

Michael Nicholas

Chief Executive Officer

COLUMBIA CAPITAL
MUNICIPAL ADVISORS

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August 25, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

RE: Request for Comment/Revised Draft MSRB Rule G-42

Dear Mr. Smith:

Please find below our comments in response to the MSRB's request for comment regarding the revised draft of its Rule G-42. Columbia Capital Management, LLC is a registered municipal advisor.

Section b(i)(F)—Fee Disclosures
We object to the revised draft as written because it creates the appearance that the MSRB takes the position that one fee modality is less preferable to all others. Anytime a municipal advisor (MA) charges a fee to its client, it creates an adversarial relationship: the MA desires to maximize its fee revenue while the issuer or obligated party seeks to reduce its costs to zero. Every fee modality creates a set of incentives and disincentives for the MA. The revised draft rule appears to favor those fee arrangements that are non-contingent and not based on the size of the transaction. While we recognize contingent, size-based fees create a financial incentive for the MA to advise its clients in such a way that transactions are both complete and large, other fee modalities suffer from similar incentives adverse to the client:

- **hourly fees** create a financial incentive for the MA to extend the transaction and to perform work that might not be necessary to fully and fairly advise the client. Abuses of hourly fee structures in the legal profession, for instance, have been widely documented in recent years.

- **fixed fees** create a financial incentive for the MA to minimize the work effort necessary to complete the scope of services, which might lead to a lower level of service or analysis.

- **non-contingent fees** may misalign the interests of a client desiring to complete a transaction, especially a complex one, with an MA that is financially rewarded equally for either a completed or uncompleted transaction. We also note that many of our clients do not have routine operating budget authority for the payment of transaction professionals outside of bond proceeds.

The debate about the "correct" fee modality has been raging in the investment advisory community for years. We encourage the MSRB to avoid entering the fray in this space.

We are not opposed to required disclosures that generally address common fee modalities for MAs and their embedded incentives and disincentives.

Section c—Documentation of Advisory Relationship
We encourage the MSRB to indicate explicitly that these required agreements and disclosures may be made in one or more documents. Many issuers have standard forms of agreements that do not permit the inclusion of information required by the draft rule.

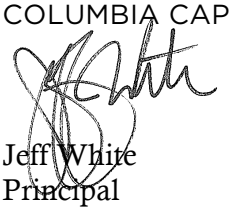
Section (f)(vi)—Municipal Advisory Relationship
We object to the striking of the word, "engages." If a person provides "advice" he/she should trigger the MA duties at the time of providing that advice and should be considered an MA unless that person qualifies for an exemption or exclusion at the time such advice is provided.

Supplementary .07—Applicability of State or Other Laws
We suggest that the added language contemplates a situation where an MA **could** serve as a principal in a transaction for which it provides MA services, creating a conflict with new Section e(iii). We suggest the MSRB strike the added language to avoid any ambiguity with respect to the draft rule's absolute prohibition of principal transactions in Section e(iii).

Supplementary .11—Excessive Compensation
For the reasons described above, we suggest the MSRB strike the phrase, "whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product." Additionally we suggest the MSRB add, as an additional factor, a comparison of the MA's fee to those of other professionals engaged on the transaction in question.

We appreciate your consideration of our comments.

Respectfully submitted,
COLUMBIA CAPITAL MANAGEMENT, LLC



Jeff White
Principal

Dave A. Sanchez, Attorney at Law

August 25, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: MSRB Notice 2014-12 Relating to Standards of Conduct for Municipal Advisors

Dear Mr. Smith:

I appreciate the opportunity to provide comments to the Municipal Securities Rulemaking Board (MSRB) on the revised version of proposed Rule G-42, which would govern standards of conduct for non-solicitor municipal advisors.

These comments are informed by a background that includes, amongst other relevant experience, advising registered municipal advisors with respect to their compliance obligations and serving as general counsel to a municipal broker-dealer that was also registered as a municipal advisor.

This proposed rule covers a wide range of potential activity and the MSRB appears to have done a very good job of incorporating comments from various perspectives into this revised proposal. However, it does appear that several of the provisions in the revised proposal appear to be overly prescriptive or not clearly targeted to achieve the MSRB's regulatory mandate with respect to the core statutory standard of conduct for municipal advisors which is their fiduciary duty to their municipal entity clients. Although in the revised proposal the MSRB cites broad statutory authority to develop standards of conduct for municipal advisors, the only specific statutory authority afforded to the MSRB with respect to the fiduciary duty of municipal advisors is found in Section 15B(b)(2)(L)(i) of the Exchange Act. That Section of the Exchange Act directs the MSRB to "prescribe means reasonably designed to *prevent* acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients." (emphasis added). Notably, the Exchange Act does not contain a specific direction to the MSRB to define "fiduciary duty" or to prescribe means designed to effectuate the performance of that duty. Although it is true that the MSRB has broader authority under the Exchange Act to adopt rules (with respect to municipal advisory activities) designed to prevent fraudulent and manipulative acts and practices, and, in general, to protect municipal entities, obligated persons, and the public interest, the MSRB should consider the view that in the exercise of such authority they should, as some prior commenters suggested, identify the fraudulent and manipulative acts and practices they are addressing in the exercise of such authority.

My specific comments on the proposed rule are set forth below.

Rule G-42(a)(i) and Supplementary Material .01 Duty of Care

Please see comments below regarding Supplementary Material .01.

Rule G-42(b)(i)(A) and Rule G-42(b)(i)(G) [with respect to obligated person clients]

Although the MSRB does not believe that the Draft Rule G-42 implicitly and inappropriately imposed fiduciary duty obligations on municipal advisors whose clients are obligated persons, the language in proposed Rules G-42(b)(i)(A) and G-42(b)(i)(G) appear to import the duty of loyalty and duty of care into the representations of obligated persons by using the phrase "unbiased and competent advice" with respect to advice provided to or on behalf of obligated persons. These provisions may generate fewer objections if they were worded to say "impair its ability to render advice to or on behalf of the obligated person in accordance with the standards of conduct required in clause (a)" in lieu of the offending phrase referencing "unbiased and competent advice."

Rule G-42 (b)(i)

The last sentence of this section requires a municipal advisor to provide "written documentation" of its conclusion that is has no material conflicts of interest. The MSRB should consider why a "written statement" to that effect is not sufficient. It is difficult to imagine what level of documentation is required to demonstrate a negative conclusion.

Rule G-42 (b)(ii)

This requirement appears to be overly burdensome particularly because it applies to every engagement. It is undoubtedly important that municipal entities, in particular, are aware of any legal or disciplinary event that is "material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel" but it should be sufficient for purposes of this rule that a municipal advisor be required to direct clients to their EDGAR filings by providing clients with sufficiently specific information to locate their EDGAR filings. In this revised proposal, the municipal advisor now has to potentially make two separate written disclosures (see also Rule G-42 (c) below) to describe to clients information that is already publicly available on EDGAR and which is also routinely requested by municipal entities as part of their RFP/RFQ processes.

The MSRB should also consider the question of how this additional written disclosure of publicly available information "prevents" acts inconsistent with fiduciary duty or what specific fraudulent and manipulative acts and practices it prevents. In any event, in conjunction with its determinations with respect to this

proposed rule, the MSRB should concurrently consider whether such additional written disclosure regarding publicly available information should also be required of brokers, dealers and municipal securities dealers in connection with their standards of conduct.

Rule G-42(c)

The requirements of clauses (iii) and (iv) in proposed Rule G-42 (c) certainly appear overly prescriptive and not reasonably designed to *prevent* acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients. As noted above, it would appear to be a legitimate requirement for purposes of protecting municipal entities and obligated persons for a municipal advisor to provide information identifying where their client may electronically access their specific Form MA and Forms MA-I but all of the other information required by these two clauses is duplicative and especially burdensome to have to be included in <u>every</u> contract. This level of disclosure regarding legal events and disciplinary history is certainly not required of other regulated entities. In addition, many municipal entities routinely require disclosure of this type of information in conjunction with their RFP and RFQ processes. This would mean that a municipal advisor, in addition to being required to make disciplinary information freely and publicly available on EDGAR and in conjunction with an RFP or RFQ, would also have to possibly provide the same information to a client two more times in order to satisfy the requirements of proposed Rules G-42(b) and (c).

As noted in the prior sentence, the MSRB should also consider whether the wording of clause (ii) in proposed Rule G-42(c), in conjunction with the requirements of proposed Rule G-42(b) appears to require the same disclosures to be made in writing to the client twice in certain circumstances.

Rule G-42 (e)

Rule G-42(e)(i)(E) should also allow for reasonable fees paid to affiliates because soliciting on behalf of affiliates does not trigger a requirement for a person to register as a municipal advisor.

Definition of "engaging in a principal transaction"

It would be helpful for purposes of clarity to include a non-exhaustive list of specific common roles (such as underwriter) in addition to the general description.

Supplementary Material

.01 Duty of Care

The MSRB should consider whether the information for which "a municipal advisor must have a reasonable basis for" incorporated in clauses (a) through (c) is not already addressed in the standards of conduct required of municipal advisors by MSRB Rule G-17 and general antifraud rules related to municipal securities disclosure. While it seems consistent with appropriate standards of conduct to require in clause (a) a municipal advisor to have a reasonable basis for any advice provided to or on behalf of a client that requirement appears to already be embodied in the previous text of this Supplementary Material. The requirements of clauses (b) and (c) create obligations with respect to third parties and/or investors that are already addressed in MSRB Rule G-17 and the antifraud rules applicable to municipal securities disclosure. The MSRB should delete all text after "Among other matters . . . " from this Supplementary Material in order to avoid unnecessarily duplicative regulatory requirements.

.05 Conflicts of Interest

It appears overly broad for the MSRB to require that conflict disclosures include an explanation of how the advisor addresses or intends to manage or mitigate each conflict. This requirement is not imposed on municipal broker-dealers and the MSRB has not articulated why such additional requirement with respect to conflict disclosure is warranted in this circumstance. The MSRB should consider requiring such explanation of a municipal advisor to be delivered only if requested by their client.

.06 Inadvertent Advice

While it appears reasonably clear at the moment that Supplementary Material .06 is only intended to provide relief from subsections (b) and (c) of proposed Rule G-42, it would probably be useful for the MSRB to also include an affirmative statement that even inadvertent advice is subject all other rules and requirements applicable to municipal advisory activities and financial advisory relationships entered into by broker-dealers under MSRB Rule G-23. This would provide additional clarity and avoid the possibility that this provision would result in a dangerous loophole that could be exploited in the future with the argument that complying with these procedures resulted in a finding that no advice was provided.

.07 Applicability of State or Other Laws and Rules

This Supplementary Material provides that it is not a violation of proposed Rule G-42(e)(ii) for a broker, dealer or municipal securities dealer to act as an underwriter

with respect to an issuance of municipal securities for which they also act as a municipal advisor as long as they comply with all of the provisions of MSRB Rule G-23. The plain text of MSRB Rule G-23, and in particular the last sentence of MSRB Rule G-23(b) provides that "For purposes of this rule, a financial advisory relationship shall not be deemed to exist when, in the course of acting as an underwriter and not as a financial advisor, a broker, dealer or municipal securities dealer renders advice to an issuer, including advice with respect to the structure, timing, terms and other similar matters concerning the issuance of municipal securities."

A plain text reading of this provision (substituting "municipal advisor" for "financial advisor") would appear to be consistent with the Exchange Act. However, the MSRB's interpretive notice of November 27, 2011 of this provision and Rule G-23(d) contain guidance that is at odds with the Exchange Act as subsequently interpreted by the SEC in the Commission's final municipal advisor rule. For example, this November 2011 guidance states that "a dealer that clearly identifies itself in writing as an underwriter and not as a financial advisor from the earliest stages of its relationship with the issuer with respect to that issue (e.g., in a response to a request for proposals or in promotional materials provided to an issuer) will be considered to be "acting as an underwriter" under Rule G-23(b) with respect to that issue." This guidance would allow a dealer to comply with proposed Rule G-42 simply by making a G-23 disclosure and then acting as both an underwriter and municipal advisor (using the SEC interpretation of both of those terms) for the same issuance of municipal securities. This guidance would appear to be directly at odds with SEC' staff guidance in its FAQs with respect to the municipal advisor rule that specifically said a broker-dealer could not serve "as the municipal advisor to a municipal entity in the early stages of a financing transaction involving the issuance of municipal securities and then switch roles to serve as the underwriter when the municipal entity decides to proceed with that issuance of municipal securities." That November 2011 guidance on G-23 further provides that "it shall not be a violation of Rule G-23(d) for a dealer that states that it is acting as an underwriter with respect to the issuance of municipal securities to provide advice with respect to the investment of the proceeds of the issue, municipal derivatives integrally related to the issue, or other similar matters concerning the issue." This guidance would presumably allow a broker-dealer to provide all manner of municipal advice to a municipal entity at the same time that it is serving as an underwriter even though the SEC has specifically identified advice with respect to municipal derivatives and advice with respect to the investment of proceeds as being outside the scope of an underwriting. Had the SEC approved this guidance subsequent to the Commission's adoption of the final municipal advisor rule, it might make sense to allow for its incorporation in proposed Rule G-42 but any SEC determination that such guidance was consistent with the Exchange Act in 2011 would probably not survive its subsequent interpretation of key Exchange Act provisions in its final municipal advisor rule.

It appears that this November 2011 guidance on Rule G-23 is not consistent with the Exchange Act as subsequently interpreted by the SEC and the MSRB should consider retracting and revising this guidance if it wants to allow G-23 "conflicts" compliance to stand in for G-42 standards of conduct compliance for municipal broker-dealers as contemplated by Supplementary Material .07. In addition to being developed prior to the adoption of the final municipal advisor rule, that November 2011 guidance was not developed with a municipal advisor's fiduciary duty in mind but was solely a "conflicts rule" and not a standard of conduct rule. That November 2011 guidance explicitly states that "Rule G-23 is solely a conflicts rule" and that "this [G-23 interpretive] notice does not address whether provision of the advice permitted by Rule G-23 would cause the dealer to be considered a "municipal advisor" under the Exchange Act and the rules promulgated thereunder." It seems odd for the MSRB to incorporate that conflicts guidance whole cloth into standards of conduct for municipal advisors when the guidance was developed prior to the SEC's interpretation of core provisions of the Exchange Act and without consideration of the fiduciary duty of a municipal advisor particularly when the MSRB has not discussed why it believes that the November 2011 guidance is still consistent with the Exchange Act.

.08 Disclosure to Investors and Rule G-8(h)(iv)(B)

It is unclear why these provisions are included in this standard of conduct rule. These provisions presume that a conflict of interest that is material to a client is also material to investors in a particular issuance of municipal securities. And, even if that were the case, antifraud rules already govern the requirement to make this disclosure. These provisions should be eliminated.

I appreciate the opportunity to provide these comments. If you have any questions regarding these comments please feel free to contact me by phone at (415-717-6588).

Sincerely,

/s/

Dave A. Sanchez

August 25, 2014

Submitted electronically to
http://www.msrb.org/CommentForm.aspx

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: **MSRB Regulatory Notice 2014-12 Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors**

Dear Mr. Smith:

The Financial Services Roundtable[1] ("FSR") appreciates the opportunity to comment on revised draft Municipal Securities Rulemaking Board ("MSRB") Rule G-42 ("Revised Draft Rule G-42"), which would specify the standards of conduct and duties of non-solicitor municipal advisors.[2]

I. Executive Summary

FSR commends the MSRB for its responsiveness to many of the concerns that commenters expressed about its initial draft of Rule G-42 ("Initial Draft Rule").[3]

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[1] *As advocates for a strong financial future*™, the Financial Services Roundtable represents 100 integrated financial services companies providing banking, insurance, payment and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine, accounting directly for $ 92.7 trillion in managed assets, $1.2 trillion in revenue, and 2.3 million jobs. Learn more at FSRoundtable.org.

[2] *See* Regulatory Notice 2014-12; *Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors* (Jul. 23, 2014), *available at* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-12.ashx?n=1 ("Regulatory Notice 2014-12").

[3] *See* MSRB Notice 2014-01, *Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors* (Jan. 9, 2014), *available at* http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-01.ashx?n=1.

Notwithstanding the modifications to Draft Rule G-42, FSR's members continue to have several concerns about the proposed rule.

i. Prohibition on Principal Transactions. When acting as a principal for one's own account, Revised Draft Rule G-42(e)(ii) would prohibit a municipal advisor from "selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client." Although the MSRB drew upon the prohibition on principal transactions in Section 206(3) of the Investment Advisers Act of 1940 ("Advisers Act"), it did not include any of the alternative means of compliance with the statutory prohibition that have been provided by the Securities and Exchange Commission ("SEC").[4] FSR's members strongly believe that, as with the prohibition on principal transactions applicable to SEC-registered investment advisers pursuant to Section 206(3), the MSRB should include an alternative mechanism for municipal advisors that would permit them to engage in principal transactions with municipal entities subject to disclosure and consent requirements. Given that municipal entities do not give discretionary authority to municipal advisors when they are acting in such capacity, such relief would be consistent with the relief granted by Advisers Act Rule 206(3)-(3)T.

ii. Disclosure Requirements. Revised Draft Rule G-42 would require municipal advisors to provide full and fair written disclosure to a municipal entity or obligated person client of all material conflicts of interest, including disclosure of any of its affiliates that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor. Municipal advisors are required to exercise reasonable diligence to identify material conflicts and, if none are identified, to provide disclosure to that effect to its clients. FSR's members are concerned that the requirement to disclose any advice, services or products provided indirectly by the municipal advisor as well as by any of its affiliates is vague and overly broad and would be very difficult for a municipal advisor to comply with if it is part of a large multi-service financial conglomerate.

Revised Draft Rule G-42 also would require a municipal advisor to provide written disclosure of any legal or disciplinary event that is material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel; and a description of the type of legal and disciplinary event required on Form MA and Form MA-I. FSR's members respectfully request that the MSRB provide guidance that if a municipal advisor is current in its publicly-available disclosures, and provides each municipal entity or obligated person client with information about where the advisor's Form MA and Form MA-I are located, the requirements of Revised Draft Rule G-42 will have been satisfied.

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4 *See, e.g.*, Rule 206(3)-3T under the Advisers Act.

II. Prohibition on Principal Transactions

Revised Draft Rule G-42(e)(ii) would prohibit a municipal advisor and its affiliates from "engaging in a principal transaction" directly related to the same municipal securities transaction or municipal financial product to which the municipal advisor is providing advice to the municipal entity client. "Engaging in a principal transaction" is proposed to be defined in paragraph (f)(i) of Revised Draft Rule G-42 to mean, "when acting as a principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client."

Although the MSRB noted that the principal trading prohibition is modeled on the prohibition in Section 206(3) of the Adviser Act, the MSRB did not include alternatives to the prohibition, such as those that are included in Rule 206(3)-3(T), which permits principal transactions with certain clients; provided that the adviser complies with prescribed disclosure and consent requirements. The SEC's approach to principal transactions by registered investment advisers recognizes that, while certain principal transactions may present conflicts of interest, in many cases it is appropriate to manage those conflicts through disclosure to and waiver by the client, at its discretion. FSR's members believe that a similar approach is appropriate for municipal advisors' principal transactions.

The approach set forth in in Revised Draft Rule G-42 is overbroad and unnecessary, particularly when, as the MSRB noted, municipal advisors are subject to the MSRB's fundamental fair-practice rule, Rule G-17. A prohibition on principal transactions could deprive clients of access to certain products and services because a municipal advisor or its affiliates may be prohibited from transacting with a municipal entity that engages the municipal advisor to provide municipal advisory services. Rather than imposing such a broad brush prohibition, FSR's members recommend that the MSRB permit municipal advisors and their affiliates to manage conflicts through disclosure and consent, as appropriate under the circumstances. As currently drafted, this prohibition may cause some organizations to assess the economic impact of acting as a municipal advisor in comparison to the value of providing all other services and products to municipal clients.

To the extent the MSRB does not revise the prohibition on principal transactions to allow for disclosure of and consent to any potential conflicts rather than a complete ban, the MSRB should consider the extent to which this prohibition should apply to municipal advisor affiliates. It is common for large financial institutions to have operations spread across the globe with many affiliates performing various business activities. Even with the Revised Draft Rule G-42 limiting this prohibition to transactions "directly related" to the same municipal securities transactions or municipal financial products to which the municipal advisor is providing advice, a municipal advisor and its affiliates would be required to create a costly, ongoing infrastructure across entities to identify all municipal entities and possibly prohibited transactions.

III. Disclosure Requirements

Revised Draft Rule G-42(b)(i)(B) would require a municipal advisor to disclose to a client in writing all material conflicts of interest, including any affiliate of the advisor that provides "any advice, service, or product to or on behalf of the client that is directly or indirectly related to the municipal advisory activities to be performed by the disclosing municipal advisor." Extending the disclosure requirement to "any advice, service, or product" that is indirectly related to the municipal advisory services creates a requirement that is so broad as to be vague, and would create significant uncertainty that will make compliance exceedingly difficult. Moreover, although the members recognize that the MSRB revised paragraph (b)(i)(G) of Revised Draft Rule G-42 to eliminate the requirement that municipal advisors provide information about "any other engagements or relationships" of any affiliate that might impair the advisor's ability to provide unbiased and competent advice to or on behalf of an obligated person client or to fulfill its fiduciary duty to a municipal entity client, the broadly drafted requirement of paragraph (b)(i)(G) limits the efficacy of the MSRB's revision.

FSR's members further believe that the proposed requirement in Revised Draft Rule G-42(b)(ii) to provide written disclosure of legal or disciplinary events that are material to a client's evaluation of the municipal advisor or the integrity of its management or personnel, and in Revised Draft Rule G-42(c)(iii) to describe the type of information regarding legal events and disciplinary history provided on Forms MA and MA-I is redundant in light of the same disclosures already required to be made by advisors on those forms. The members recommend that municipal advisors not be required to provide separate disclosure of legal or disciplinary events to clients, or proposed clients, if such disclosure is already available publicly, and that these disclosure requirements be deemed satisfied if an advisor provides information about where clients may access electronically the advisor's most recent Forms MA and MA-I, along with the date of the last material amendment to any legal or disciplinary event disclosure on such forms.

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FSR appreciates the opportunity to submit comments on the MSRB's request for comments on Draft Rule G-42. If it would be helpful to discuss FSR's specific comments or general views on this issue, please contact Richard.Foster@FSRoundtable.org.

Sincerely yours,

Richard Foster
Vice President and Senior Counsel for Regulatory and Legal Affairs
Financial Services Roundtable

With a copy to:

Municipal Securities Rulemaking Board
Lynette Kelly, Executive Director
Gary Goldsholle, General Counsel
Michael Post, Deputy General Counsel
Kathleen Miles, Associate General Counsel

Securities and Exchange Commission
John Cross, Director of the Office of Municipal Securities

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COMMISSIONER OF AGRICULTURE

August 22, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: Revised Draft MSRB Rule G-42

Dear Mr. Smith:

This letter is in response to the request for comments on Revised Draft MSRB Rule G-42. Section (c) of the draft rule requires documentation of the municipal advisory relationship and sets forth specific information that must be included in the writing. However, the draft rule lacks any requirement that the writing be a contract or that the municipal advisor obtain an acknowledgment from the government entity/issuer that it is aware of and in agreement with the terms governing the municipal advisory relationship.

The GFOA "Best Practice" for selecting and managing a municipal advisor calls for issuers to enter into a written contract with municipal advisors to define the scope of services and the method of compensation. ***To ensure that issuers are aware of and agree to the scope of services and method of compensation, the draft rule should require municipal advisors to enter into a written contract with the issuer that contains the required terms.*** Alternatively, the rule should, at a minimum, require the municipal advisor to obtain an acknowledgment from the issuer that it agrees with the terms of the engagement and method of compensation. Such a requirement would be consistent with best practices and encourage a dialogue between the municipal advisor and issuer about the terms of the relationship rather than an obligation for the municipal advisor to "paper the file".

Thank you for your consideration.

Very truly yours,

J. Ben Watkins III

Government Finance Officers Association
1301 Pennsylvania Avenue, NW Suite 309
Washington, DC 20004
(202) 393-8020

September 2, 2014

Mr. Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Draft MSRB Rule G-42 – Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

Thank you for the opportunity to comment on the important topic of the Municipal Securities Rulemaking Board's (MSRB) revised draft Rule G-42, pertaining to the duties of non-solicitor municipal advisors (MAs). The MSRB's development of regulations related to the SEC's final Municipal Advisor Rule is of great interest to many of our members, as issuers will be affected by the proposed regulatory framework for these professionals, particularly with regard to fiduciary duty.

Members of the Government Finance Officers Association's (GFOA) Governmental Debt Management Committee helped develop these comments, and remain concerned about the fiduciary responsibilities of MAs as discussed in the draft Rule, as well as the roles that MAs should serve as defined and referred to throughout the Rule.

Below are our comments on the specific provisions in the proposed Rule that relate to our members.

Principal Transactions

The GFOA maintains that the section of the proposed Rule on principal transactions is one of the most important parts of the draft rulemaking, and very much appreciates the MSRB's inclusion in the updated draft of a definition of the term *engaging in a principal transaction* to be limited to the transaction for which the MA is providing advice.

Municipal Advisor/Issuer Relationship and Scope of Work

We are also very appreciative of the MSRB's consideration of suggestions included in our March 13, 2014 comment letter on the MSRB's initial draft of this Rule, in which we advocated for enabling issuers to set the standard for their scope of work and control of engagement with their MAs, rather than the MSRB dictating the terms of these arrangements and establishing specific criteria for the type of work an MA should provide. This modification will allow issuers greater flexibility in defining the parameters of engagements with MAs based on the needs of the issuer, rather than having to rely on prescriptive one-size-fits-all criteria set by the MSRB. We are also appreciative of language included in the revised draft with respect to documenting a municipal advisory relationship. While there may not always be a need for a specific contract, and the draft Rule does not prohibit an issuer from requiring a contract, the terms of the relationship with a MA do need to be defined and documented as soon as engagement with an issuer begins. Note that we advise in the GFOA Best Practice *Selecting and Managing Municipal Advisors* that "*Issuers should have a written contract for municipal advisory services that should detail the scope of services and basis for compensation*."

Recommendations to Clients/Suitability and Duties

We support the proposed Rule's standards for suitability, duty of care, duty of loyalty and know your client. These should be maintained in subsequent revisions of the Rule. However we do note that the revised draft Rule deleted language that instructed MAs to only recommend municipal securities transactions and financial products that are in the issuers' best interest. While the duty of loyalty still requires a MA to act in a municipal entity client's best interests, we would like to see this express language in the context of recommendations reinserted in the Rule. We note that the draft Rule now does not even require that a MA's own recommendation be suitable for its client, which represents a substantial weakening of the Rule.

Prohibited Activities/Conflicts of Interest

As we noted above regarding principal transactions, we appreciate the MSRB providing a definition of the term *engaging in a principal transaction* and clarity on when a firm may serve as an MA and also be party to other transactions with a municipal entity – the clarification being that the conflict of interest would only arise if it is related to the same transaction where the MA is providing advice. We also support the need for MAs to disclose conflicts of interest, including disclosure of any finder's fees, fee splitting, payments to consultants, or other contractual arrangements of the firm that could present a real or perceived conflict of interest. In this area, we note that the previous draft of this Rule stated that the MA must disclose to the issuer any conflicts of interest and other information at the inception of the MA relationship. However, the revised draft states that it must be done upon or prior to engaging in MA activities. We would like to see this section clarified in any forthcoming revisions of this proposed Rule, to define exactly what point in the path to issuer/MA engagement conflicts of interest must be disclosed. GFOA's preference would be for MAs to disclose all conflicts of interest to issuers in writing prior to engaging in MA activities on the issuers behalf.

Additionally, while the revised draft clearly defines what is and what is not a principal transaction, the GFOA also wants to ensure that no component of a final Rule on G-42 removes the authority of issuers to decide for themselves how they utilize a MA or underwriter on a transaction so long as compliance with MSRB Rule G-23, MSRB Rule G-42 and the SEC's Municipal Advisor Rule are maintained. As we indicate in the GFOA Best Practice *Selecting and Managing Municipal Advisors*, *"Due to potential conflicts of interest, the issuer also should enact a policy regarding whether, and under what circumstances, it would permit a firm to serve as an underwriter on one transaction and a municipal advisor on another transaction."* The draft Rule in supplementary section .07 refers to the way Rule G-42 will work with other rules, including Rule G-23. To avoid any confusion or conflict between Rules G-42 and G-23, we would suggest that this section specifically state that a professional does not Violate Rule G-42 when meeting specific standards set forth in Rule G-23. These would be for work related to three types of transactions – pools, remarketing and purchasing bonds for clients.

MSRB Fees Imposed on MAs

We request that the MSRB include similar language in the Rule that is in place for bond dealers that prohibits fees from being passed through to issuers.

Inadvertent Advice

This new section added to the revised Rule is very important to the market. However, we would appreciate additional clarification and some examples of instances in which inadvertent advice might given and how the forthcoming MSRB MA Rules and current broker/dealer rules would apply in these instances.

Investment of Bond Proceeds

Some of our members continue to request clarification on the regulation of advice from brokers to issuers related to the investment of bond proceeds. This draft, as does the original, appears to prohibit

broker/dealers from selling securities to issuers after having advised them to invest their bond proceeds in those investments. The GFOA suggests that SEC and MSRB work together to carefully craft a solution that adheres to the spirit of the MA Rule but also does not create significant disruption in current business practices.

Rule Parity

Finally, GFOA would like to reiterate our contention that all MSRB rulemaking for issuers that is similar to current rules for broker/dealers should, where possible, be congruent.

Thank you for re-proposing this rule and again for the opportunity to comment on this important rulemaking.

Sincerely,

Dustin McDonald
Director, Federal Liaison Center

1401 H Street, NW, Washington, DC 20005-2148, USA
202/326-5800 www.ici.org

August 19, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

Re: MSRB Notice 2014-12 Relating to
Standards of Conduct for Municipal Advisors

Dear Mr. Smith:

The Investment Company Institute[1] appreciates the opportunity to provide comments to the Municipal Securities Rulemaking Board (MSRB) on the revised version of proposed Rule G-42, which would govern standards of conduct for non-solicitor municipal advisors.[2] According to the Notice, the MSRB has made significant modifications to the proposed rule since it was first published for comment in January 2014 and is now seeking additional comment on these modifications. As with our previous comment letter,[3] we support the rule's adoption and again commend the MSRB for pursuing adoption of this rule in order to establish standards of conduct for municipal advisors. Notwithstanding our support, we recommend that the MSRB consider making additional revisions to the rule to better address its application to persons who qualify as municipal advisors as a result of the advice they render

[1] The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $17.3 trillion and serve more than 90 million shareholders.

[2] *See Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors,* MSRB Notice No. 2014-12 (July 23, 2014) ("Notice"), which is available at: http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-12.ashx?n=1. Consistent with the scope of the proposed rule, as used in this letter the term "municipal advisor" or "advisor" refers to a "non-solicitor municipal advisor."

[3] *See* Letter from the undersigned to Ronald W. Smith, Corporate Secretary, MSRB, dated March 4, 2014, commenting on MSRB Notice 2014-01 ("ICI's March Letter").

to 529 college savings plans.[4] We also again recommend that the MSRB clarify that the rule only shall apply prospectively. Each of our recommendations is discussed below.

I. THE INSTITUTE'S COMMENTS ON THE PREVIOUS VERSION OF RULE G-42

ICI's March Letter generally supported the proposed rule, but expressed concern regarding the impact of certain of the rule's provisions on municipal advisors that provide advice to states' 529 college savings plans. We are pleased that, in response to such comments, the MSRB has: deleted the provision in Supplementary Material .02 that would have required a municipal advisor to investigate and consider alternatives to the advisor's advice; deleted the provision in proposed Rule G-42(b) that would have required advisors to disclose their insurance coverage; revised the provision in proposed Rule G-42(c) relating to updating disclosures provided to the client to only require such updates in the event of material changes to information; and deleted the provision in proposed Rule G-42(d) that would have required an advisor to recommend only a municipal financial product that is "in the client's best interest."

As discussed below, the Institute continues to be concerned about the following provisions that were in the original proposal and that remain in the revised rule. We previously commented on each of these: the provision in Supplementary Material .01 that would require an advisor to undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information; the provision in Supplementary Material .08[5] that would require municipal advisors to make specified disclosures relating to a conflict of interest to "investors;" and the provision in Supplementary Material .09[6] that lists the factors that must form the basis for a municipal advisor's recommendation to a municipal entity.

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[4] Supplementary Material .12 to the proposed rule expressly affirms that the rule applies to municipal advisors to sponsors or trustees of college savings plans and other municipal fund securities. In light of this and as discussed in more detail in this letter, we believe additional revisions or clarification are needed to better understand how the rule will apply in the context of advice provided to a municipal entity relating to a state's 529 college savings plan.

[5] In the revised version of the rule, Supplementary Material .07 has been renumbered as .08.

[6] In the revised version of the rule, Supplementary Material .08 has been renumbered as .09.

II. THE INSTITUTE'S CONTINUING CONCERNS WITH PROPOSED RULE G-42 AS APPLIED TO 529 PLANS

A. Supplementary Material .01, Duty of Care

Rule G-42(a) would define a municipal advisor's standard of conduct to include a duty of care. According to Supplementary Material .01, this duty of care would require, in part, an advisor to "undertake a reasonable investigation to determine that it is not basing any recommendation [made to the municipal client] on materially inaccurate or incomplete information." As noted above, ICI's March Letter objected to the MSRB prohibiting a municipal advisor from being able, without undertaking an investigation, to rely on information provided to it by its municipal entity client. In response to this concern, the MSRB's current Notice merely states, "[t]he Revised Draft Rule does not provide an exception for information that is provided to the advisor by the client."[7] With respect to 529 plans specifically, the Notice continues: "In addition, the MSRB believes that in some circumstances the information may be provided to the advisor by the client in connection with the preparation of the official statement. . . . The MSRB believes at this juncture that the provisions of the Revised Draft Rule are appropriate and does not believe that advisors to 529 plans should be relieved from an obligation to inquire as to material provided by it to its client or other parties in connection with the preparation of an official statement."[8]

We continue to have serious concerns regarding the investigation required by Supplementary Material .01. While Rule G-42(d) would require a municipal advisor making a recommendation to a client to ensure that the recommendation is suitable for the client, the investigation required by Supplementary Material .01 would go far beyond that, and require a municipal adviser to actively investigate the veracity of information provided to it by a client prior to making a recommendation to the client. As discussed below, such requirement is both impractical and inconsistent with the rule's intent. Moreover, we are aware of no other financial professionals registered under the Federal securities laws that are required by law to investigate the veracity of information provided to them by a client prior to making a recommendation to the client.

In our view, an advisor should be able to rely on information provided to it by its state partner. We remain concerned that, in its current form, this provision imposes upon municipal advisors, alone among financial professionals, a duty to investigate information that may be wholly within the client's

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[7] Notice at p. 17.

[8] Notice at pp. 17-18. As discussed below, we are concerned that this discussion in the Notice appears to confuse information provided by a municipal client to an advisor in connection with rendering advice with information provided by the client to the advisor for purposes of preparing the client's official statement.

control. In particular, as discussed in ICI's March Letter, this requirement presumes that a municipal advisor will have access to the information it needs to assess the veracity and completeness of information provided by the client. We respectfully submit that this may not be the case. Indeed, much of the information necessary to confirm the accuracy and completeness of information provided by the client and relied upon by the municipal advisor may be non-pubic information in the client's possession that is not available to the advisor.[9] We question how an advisor can complete the required investigation if it is unable to obtain the information necessary to assess the accuracy or completeness of information provided by its client.

This requirement also appears to be inconsistent with the rule's overarching principle "that the [municipal] client should be empowered to determine the scope of services and control the engagement with the municipal advisor."[10] We concur with the MSRB's interest in empowering the municipal client. Such empowerment, however, comes with responsibility and, in our view, this responsibility should include the client dealing fairly and honestly with the municipal advisor and the advisor, in turn, being able to rely on the information provided to it by the client. We therefore do not support including in the rule a provision that imposes upon the advisor a burden to uncover any false or misleading information provided by the client.[11]

In addition to our concerns with duty imposed on advisors by Supplementary Material .01, we are troubled by the Notice confusing the type of investigation required by Supplementary Material .01 with the type of investigation that occurs to verify information prior to including it in an official statement. In our view, these are very different activities. Our comments and concerns with Supplementary Material .01 go to the former. With respect to the latter, we understand that, prior to publishing any information in an official statement, prospectus, or other public document, much vetting and due diligence occurs – beyond statements made by the issuer or its representatives – to ensure that investors are provided accurate, full, and fair disclosure of material information. As such,

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[9] For example, in the context of a 529 college savings plan, assume the state will administer the plan but is working with the municipal advisor to design the plan and such design needs to ensure that the plan generates sufficient revenues to cover the state's costs of administration. If, in working with the municipal advisor, the state provides the advisor information regarding the total costs that must be covered by the revenues generated by the plan, the advisor would likely not have access to the non-public information that would be necessary to verify the information provided by the client regarding the total amount or component parts of such costs. We question, therefore, how the MSRB would expect the advisor to determine the accuracy or completeness of the information the state client provides to the municipal advisor.

[10] Notice at p. 7.

[11] For example, consider a hypothetical situation in which a municipal entity seeks advice from an advisor and, in doing so, deliberately lies to the advisor or provides the advisor with information the client knows to be false. Under the proposed rule, it is the advisor's obligation to determine the false nature of the information and, if it does not, it is the *advisor* who has violated the rule both by relying on the inaccurate information and failing to discern its accuracy. This seems patently unfair.

the role of an advisor that has been retained to provide advice to a municipal client should not be confused with the role of an advisor that has been retained to assist the municipality in preparing and producing an official statement. Accordingly, we encourage the MSRB not to presume that an advisor that has been retained to provide advice to a municipal entity regarding a 529 plan will also have any role in preparing, drafting, and vetting the plan's official statement as this may not, in fact, be the case.

For all of the above reasons, we again strongly recommend that the MSRB reconsider its decision to impose through Supplementary Material .01 a duty on municipal advisors to investigate information provided by the advisor's municipal client. If Supplementary Material .01 is not revised as we recommend, we request that the MSRB provide guidance regarding how a municipal advisor is to conduct an investigation when the information that would be necessary to verify the accuracy and completeness of the information provided by the municipal client is wholly within the client's control and unavailable to the advisor.

B. Supplementary Material .08, Disclosure of Conflicts of Interest

Supplementary Material .08 provides additional guidance regarding an advisor's disclosure obligations under Rule G-42(b), which requires disclosures of conflicts of interest and other information. Among other things, Supplementary Material .08 would require a municipal advisor to "provide written disclosure to investors" of certain affiliations that must be disclosed pursuant to the rule.

ICI's March Letter opposed advisors to 529 plans being required to provide disclosures "to investors" regarding the advisor's affiliations. The Notice includes two responses to the Institute's recommendation that this requirement be deleted: (1) this disclosure requirement "would be satisfied if the advisor's affiliate were to provide written disclosure of the affiliation to investors" and (2) the MSRB believes such disclosure is warranted "because advisors to 529 plans may have material conflicts of interest including those that may arise in connection with affiliates of an advisor that may be registered investment companies that are included in one or more of the investment options in the 529 plan to or on behalf of which the advisor is providing advice."[12]

We respectfully submit that neither response addresses our concerns with this requirement. Our concerns are two-fold: (1) it seems wholly inappropriate to require the advisor to a municipal entity to make disclosures to persons investing in securities issued by that entity; and (2) this requirement is premised on the advisor to a 529 plan having access to the names and contact information for the plan's investors.

[12] Notice at p. 18.

With respect to our first concern, the Institute fully understands the importance of Rule G-42(b) requiring a municipal advisor to make specified written disclosures to the municipal client (*i.e.,* the 529 plan) relating to the advisor's conflicts of interest, including information on any affiliates of the advisor that provide any advice, service, or product to, or on behalf of, the municipal entity. We support this requirement because such disclosures are necessary for the municipal client to be able to assess the advisor's conflicts of interest and determine whether they might inappropriately or improperly impact the municipal entity's relationship with the advisor. We fail to understand, however – and the Notice fails to explain – why such information is relevant to a person *investing* in 529 plan securities. Indeed, if all material terms and conditions of the 529 plan offering already are disclosed in the offering document that is provided to investors and potential investors, this supplemental disclosure would not provide any additional protection to investors.[13]

We expect that the municipal entity entering into a contract with the advisor already has determined that any conflicts of interest presented by the advisor's affiliates do not impair the ability of the advisor to render impartial advice to the municipal entity. This being the case, we question why the MSRB believes that *investors in the plan* need to be able to assess independently the conflicts that the municipal advisor has already considered and resolved or addressed. We also question what the MSRB expects an investor to do with this information since, aside from deciding not to purchase a particular's state's 529 plan, the investor lacks any ability to influence the plan's structure or alter the services provided to the plan by the advisor's affiliates. For all of these reasons, such disclosure seems both unnecessary and of questionable value to investors.[14]

With respect to our second concern, the Notice fails to explain how an advisor to a municipal entity is expected to know the identities of and contact information for investors in a state's 529 plan so that the advisor can provide the required disclosure to such investors. As explained in ICI's March

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[13] We note that the disclosure principles of the College Savings Plan Network have long recommended that the official statement for a 529 plan include: the name of any private program manager or investment manager; the identity of the State administrator and, if applicable, of principal private contractors with direct investment management or program management experience and the current expiration date of any such contracts; and the identity of any trustee for or custodian of account assets. *See College Savings Plan Network Disclosure Principles No. 5* (Adopted May 3, 2011) at Items 3.A., 3.B., and 3.J. Item 2 of the *Principles* recommends that "State issuers should provide interim supplements to the Offering Materials as deemed necessary by the State Issuer in order to prevent the Offering Materials from containing an untrue statement of material fact or omitting to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." We believe the disclosure provided to a plan's investors amply addresses the MSRB's concerns.

[14] While it is very common for states to retain affiliates of a municipal advisor to the states' 529 plans to provide services to their plans, we are not aware of instances – and the MSRB provides no examples of such instances – where these affiliated relationships have adversely impacted 529 plan investors. The efficiencies resulting from these affiliated relationships benefit investors, which is why the states often utilize a municipal advisor's affiliates in their 529 college savings plans.

Letter, because of the structure of 529 plans and Federal and state restrictions on the ability of financial institutions to share their customers' non-public personal information, a municipal advisor likely has no access to information about the plan's investors or how to contact them. Also, as we previously noted, even if the advisor could obtain such information and contact investors in the plan, such investors would likely be confused by such disclosure, as they may have no relationship with the advisor and question why the information is being provided to them. While we appreciate the MSRB permitting such disclosure to be provided in the plan's official statement, this accommodation fails to recognize that the advisor may have no involvement in or influence or control over the contents of the official statement used by the plan or its underwriter so it would be unable to require the plan or its underwriter to include the required disclosure in such document.

Accordingly, we strongly recommend that the MSRB either delete Supplementary Material .08 in its entirety or clarify that its disclosure and delivery requirements do not apply to advisors that provide advice to 529 plans. If the MSRB determines to retain this Supplementary Material in its current form, we recommend that the MSRB better explain why this information is necessary for investors and also provide guidance regarding how municipal advisors that lack access to information regarding the plan's investors are to provide such disclosures to such investors if the plan's official statement does not include the required disclosure.

C. Supplementary Material .09, Suitability

Rule G-42(d) imposes a suitability standard on the advice rendered by a municipal advisor to its municipal entity client. Supplementary Material .09 lists the factors on which this determination must be based as follows:

> . . . the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued in the municipal securities transaction are reasonably expected to be outstanding and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry.[15]

[15] The suitability factors listed in Supplementary Material .09 are substantially similar to those listed in FINRA Rule 2111(a). FINRA Rule 2111(a) prohibits a FINRA member from recommending a transaction or an investment strategy to a customer unless the member determines the recommendation is suitable based on the customer's investment profile, which includes the customer's "age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose to the member . . .." Importantly, however, unlike the MSRB's proposal, subsection (b) of FINRA's rule tailors the rule's application to "an institutional account." Also, it bears noting that FINRA's rule does not require a broker-dealer to verify

We continue to have concerns with the application of Supplementary Material .09 to 529 plans. We note that this provision remains unchanged from its previous version and the MSRB's Notice contains no mention or discussion of the concerns with it that were raised in ICI's March Letter.

While factors such as the municipal client's tax status,[16] risk tolerance, liquidity needs, and financial capacity to withstand changes in market conditions during the term of the offering may be relevant to advice rendered in connection with a bond offering, they would appear largely irrelevant in the context of rendering advice to a 529 plan. Similarly, the client's "financial situation and needs" would also appear to be largely irrelevant in the 529 plan context as these plans are not designed and sponsored to satisfy the client's financial situation and needs, but rather to implement a statutory program that enables retail investors to save for higher education.

Imposing this requirement on municipal advisors without regard to the product they are advising a client on – *i.e.,* a traditional bond as compared to a 529 plan – overlooks fundamental differences in these products and the advice related to them. Indeed, 529 plans are quite different from bond offerings. For example, 529 offerings are not discrete offerings with a limited number of bonds offered to the public for a limited period of time; they are unlimited ("evergreen") offerings with no predetermined duration. Also, unlike bond offerings, 529 plan offerings are not dependent upon external sources of revenue or funding in order to satisfy the claims of investors. The value of an investor's interest in a 529 plan is not negotiated between the buyer and seller and the price of 529 shares do not fluctuate intraday based on such negotiations. Instead, proceeds from the sale of 529 plan interests are pooled and invested in securities consistent with the plan's investment objectives and limitations. On each business day, after the plan's expenses and fees are deducted from the plan's assets under management, the net asset value ("NAV") of the plan is determined. This NAV determines the price that is paid to an investor redeeming an interest in the plan or purchasing an interest in the plan on that day. The calculated NAV is applied to all investors' transaction that are processed effective that day. Also, unlike bonds, which are issued to raise revenue for specific public works projects or activities, 529 plans are created by states to provide an investment vehicle to assist families in saving for qualified higher education.

We believe the differences between advice rendered in connection with municipal securities and that rendered in connection with 529 plans should be recognized in Supplementary Material .09. Because it is not, we again recommend that the MSRB address our concerns by either affirming that the

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the accuracy or completeness of the information the investor provides to the broker-dealer for purposes of determining the suitability of the broker-dealer's recommendations.

[16] We question the inclusion of a municipal client's "tax status" since we presume all government clients would be exempt from any state or federal taxes.

suitability factors listed in Supplementary Material .09 do not apply to advice relating to such plans or clarifying how the MSRB intends the listed factors to apply to such plans in light of their unique structure vis-à-vis bonds and our concerns.[17]

III. PROSPECTIVE APPLICATION OF RULE G-42

Finally, we note that the Notice is silent regarding a proposed compliance date for the revisions to Rule G-42. We again recommend that the MSRB clarify that, once adopted, Rule G-42 will only apply prospectively. As such, a municipal advisor will only be required to comply with the relevant requirements of Rule G-42 when it either enters into a new advisory relationship with a municipal client or when it recommends a new municipal securities transaction or municipal financial product to an existing municipal client. With respect to 529 plans, due to the nature of the advisor's relationship with the plan and the duration of existing 529 plan contracts, this clarification is particularly important in order to avoid disrupting existing relationships and contracts.

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We appreciate the opportunity to provide these comments and your consideration of them. If you have any questions, please contact the undersigned at (202)326-5825.

Sincerely,
/s/
Tamara K. Salmon
Senior Associate Counsel

[17] Alternatively, the MSRB could address our concerns by revising Supplementary Material .09 to read, in relevant part "... must be based on the following factors to the extent applicable to the nature of the advisory relationship or to the product or service being recommended to the advisory client: the client's financial situation and needs, ..." [Underscoring indicates the language we recommend be added to this provision.}

LEWIS YOUNG
ROBERTSON & BURNINGHAM, INC.
AN INDEPENDENT MUNICIPAL FINANCIAL ADVISORY
AND CONSULTING FIRM

August 25, 2014

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314
Via electronic delivery to: http://www.msrb.org/CommentForm.aspx

Re: MSRB Notice 2014-12, Request for Comment on Revised Draft MSRB Rule G-42

Ladies and Gentlemen:

Lewis Young Robertson & Burningham ("LYRB") is pleased to submit comments on the above-referenced Notice.

LYRB is an independent financial advisory firm which has elected, since its inception 18 years ago, to be regulated as a broker dealer and, therefore, has been and remains subject to MSRB regulations. We are now also registered as a municipal advisor with the Securities and Exchange Commission and the MSRB pursuant to Rule 15Ba1-2 of the Commission.

LYRB does not underwrite or purchase securities for our own account or for sale to others nor do we carry customer accounts of any kind. We do not participate as a co-manager or member of selling groups and do not act as a remarketing agent. We are a major financial advisor in the State of Utah and work in some other states as well. LYRB has acted as a financial advisor on hundreds of transactions with a volume of over $7 billion. These transactions run the gamut from small to large, and include general obligation bonds, various types of revenue and tax backed bonds, revenue and bond anticipation notes, and taxable and tax-exempt (including Build America Bonds) bonds in both fixed rate and variable rate structures.

The Revised Draft of Proposed Rule G-42 ("Revised Draft") generally covers the subject matter of Proposed Rule G-36, which was later withdrawn. We commented on that proposal in a letter to you dated April 11, 2011. We commented on the originally distributed Draft Rule G-42 in a letter to you dated March 3, 2014. While the Revised Draft represents an improvement in numerous respects over the original Proposed Rule G-42, we nevertheless have several comments and concerns.

Comments on Proposed G-42(b)

In section (b)(i)(G) we suggest replacing the word "might" with "would". Many times we will have arrangements with entities which we do not expect will create conflicts, but which could create a conflict if circumstances we do not expect to occur in fact arise at a later point. It would be impossible to address all such hypothetical contingencies in advance without overly elaborate (and likely confusing, to less sophisticated clients) disclosures.

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Comments on Proposed G-42(c)

The addition of new clause (c)(vii)creates a potential unintended consequence. We surmise the addition of this clause was to cover instances in which a municipal advisor advising a municipal entity needs to withdraw for some reason (e.g. an unresolveable conflict which arose in the midst of an ongoing project), but must supply ongoing services until a suitable replacement can be selected, similar to rules governing lawyers. This seems fine. However, we believe that some broker dealers who also act as municipal advisors can and will use this rule to escape the consequences of Rule G-23 as recently amended. If a municipal advisor has a term contract covering all debt of an issue for say, the next 5 years, and includes a withdrawal provision in their contract pursuant to clause (c)(vii), which in effect says "we can withdraw for any individual bond issue so long as we have not begun to give you 'advice' on that issue yet, and act as an underwriter", then the engagement for "all issues" ceases to become a barrier to that dealer's trading on its fiduciary relationship to "shift" roles and act as an underwriter. This is, in general, what the recent amendments to Rule G-23 were designed to prevent. While navigating the many potential issues such a course might have for an MA/underwriter might prove difficult or even problematic for them, we are sure there will be those who will try this and claim cover for doing so based on this rule. We suggest (c)(vii) be modified or withdrawn altogether.

Comments on Proposed G-42(e)

This rule is unnecessary, as it is covered by Proposed G-42(a) and is a basic part of a generally engaged financial advisor's work. If you must approach it this way, we suggest that Proposed 42(e) may be better referenced in the Supplementary Material, so as not to detract from the breadth of the basic rule.

More specifically, we comment on new (e)(ii). Your principal transaction prohibition has gone from too broad to too narrow. A bank operating under this rule could claim that it is not prohibited from *both* giving "fiduciary" advice, putting the client's interests ahead of its own, and for its own (or an affiliate's) account, making a loan to a municipal entity in the form of a privately placed bond sale. For state law purposes, such a loan would typically take the form of a bond or a note, but may not be a "security" for federal law purposes. Usually, such a loan is considered in juxtaposition to issuance of publicly offered securities for the same purpose and is an *integral part* of what the advisor discussed with its municipal client. Making such a loan is incompatible with the bank's fiduciary obligation as a municipal advisor. If allowing bankers to do this is your intention, we believe it violates the mandate of the Dodd-Frank Act that a fiduciary standard apply to municipal advisors as there is no difference between a loan and a security from the borrower's perspective, when the borrower is relying on a fiduciary for advice. No court would agree that principal transactions with a client which are the subject of fiduciary advice owed that client can be done as a fiduciary without a conflict of interest, as buyer and seller *always* have competing interests and it is impossible to set those aside to fill the fiduciary duty. Your rule should be consistent with this concept.

One final thought which we provided in our earlier comments, but which has not, as yet, been addressed in the Proposed Rule: an orderly transition provision or phased effective date is necessary. While we see no issues with providing financial advisory agreements to our clients

for new engagements on and after the effective date of the Proposed Rule G-42 that meet the requirements of paragraph (c), we believe that the Rule should include a transitional provision that recognized that financial advisory agreements are binding bilateral contracts and explicitly confirms that existing agreements are not required to be amended until they expire in accordance with their terms. Such a transitional provision could include a requirement that a municipal advisor with financial advisory agreements in existence as of the effective date of the Rule provide, as supplemental disclosures to its clients, the information required by paragraph (c)(ii), (iii) and (iv) of Proposed Rule G-42. At a minimum, we believe that the Board should recognize that many Financial Advisory engagements are longer-term arrangements and advisors should be provided with a reasonable opportunity to conform existing agreements to the requirements of Proposed Rule G-42 when they are renewed or after a reasonable phase-in period after Rule G-42 is approved by the SEC. The approval of amendments to an existing financial advisory agreement as well as the approval of a new financial advisory agreement frequently involves extended internal review processes by municipal entities as well as governing body approval. The timing for a municipal entity's review and approval process is, of course, outside of the control of a municipal advisor and accordingly, an advisor should be held to a commercially reasonable efforts standard in this regard as opposed to a mandated deadline, particularly with regard to existing financial advisory agreements.

Lewis Young Robertson & Burningham, Inc.

By: Laura D Lewis

Principal

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August 25, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: MSRB Notice 2014-12

The National Association of Independent Public Finance Advisors ("NAIPFA") appreciates this opportunity to provide comments in connection with Municipal Securities Rulemaking Board ("MSRB") Notice 2014-12 – Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors (the "Revised Notice").

Comments

The Revised Notice and the proposed version of MSRB Rule G-42 set forth therein (the "Rule") are significantly more aligned with the needs of Municipal Advisors as well as municipal entities and obligated persons than the prior versions of both. We appreciate the MSRB's determinations in this regard. That being said, NAIPFA believes that those portions of the Rule that were no amended in accordance with NAIPFA prior comments still require revision. To that end, NAIPFA has attached the comments we submitted in connection with the prior notice hereto as Exhibit A and incorporate those comments herein. In addition, as described more fully below, we find the inclusion of Supplementary Paragraph .06 (the "Paragraph") both troubling and unwarranted.

NAIPFA does not believe that the Paragraph is appropriate for inclusion within the Rule. The Paragraph and the provisions contained therein are not designed for the benefit municipal entities, obligated persons, the public or Municipal Advisors as a whole. Instead, the Paragraph will benefit, to the detriment of all other market participants, only those Municipal Advisors who are also registered broker-dealers who wish to avoid being prohibited from underwriting an issuance of securities pursuant to MSRB Rule G-23. In other words, except for situations in which a broker-dealer acts as a Municipal Advisor and wishes to serve in another capacity, specifically, as an underwriter, it is unlikely that this provision will be utilized. As such, NAIPFA believes that this exemption, if it is to be created, would be more appropriately fall under MSRB Rule G-23 rather than the Rule.

That being said, this issue has already been vetted by the SEC through its preparation of Release No. 34-70462 (the "Release") and its adoption of Rule 15Ba1-1 ("Rule 15Ba1-1"). If the SEC had intended for there to be an "inadvertent advice" exception it would have included such an exemption within the Release and Rule 15Ba1-1. Illustrative of this are the numerous

exemptions that were created, including: (i) the Public Officials and Employees of Municipal Entities and Obligated Persons Exception; (ii) the Responses to Requests for Proposals or Requests for Qualifications Exception; (iii) the Municipal Entity or Obligated Person Represented by an Independent Municipal Advisor Exemption; (iv) the Broker, Dealer or Municipal Securities Dealer Serving as an Underwriter Exception; (v) the Registered Investment Advisers Exemption; (vi) the Registered Commodity Trading Advisors/Swap Dealers Exemption; (vi) the Accountants, Attorneys, Engineers and Other Professionals Exemptions; and (vii) the Banks Exemption.

The fact that the SEC determined not to create an "inadvertent advice" exception is particularly noteworthy in light of a recent commentary from SIFMA in which it pointed out that President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") into law almost four years ago.[1] Although absent from SIFMA's comments, this nearly four year delay was instigated principally by the broker-dealer community who argued that the MSRB, which had proposed numerous Municipal Advisor rules in 2011, should delay its rulemaking until the SEC adopted a final definition of the term "Municipal Advisor."[2] Importantly, while seeking to delay MSRB rulemaking, which has continued through today, broker-dealer groups have engaged in a comprehensive lobbying campaign utilizing both legislative[3] and regulatory[4] efforts that are designed to weaken the issuer and public protections put in place by the Dodd-Frank Act. All told, broker-dealer groups, and others, had nearly four years with which to have their voices heard on this very topic and in the end the SEC (and Congress) have determined not to grant an "inadvertent advice" exemption. As such, NAIPFA believes that the time has passed for creating additional exemptions from the definition of the term "Municipal Advisor," particularly when such exceptions are likely to lead to a continuation of the abusive practices that were the impetus for the enactment of the Dodd-Frank Act.

Of particular note in this regard are the statements within the SEC's Registration of Municipal Advisors Frequently Asked Questions dated January 10, 2014, as amended. Therein, the SEC states,

> If a broker-dealer acts as a municipal advisor to a municipal entity with respect to an issuance of municipal securities, it owes fiduciary duty to the municipal entity with respect to that issuance and must not take any action inconsistent with its fiduciary duty to the municipal entity. Additionally, the broker-dealer must comply with MSRB Rule G-23,

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[1] Kenneth Bentsen, Jr., "Commentary: Regulation of MAs: Bring it On", *The Bond Buyer* (July 31, 2014).
[2] SIFMA Letter to MSRB, Re: MSRB Notice 2011-28 (June 24, 2011) ("SIFMA Letter"); *See* BDA Letter to MSRB, Re: MSRB Notice 2011-28 (June 24, 2011); SIFMA Letter to MSRB, Re: MSRB Notices 2011-14 and 2011-13 (April 11, 2011); SIFMA Letter to MSRB, Re: MSRB Notice 2011-16 (April 5, 2011); SIMFA Letter to MSRB, Re: MSRB Notice 2011-04 (February 25, 2011).
[3] *See* HR 2827; *See* HR 797.
[4] From June 14, 2011 through September 16, 2013, SIFMA and BDA met with the SEC approximately twelve times specifically regarding the registration requirements for Municipal Advisors, which included the definition of the term "Municipal Advisor" that was ultimately contained within SEC Rule 15Ba1-1.

> which prohibits persons from switching from the role of financial advisor to the role of underwriter with respect to the same issuance of municipal securities.[5]

Here, the SEC's position is unequivocal, when a broker-dealer acts as a municipal advisor it cannot then serve as the underwriter in connection with the same issuance of municipal securities. Similarly, interpretive guidance to MSRB Rule G-23 notes that

> The dealer must not engage in a course of conduct that is inconsistent with an arm's-length relationship with the issuer in connection with such issue of municipal securities or the dealer will be deemed to be a financial advisor with respect to that issue and precluded from underwriting that issue by Rule G-23(d).[6]

MSRB Rule G-23 itself contains no exception for broker-dealers who may "inadvertently" engage in a course of conduct that is inconsistent with an arm's-length relationship with the issuer. Thus, NAIPFA is concerned that the Paragraph will lead to widespread abuses by broker-dealers seeking to circumvent both 15Ba1-1 and MSRB Rule G-23 notwithstanding their obligation to review their policies and procedures.

In light of the foregoing, the Paragraph is inconsistent with both Rule 15Ba1-1 and MSRB Rule G-23 and would have significant detrimental impacts on the interests of municipal entities, obligated persons and the public. Therefore, NAIPFA believes that the Paragraph should be deleted in its entirety.

However, if the MSRB determines to create an exemption from the definition of "Municipal Advisor" that goes beyond what the SEC has determined to create, NAIPFA believes that the Paragraph should be significantly revised so as to ensure the protection of municipal entities, obligated persons and the public. The Paragraph as currently written, gain, notwithstanding the requirement that Municipal Advisors review their policies and procedures, contains protocols that are significantly different, and notably less stringent, than similar MSRB rules, particularly the exemption relative to inadvertent political contributions contained within MSRB Rules G-37(i) and (j) (collectively, "G-37").

As such, NAIPFA respectfully suggest that the Paragraph be amended in a manner that will make it consistent with G-37. Absent further explanation from the MSRB, NAIPFA sees no justification for allowing the Paragraph to create a broader exemption protocol than that which is contained within G-37. This is particularly the case since the abuses that are likely to occur with respect to the provision of "inadvertent" advice are at least as great as those that would arise from the provision of impermissible political contributions. In this regard, NAIPFA recommends that the Paragraph be amended to read as follows:

> Paragraph .06:

[5] Registration of Municipal Advisors, Frequently Asked Questions, Office of Municipal Securities, Question 5.2.
[6] Guidance on the Prohibition on Underwriting Issues of Municipal Securities for which a Financial Advisory Relationship Exists Under Rule G-23 – November 27, 2011.

(i) If a municipal advisor that inadvertently engages in municipal advisory activities for or on behalf of a municipal entity or obligated person and does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship, the municipal advisor is entitled to an automatic exemption, subject to (ii) and (iii) herein, and shall not be required to comply with section (b) and (c) of this rule so long as, as promptly as possible, the advisor provides a document to such municipal entity or obligated person that is dated and includes:

(A) a disclaimer that the advisor did not intend to provide advice and that, effective immediately, it has ceased engaging in municipal advisory activities;

(B) a notification that such municipal entity or obligated person should be aware that the disclosure of material conflicts of interest and other information required by section (b) of this rule has not be provided;

(C) a full identification of all advice that was inadvertently provided by the advisor within 10 business days of the date of the discovery of such advice by the advisor; and

(D) a request that the municipal entity or obligated person acknowledge receipt of such document.

(ii) An advisor is entitled to no more than two automatic exemptions per 12-month period.

(iii) An advisor may not execute more than one exemption relating to inadvertent advice by the same municipal advisor representative regardless of the time period.

(iv) Any exemption beyond those permissible under (ii) and (iii) above shall only be permissible with respect to any advisor upon application to a registered securities association or the appropriate regulatory agency, and such association or agency may exempt, conditionally or unconditionally, an advisor who is otherwise prohibited from discontinuing their municipal advisory relationship with a municipal entity or obligated person. In determining whether to grant such exemption, the registered securities association or appropriate regulatory agency shall consider, among other factors:

(A) whether such exemption is consistent with the public interest, the protection of municipal entities, obligated persons and the public, and the purposes of this rule;

(B) whether such municipal advisor (1) prior to the time of the provision of inadvertent advice was made, had developed and instituted procedures reasonably designed to ensure compliance with this rule; (2) prior to or at the time the inadvertent advice was made, had no actual knowledge that such advice would constitute engaging in municipal advisory activities; (3) has taken all available steps described in (i) of this Paragraph .06; and (4) has taken such other remedial or preventive measures, as may be appropriate under the circumstances, and the nature of such other remedial or preventive

measures directed specifically toward the provider of inadvertent advice and all employees of the advisor;

(C) the timing and amount of the inadvertent advice that resulted in the prohibition;

(D) the nature of the inadvertent advice; and

(E) the advisor's apparent intent or motive in making the inadvertent advice, as evidenced by the facts and circumstances surrounding the provision thereof.

Supportive of the above revisions is the fact that the Paragraph as currently written appears to contain internal inconsistencies. On the one hand, the Paragraph assumes that the individual who has "inadvertently" provided advice is able to identify the fact that they have done so,[7] while on the other hand requiring the individual to merely represent that it "has undertaken reasonable efforts to identify the advice that was inadvertently provided"[8] without requiring such person to actually disclose the extent, or identify the content, of the advice actually provided. Apart from the other comments contained hereinafter, NAIPFA believes that there is no reason why a person utilizing this exemption should not be obligated to clearly identify the advice that was provided inadvertently rather than simply, "in good faith," utilize "reasonable efforts to identify the advice," since it is unlikely that a person will act pursuant to this Paragraph if they have not already identify instances in which advice is given, inadvertently or otherwise.

In addition, appropriate disclosure of inadvertent advice, unlike the disclosure of an impermissible political contribution, must be made in a relatively short period of time following its discovery. As noted in the above revisions to the Paragraph, this disclosure would need to occur within 10 business days of the date of discovery. This short period is necessary with respect to the provision of inadvertent advice due to the likelihood that such advice will be given during the course of an ongoing transaction and the disclosure thereof will need to be made within a sufficient amount of time to allow the municipal entity or obligated person to make an informed decision with respect to how to proceed without causing the transaction to be unduly delayed.

These revisions would also provide flexibility in that Municipal Advisors could either utilize the automatic exemption provisions contained within subsection (i) of the proposed revisions to the Paragraph, or seek an exemption by application to the appropriate registered securities association or regulatory agency. In this regard, these revisions would appropriately balance the needs of Municipal Advisors who may inadvertently provide advice while curtailing the likelihood that persons will abuse this exemption, inadvertently or otherwise, to the detriment of municipal entities, obligated person and the public.

[7] *See* Paragraph .06 ("In the event that a municipal advisor inadvertently engages in municipal advisor activities… and does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship…").
[8] Paragraph .06(C).

Conclusion

In light of the foregoing, NAIPFA urges the MSRB to remove Paragraph .06 from the Supplementary Materials; it will serve no legitimate purpose other than to allow broker-dealers to continue their pre-Dodd Frank Act practices of providing advice to municipal entities and obligated persons as their advisors without obtaining corresponding fiduciary responsibilities and will ultimately allow such advisors to serve as underwriters of the securities being issued. These are precisely the conflict of interest riddled and abusive practices that the Dodd-Frank Act, Rule 15Ba1-1 and MSRB Rule G-23 were designed to prevent.

We acknowledge that some market participants may have difficulty in understanding how to avoid being deemed Municipal Advisors. However, we do not believe that a lack of competence should be an excuse to take advantage of municipal entities, obligated person or the public, inadvertently or otherwise. That being said, since broker-dealers in particular have not previously been regulated with respect to their municipal advisory activities, we understand that they will likely make mistakes in the course of their dealings with municipal entities, and we are sensitive to that. Therefore, although we do not believe it is prudent, as an alternative to eliminating Paragraph .06 in its entirety, we would be amenable to the revision thereof in a manner that is consistent with the foregoing comments.

Notwithstanding the foregoing, we believe that there would be no need to include Paragraph .06 is broker-dealers were required to disclose to a prospective municipal entity client at the earliest possible time what their intentions are with respect to their role in the transaction. In other words, if broker-dealers were required to state at the earliest possible point in their relationship with a municipal entity whether they intended to serve as the municipal entities Municipal Advisor or underwriter, the need for Paragraph .06, or any similar provisions, would be greatly reduced since there would then be no question in the mind of any of the parties as to what role the broker-dealer was playing in the transaction.

Sincerely,

Jeanine Rodgers Caruso, CIPFA
President, National Association of Independent Public Finance Advisors

cc: The Honorable Mary Jo White, Chairman
The Honorable Kara Stein, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Michael Piwowar, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
Lynnette Kelly, Executive Director, Municipal Securities Rulemaking Board

EXHIBIT A

NAIPFA Comments to MSRB Notice 2014-01

(See Attached)

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March 10, 2014

Ronald W. Smith
Corporate Secretary
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1900 Duke Street, Suite 600
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Re: MSRB Notice 2014-01

The National Association of Independent Public Finance Advisors ("NAIPFA") appreciates this opportunity to provide comments in connection with Municipal Securities Rulemaking Board ("MSRB") Notice 2014-01 – Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors (the "Notice").

Introduction

In general, because of the varied nature of the engagements entered into by Municipal Advisors as well as the composition of the firms themselves, NAIPFA believes that a principles-based rule rather than the prescriptive approach taken by the Notice would better serve the municipal market. In addition, the Notice puts in place a series of regulations which will place independent registered Municipal Advisors ("IRMAs")[1] at a significant competitive disadvantage to their broker-dealer counterparts, and will impose undue regulatory burdens upon small Municipal Advisor firms.

We note that it appears from the text of the Notice that the MSRB is focusing primarily on those non-solicitor Municipal Advisors who provide advice with respect to the issuance of municipal securities, rather than those Municipal Advisors who provide services related to the investment of bond proceeds. Therefore, for purposes of these comments, unless otherwise noted, NAIPFA's use of the term "Municipal Advisor" applies solely to persons who fall within the Securities Exchange Act of 1934 and its definition of "Municipal Advisor" because they provide advice with respect to the issuance of municipal securities and often throughout the period in which an issuance is outstanding.

By way of background, Municipal Advisors have served municipal entities and obligated persons for decades, typically referring to themselves as financial advisors. Although a federal fiduciary duty has been imposed upon Municipal Advisors as a result of the passage of the Dodd-Frank Act, NAIPFA member firms have for decades accepted and acted in accordance with a fiduciary duty with respect to their municipal entity clients. Illustrative of this is the fact that NAIPFA's

[1] The term "independent Municipal Advisor" as used herein refers to those Municipal Advisors who are not, and within the past two years have not been, associated with a broker-dealer.

bylaws, even before the enactment of the Dodd-Frank Act required, as a condition of initial and continued membership, that its member firms accept "a fundamental obligation to act solely in the best interests of the public entity and provide financial advice to the public entity that is not conflicted."

In this regard, we have long supported the imposition of fiduciary responsibilities upon Municipal Advisors and will continue to do so. However, NAIPFA cannot support proposed Rule G-42 to the extent that it seeks to, or may seek to, impose obligations that go beyond what is required to ensure that Municipal Advisors adhere to their fiduciary responsibility.

In addition, NAIPFA feels strongly that in terms of our provision of municipal securities issuance-related services, although Municipal Advisors may have things in common with both investment advisers and broker-dealers, the regulation of Municipal Advisors must ultimately reflect the distinctions that exist between underwriters and investment advisors. In many ways, the role of Municipal Advisors is unique and so should the corresponding regulations.

For example, Municipal Advisors have fiduciary duties just as investment advisors. However, unlike investment advisers who generally have standardized fees and scope of services, Municipal Advisors assess fees and undertake engagements that can vary widely from transaction to transaction, and some engagements may not even involve a transaction, *per se*. Similarly, in some ways Municipal Advisors are like underwriters, such as how both may provide advice to municipal entities and obligated persons with respect to matters such as the issuance of securities. However, in many key respects, Municipal Advisors are very different from underwriters. For example, unlike underwriters, Municipal Advisors are fiduciaries, they do not hold, transfer or otherwise handle client funds, and, with respect to IRMAs, generally are of a much smaller size, both in terms of employees and annual revenue. In light of the foregoing, we believe that the regulations should reflect the unique role played by Municipal Advisors. Therefore, any rules proposed and enacted should be borrowed from those of underwriters and investment advisers only when it is appropriate to do so based upon whether such regulation advances the MSRB's interest in ensuring Municipal Advisor adherence to their fiduciary duty.

Standards of Conduct – G-42(a)

Overall, NAIPFA supports the standards of conduct proposed in the Notice. As noted above, NAIPFA and its member firms have long adhered to similar standards. As such, we do not believe that the standards themselves impose an undue regulatory burden. In addition, the proposed standards accurately differentiate the role of Municipal Advisors from that of underwriters and support Municipal Advisors in effectively discharging their fiduciary duties.

Further, NAIPFA would be supportive, notwithstanding the legality of any such measure, of a rule imposing fiduciary duties upon Municipal Advisors with respect to the advice they provide to obligated persons. As with municipal entities, NAIPFA member firms who serve obligated person clients have long accepted and adhered to a fiduciary standard with respect to their

service to such clients. Thus, we do not believe that this would, in and of itself, impose an undue regulatory burden upon Municipal Advisors.

Disclosures of Conflicts of Interest and Other Information – G-42(b)

1. Text of Rule G-42(b)(viii)

> ***G-42(b)*.** A municipal advisor must, at or prior to the inception of a municipal advisory relationship, provide the client with a document making full and fair disclosure of all material conflicts of interest, including disclosure of: ***(viii)*** the amount and scope of coverage of professional liability insurance that the municipal advisor carries (*e.g.*, coverage for errors and omissions, improper judgments, or negligence), deductible amounts, and any material limitations on such coverage, or a statement that the advisor does not carry any such coverage.

2. Comment

NAIPFA believes that an important aspect of supporting to fiduciary duties is requiring that any advice provided be free of material conflicts of interest which may inhibit a Municipal Advisor's ability to provide advice that is in the best interest of the client. In this regard, where a Municipal Advisor has a material conflict of interest, the Advisor should provide disclosures relating to such conflict to its client. Consequently, and as discussed more fully below, we cannot support the disclosure of those matters described within proposed Rule G-42(b)(viii) because the professional liability insurance disclosure requirement noted therein does not relate to any material conflict of interest. Moreover, and as discussed more below, this provision would place IRMAs and small Municipal Advisors at a distinct competitive disadvantage to underwriting firms and broker-dealer Municipal Advisors.

With respect to any disclosure to be mandated, the MSRB should weigh a variety of factors in determining whether a particular disclosure would be appropriate. These factors may include: whether such provision will increase Municipal Advisor adherence to fiduciary duties; the extent to which a particular provision may inhibit competition; and whether any such provision places an undue economic burden upon small Municipal Advisor firms. G-42(b)(viii) fails in all respects and should be eliminated from the MSRB's lists of mandatory disclosures. As discussed more fully below, NAIPFA would welcome a revised provision that states in effect that Municipal Advisors must truthfully disclose, upon request, information related to any professional liability insurance maintained.

NAIPFA does not believe that this disclosure furthers a Municipal Advisor's ability to adhere to its fiduciary duty. It is worth noting for comparative purposes that NAIPFA is unaware of any similar requirement imposed upon investment advisors or attorneys. As fiduciaries, Municipal Advisors must deal honestly with their clients. In addition, unlike all of the other disclosures contained within Rule G-42(b), this disclosure does not relate to any conflict of interest, material or otherwise. A Municipal Advisor's professional liability insurance policy, or lack thereof, neither creates nor eliminates any conflict of interest. However, to the extent that a client desires

to obtain information about a firm's professional liability insurance, that client should be entitled to request such information and expect that any information received will be accurate and complete. Thus, such a requirement would be appropriate in this context.

NAIPFA believes that RuleG-42(b)(viii) as written will curtail competition by, among other things, placing an undue economic burden upon small firms. Further, if firms are mandated to maintain professional liability insurance this burden will only be exacerbated. Large firms, broker-dealer and non-broker-dealer alike, will likely carry more extensive professional liability insurance policies than their smaller counterparts. Mandatory disclosures may cause municipal entities and obligated persons to focus upon this factor in selecting a Municipal Advisor, rather than relying upon the advisor's qualifications. This may, unfortunately, result in many otherwise qualified Municipal Advisors, such as the numerous solo practitioners who have been in the industry for upwards of 30 years, becoming unable to effectively compete against those firms who do possess such insurance.

In addition, because this provision may undermine the selection of potentially more qualified Municipal Advisors solely due to the larger policy limits of a competing firm's professional liability insurance, there could be an increase in litigation as the quality of advice provided declines due to this potential "brain drain;" even mandating professional liability coverage may increase litigation due to the effect that such a mandate would have on forcing otherwise qualified advisors out of the market. In either case, if litigation rates increase so too will the number of firms leaving the market, even further curtailing competition.

This provision may have a particularly significant impact on competition in certain parts of the country. After exploring a professional liability insurance pool and other options available to its members, NAIPFA discovered that there are portions of the country where professional liability insurance specific to Municipal Advisors may not be available. In these states, local Municipal Advisors may be at a significant competitive disadvantage if they are unable to obtain coverage when competing against larger, multistate companies which may be able to obtain insurance in their home state. With respect to small IRMAs, where coverage does exist, the cost can be prohibitive; the market infrastructure and understanding of the industry by insurance companies does not exist at this time in a way that will allow small Municipal Advisor firms to have a level playing field.

In light of the foregoing, and as noted previously, NAIPFA believes that a more appropriate approach to this issue would be to put in place a principles-based rule. Within the context of this provision, NAIPFA believes that it would be appropriate to require Municipal Advisors to truthfully and accurately disclose matters requested by their clients, which could include disclosures relating to the scope and extent of Municipal Advisors professional liability insurance. This would further Municipal Advisor adherence to fiduciary duties by reinforcing the notion that Municipal Advisors owe their municipal entity clients (and potentially obligated person clients) a duty of loyalty. This approach would also support the SEC's goal of placing issuers in control of their debt issuance process, and would ensure that when issuers wish to receive particular disclosures from a Municipal Advisor, that those disclosures are truthful and

accurate and complete. Finally, this approach would negate the negative competitive and economic impacts of the proposed rule.

Documentation of the Municipal Advisory Relationship – G-42(c)

1. Question Regarding The Phrase "Entered Into"

It is unclear from the Notice what the MSRB means by the phrase "entered into" with respect to the writing that a Municipal Advisor must utilize to evidence its engagement. Does this mean that the writing must be a two party agreement? In other words, must the writing be executed by both the Municipal Advisor and its client? NAIPFA respectfully requests clarification in this regard. To the extent that the MSRB intends for this writing to be executed by Municipal Advisors and their clients, NAIPFA hopes that the MSRB will consider the comments set forth below in terms of clarifying this provision.

2. Comments

In reviewing this portion of the Notice, NAIPFA again bases its analysis upon whether these provisions further Municipal Advisor adherence to their fiduciary duties or involve disclosure of material conflicts of interest, and the extent to which such provisions will inhibit competition and place an undue burden upon small Municipal Advisor firms. Overall, NAIPFA believes that the provisions of G-42(c) do not meet these criteria and should be revised accordingly.

In September, 2013, the SEC released its Final Rule on the Registration of Municipal Advisors, which contained a provision that stated, in essence, that a broker-dealers may rely upon the "Underwriter Exemption" if it is engaged by an issuer as its underwriter. In January, 2014, the SEC released its answers to a series of Frequently Asked Questions relating to the Registration of Municipal Advisors. Therein, the SEC explained the manner in which an underwriter can evidence its engagement with a municipal entity or obligated person client for purposes of availing itself of the Underwriter Exemption. In this regard, the SEC stated that a broker-dealer can demonstrate its engagement "either through a writing, such as an engagement letter […] or through other actions."

The features noted by the SEC that must be included within any such engagement letter include:

> (a) the governing body or any duly authorized official of the municipal entity responsible for municipal finance has executed, approved, or acknowledged the engagement letter in writing; (b) the engagement letter clearly related to providing underwriting services; (c) the engagement letter clearly states the role of the broker-dealer in the transaction; (d) the engagement letter relates to a particular issuance of municipal securities that the municipal entity or obligated person anticipates issuing and is not a general engagement for underwriting services that does not relate to any particular transaction; and (e) the engagement letter or a separate writing done at or before the time of the engagement provides all disclosures that are required to be made by underwriters by the time of an engagement under MSRB Rule G-17.

With the exception of (d) above, NAIPFA can find no reason why a parallel series of requirements could not be imposed upon Municipal Advisors with respect to any writing that they may be required to provide to evidence an engagement. With respect to (d) above, NAIPFA believes that because Municipal Advisors often advise on matters that are not "deal" specific, and are often engaged to provide services prior to, during and after a securities issuance, there is no reason to limit their engagement to a particular transaction. Further, unlike underwriters, nothing contained within the SEC's final Municipal Advisor registration rule or the FAQs would limit a Municipal Advisor's ability to enter into a multi-year or multi-transaction engagement. Thus, there is no reason in this instance to impose requirements on Municipal Advisors similar to those contained within (d) above. In addition, clauses (b) and (e) would need to be appropriately tailored to Municipal Advisors.

With respect to G-42(c), the currently proposed requirements do not support Municipal Advisor adherence to fiduciary duties, and G-42(c) imposes more onerous requirements upon Municipal Advisors than the SEC imposes upon broker-dealers wishing to serve as underwriters is counterintuitive. Municipal Advisors are required to act in the best interest of their clients and would breach that duty if they were to put their financial interests before their clients' interests. As a result, and because the SEC believes that it is appropriate for non-fiduciary broker-dealers to make the above-referenced disclosures, there seems to be no basis for imposing more stringent requirements upon Municipal Advisors.

The additional requirements imposed by G-42(c) on Municipal Advisors places them at a significant competitive disadvantage to their underwriting counterparts who are not, for example, required to provide an estimate of their anticipated compensation; underwriters, who have no duty to their clients other than to deal fairly, are able to determine their fee well into the course of a transaction, sometime not until they proffer a formal Bond Purchase Agreement. In addition, underwriters are not mandated to include any particular contract-related terms within their engagement letter, such as clauses relating to the termination of the relationship or their obligations relating to certain aspects of the transaction, whereas Municipal Advisors would be required to include these provisions. Conversely, Municipal Advisors will be required to provide a fee estimate early on in the transaction, well before the full scope of the engagement may be known. These disclosures like the disclosure relating to professional liability insurance will not further adherence to fiduciary duties and will simply result in a greater percentage of issuers choosing their professionals based upon cost rather than quality.

As an alternative to proposed G-42(c), NAIPFA would welcome MSRB efforts to further define the scope of a Municipal Advisor's fiduciary duty. NAIPFA would welcome a rule that states, in effect that, Municipal Advisors would be mandated to provide all of the services corresponding to their fiduciary duties absent a writing limiting the scope of the Municipal Advisor's engagement. With respect to the fee-related disclosures, NAIPFA believes that it would be appropriate to require Municipal Advisors whose compensation is transaction-based to provide a reasonable estimate of the Municipal Advisor's fee to the municipal entity (and potentially obligated person) within a reasonable time after the Advisor has been fully apprised of the scope

and nature of the transactions but in no event later than thirty (30) days prior to the initial estimated date of issuance. This would allow Municipal Advisors to fully assess the scope of their work, the amount of work required to complete the transaction, and the transaction's complexity, and would provide Municipal Advisor clients with an ample opportunity to assess the reasonableness of the Municipal Advisor's estimated fee.

Recommendations – G-42(d)

In general, we support G-42(d) as proposed. We believe that it appropriately reflects Municipal Advisor fiduciary duties. We are, however, concerned with the final portion of this provision, which states, "With respect to a client that is a municipal entity, a municipal advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest."

It is unclear to us how the determination of whether a particular transaction is in a client's best interest will be made. Conversely, in connection with the MSRB's mandate that Municipal Advisor recommendations be suitable, the MSRB provides guidance, such as the statement that the Municipal Advisor must have a "reasonable basis for believing, based on the information obtained through the reasonable diligence of the advisor, that the transaction or product is suitable for the client." In addition, because of the rapid pace at which the municipal market can move, without some criteria upon which the determination of what is in the client's best interest can be made, it seems difficult, if not impossible, to know whether a particular course of action will ultimately result in being what is in the "best interest" of the client.

Therefore, NAIPFA requests that additional guidance be provided that can assist Municipal Advisors in determining whether their recommendation is in the "best interest" of the client. In this regard, NAIPFA believes that a determination of what is in the Municipal Advisor's client's best interest must be based on the facts and circumstances in existence as of the time of the recommendation. We would also request that the MSRB Responses to Webinar Questions numbers 12.1 and 12.2 relating to its February 6 webinar be included in the provisions of the final version of G-42(d).

Review of Recommendations of Other Parties – G-42(e)

As currently written, proposed Rule G-42(e) appears to be inconsistent with SEC Rule 15Ba1-1(d)(3)(vi), the Independent Registered Municipal Advisor Exemption ("IRMA Exemption").

Rule G-42(e) seems to presuppose that a third party is providing advice to a municipal entity or obligated person without themselves being deemed a Municipal Advisor. In other words, such persons are relying upon an exemption from the definition of Municipal Advisor to provide this advice.

The SEC's rationale for creating the IRMA Exemption was that municipal entities would

> have the benefits associated with the regulation of municipal advisors. Such benefits include, but are not limited to, standards of conduct, training, testing for municipal advisors that may be required by the Commission or the MSRB, other requirements unique to municipal advisors that may be imposed by the MSRB, and *fiduciary duty*.[2]

Thus, the SEC's position appears to be that third parties can provide advice to municipal entities because the municipal entities will have the protections afforded to them by their engagement of an IRMA. In fact, the IRMA Exemption specifically requires that the municipal entity or obligated person provide a written representation indicating that they will rely upon the advice they receive from their Municipal Advisor. It seems inconsistent with the IRMA Exemption if G-42(e) were to allow Municipal Advisors to limit the scope of their engagement so as to not have an obligation to review any recommendation made by a third party pursuant to the exemption. In order for a third party to avail itself of the IRMA Exemption, the Municipal Advisor must be providing advice with respect to the same aspects of the municipal financial product or issuance of municipal securities as that of the third party to ensure that such party is receiving the benefits of having engaged a Municipal Advisor. It is, therefore, counterintuitive to believe that the SEC would have created the IRMA Exemption if Municipal Advisors could simply disclaim their obligations to review third-party recommendations.

Rule G-42(e) should therefore be amended to take into consideration the foregoing.

Although not stated, presumably G-42(e) would be equally applicable to advice provided in response to an RFP as well as to those parties relying on the IRMA Exemption. In this regard, Rule G-42(e)(i) through (iii) are potentially overly burdensome in terms of the scope of the obligations they impose. Financings simply would not be completed as Municipal Advisors would be required to devote an extensive amount of time to such analyses.

In light of the foregoing, a principles-based rule would be ideal. Such a rule could simply state that when requested and when such acts are within the Municipal Advisor's scope of engagement, a Municipal Advisor is to consider the recommendations of third parties and determine whether such recommendations are in the best interest of their municipal entity or obligated person client based on all the relevant facts and circumstances. This approach would strike the right balance by protecting the interests of municipal entities and allowing Municipal Advisors to view each recommendation within the context of their particular engagement, without having to go through potentially time consuming and unnecessary analyses.

Principals Transaction & Specific Prohibitions – G-42(f) and (g)

NAIPFA agrees with proposed Rule G-42(f) and (g). We believe that these rules are important measures that are needed to eliminate certain practices that often carry unmanageable conflicts of

[2] Securities and Exchange Commission, 17 CRF Parts 240 and 249 [Release No. 34-70462; File No. S7-45-10], at 156.

interest inconsistent with Municipal Advisor fiduciary duties. As proposed, NAIPFA believes these provisions are appropriately tailored and do not impose undue regulatory burdens.

Notwithstanding the foregoing, with respect to G-42(f), NAIPFA believes that additional guidance would be appropriate to clarify further the provision's use of the phrase "principal capacity." NAIPFA believes that it would be appropriate to specify that, for purposes of this section, the phrase "principal capacity" would include a party's activities as an underwriter of securities, remarketing agent, counterparty on swaps or other derivative transactions, or other similar capacity. In general, these kinds of relationships could conflict with the interests of municipal entities and obligated persons, and, therefore, such relationships should be prohibited in instances where the "principal" or an affiliate thereof also serves as the Municipal Advisor to such municipal entity or obligated person.

Comments to the Notice's General Questions

1. Fiduciary Duties to All Clients

As noted above, NAIPFA supports the imposition of a uniform fiduciary standard. Such a standard would further ensure the protection of the public interest.

2. Obligation to Review Official Statement

In general, NAIPFA believes that Municipal Advisors should be obligated to review the issuer's official statement. However, this review should be limited to determining whether appropriate disclosures have been made and must not obligate a Municipal Advisor to conduct an independent inquiry into the accuracy of such disclosures, unless the Municipal Advisor reasonably believes that any such disclosure is not materially accurate. In other words, absent information indicating that a disclosure may be materially inaccurate, Municipal Advisors should be permitted to conclusively rely upon the information provided by the issuer and, to the extent that the official statement is prepared by a third party, the information contained within the official statement.

3. Prohibition on Fee Splitting Arrangements

In general, NAIPFA is not opposed to prohibiting certain fee splitting arrangements. However, NAIPFA believes that a clear definition of "Fee Splitting Arrangement" should be developed prior to imposing any prohibitions. In so doing, NAIPFA urges the MSRB to recognize that a Municipal Advisor's utilization of independent contractors/subcontractors in connection with particular engagements should fall outside of any such definition.

4. Timing of Disclosures

Except as noted above with respect to a Municipal Advisor's reasonable estimate of its fee, NAIPFA believes that the timing of the provision of disclosures under the Notice is appropriate.

5. Required Acknowledgement of Conflicts

NAIPFA believes that it is appropriate to require Municipal Advisors, like underwriters and professionals possessing fiduciary duties, to obtain an acknowledgment from their clients. In this regard, we believe it would also be appropriate for such obligations to mirror those currently in place for broker-dealers under MSRB Rule G-17.

6. Disciplinary Events

To the extent that disciplinary events will be noted on any Form MA-I filed by the Municipal Advisor firm, additional disclosures seem superfluous and will place additional regulatory burdens on small Municipal Advisor firms in particular. Notably, there is no similar requirement imposed on underwriters, even though they do not possess fiduciary duties and arguably such disclosures would be more pertinent in such a case. As such, NAIPFA believes these disclosures will place Municipal Advisors at a significant competitive disadvantage.

7. Professional Liability Requirements

As discussed above, NAIPFA believes that both mandatory disclosures and mandatory professional liability insurance coverage will place IRMAs at a significant competitive disadvantage to broker-dealer firms. Such requirements will adversely impact the ability of small Municipal Advisor firms to compete for municipal advisory business. These requirements would also pose significant barriers to entry with respect to individuals and small groups of individuals wishing to form Municipal Advisor firms. In total, this will result in less competition and higher costs of issuance resulting not only from higher Municipal Advisor fees, but also from a simple lack of available advisors. In addition, municipal entities and obligated persons will be forced to rely more heavily on advice from underwriters, who do not possess fiduciary duties, thereby further increasing the costs borne by tax and rate payers.

Furthermore, it is important to note, again, that there are no similar disclosure or insurance coverage requirements in place for investment advisors or attorneys who also possess fiduciary duties. With respect to these aspects of G-42, the MSRB has determined to treat Municipal Advisors more like broker-dealers, who, for good reason, have capital requirements, than other parties who possess fiduciary duties. NAIPFA can find no rational basis for this. Therefore, neither the proposed rule's disclosure requirements nor the prospective imposition of mandatory professional liability insurance coverage are appropriate.

Finally, we anticipate that organizations representing broker-dealers will fully support the proposed rule. We also anticipate that these groups will support the imposition of mandatory liability insurance coverage. The imposition by the MSRB of mandatory professional liability insurance as discussed more fully below, or even insurance-related disclosures, may effectively eliminate small Municipal Advisor firms from the market, and we are concerned that the

underwriter community will support these requirements merely as a means of putting Municipal Advisors at a competitive disadvantage, if not out of business entirely.

8. Feasibility Study Reviews

MSRB Question #11 asks: "Should an advisor be required to review any feasibility study as a part of the information considered in its evaluation of whether a transaction it recommends is suitable for the client?"

NAIPFA believes it would be appropriate to enact a provision that requires Municipal Advisors to disclose to any client whether the scope of their engagement includes an obligation to review any feasibility study. Municipal Advisors who are engaged to review feasibility studies would have to conduct a reasonable review of any such feasibility study and make an assessment of whether the conclusions reached are in accordance with the best interests of their client. Municipal Advisors should not, however, be obligated to assess the assumptions made by a third party with respect to any conclusion made, unless such services are requested of and agreed to by the Municipal Advisor.

Comments to the Notice's Economic Analysis Questions

1. Should the MSRB Articulate the Duties or Measures to Prevent Breaches of a Municipal Advisor's Fiduciary Duty? If so, Does the Rule Address This?

NAIPFA strongly believes that the MSRB should articulate duties and prescribe means of preventing breaches of Municipal Advisor fiduciary duties. However, any duty articulated or means prescribed must be designed to prevent such breaches. As discussed above with respect to the liability insurance coverage, any disclosure that is not reasonably likely to cause Municipal Advisors to better adhere to their fiduciary duties or which relates to material conflict of interest should not be required. Where the disclosure does not reasonably relate to a Municipal Advisor's fiduciary duty, municipal entities and, if appropriate, obligated persons are not likely to receive any appreciable benefit from such disclosures. Rather, the increased burden and expense caused on Municipal Advisors by such disclosures as well as the barriers to competition erected will likely increase costs of issuance. Therefore, we would encourage the MSRB to look at any disclosure related rules primarily with respect to whether any such proposed rule will benefit municipal entities and obligated persons in terms of the quality of advice provided and whether such rule is appropriately tailored to minimize any potential increases in issuance costs resulting from such rules.

2. Questions #2 through #8

NAIPFA respectfully requests that Questions #2 through #8 be revised and resubmitted for response. We are simply not sure how to answer the questions posed. In particular, we ask that the MSRB articulate what it means by the term "baseline" within the various questions.

In general, however, NAIPFA believes that from an economic standpoint our member firms will judge the economic impacts of proposed regulations based on the two plus decades that many of these firms have been in existence. Again, during this time, our member firms have acted with fiduciary responsibilities towards their clients. The cost of their adherence to this duty has, until now, been minimal. Conversely, every regulation put in place costs Municipal Advisors money and increase costs of issuance. As such, we urge the MSRB to strongly consider this when imposing regulations.

Notwithstanding our economic concerns, we believe that appropriately tailored regulations are important. Therefore, NAIPFA proposes that rather than establish "baselines" for its economic analysis, the MSRB attempt to quantify its proposed rules in terms of dollars. The MSRB should then conduct a cost benefit analysis to determine if the potential benefits of any particular regulation outweigh the financial burden that such regulations would place upon Municipal Advisor firms, particularly, small firms, municipal issuers and obligated persons, and tax and rate payers.

3. Lower-Cost Alternatives to Requiring Disclosures of the Amount of Professional Liability Coverage

NAIPFA does not believe that this question is able to be answered effectively because it presupposes that a disclosure relating to professional liability insurance is appropriate. Notwithstanding this, NAIPFA believes that a lower cost alternative would be to require municipal advisors to provide such information as part of their annual MSRB renewal filing or upon their client's request. This would lower the overall compliance costs by decreasing the quantity of disclosures that a Municipal Advisor would otherwise be required to make on a per transaction basis. Requiring this disclosure in connection with Municipal Advisor annual MSRB renewals would also be consistent with the MSRB's goal of transitioning EMMA towards becoming a more non-industry centric platform for municipal securities related matters, including disclosure.

4. Will the New Standards Change the Quality of Advice Offered by Municipal Advisors?

These new standards will likely cause Municipal Advisors to incur additional costs due to compliance. This additional time and cost will put some strain upon small Municipal Advisor firms in particular, which could reduce competition. With respect to those firms who may be less impacted financially by these standards, NAIPFA does not anticipate that these regulations will have any appreciable benefit upon the quality of advice provided. Regardless, NAIPFA does not believe that this should be the goal of G-42. We believe that G-42 should be designed to protect the interests of Municipal Advisor clients. That being said, the advice Municipal Advisor clients have received has, for the most part, served them well. Therefore, NAIPFA believes that the MSRB should focus on ways to ensure that Municipal Advisors adhere to their fiduciary duties and to do so in as minimally burdensome of a manner as possible and not, within the context of G-42, necessarily focus on improving the quality of the advice provided but,

rather, ensuring that municipal issuers and obligated persons have access to and can accurately identify professionals who can provide high quality advice.

5. Will G-42 Affect the Willingness of Market Participants to Use Municipal Advisors?

Our member firms, as well as other Municipal Advisor firms, have acted with and advertised themselves as having fiduciary duties to their clients for many years. Municipal Advisors have also been required to act pursuant to a federal fiduciary duty to municipal entity clients since 2010. In addition, since the enactment of Dodd-Frank, NAIPFA is not aware of any law suits or regulatory actions that have been initiated relative to a breach of a Municipal Advisor's fiduciary duty. In light of the foregoing, we believe that if an increase in the use of Municipal Advisors arising from their fiduciary duties was to occur, that such an increase has likely already begun and will likely continue regardless of these rules. Therefore, we do not believe that proposed Rule G-42 will appreciably increase the use of Municipal Advisors.

6. Will G-42 Reduce Issuance Costs, Lead to Better Financing Terms, and Improve Capital Formation?

NAIPFA does not believe that these rules will achieve any of these objectives. The increased regulatory burden upon Municipal Advisors will likely lead to increased issuance costs. NAIPFA finds no reason to believe that proposed Rule G-42 will lead to better financing terms for issuers; again, Municipal Advisors have acted with a federal imposed fiduciary duty since 2010, at least with respect to municipal entity clients. Thus, capital formation, to the extent that it would have been impacted by a federal fiduciary standard, has likely already improved and will continue to improve with or without the imposition of proposed G-42, although this may be difficult to measure due to ongoing changes in market conditions.

7. Would the requirements of draft rule G-42 assist market participants in Municipal Advisor hiring decisions?

As discussed above, we believe that the disclosures that relate to material conflicts of interest will benefit municipal entity and obligated person decision making. Nonetheless, and as discussed above, some of the disclosures and other measures described within the proposed rule will not assist such decision making because such disclosures do not relate to the discharge of fiduciary duties. If municipal entities and obligated persons wish to receive information that goes beyond what is mandated by the MSRB, those municipal entities and obligated persons should be free to inquire into such other matters, and the MSRB should support this by requiring Municipal Advisors to truthfully provide such other information upon a client's request. The MSRB should be similarly supportive of contractual provisions between municipal entities and obligated person and their Municipal Advisors which extend beyond the requirements of G-42 and other MSRB rules. Again, this would strike the right balance in terms of creating effective regulation, minimizing regulatory burdens, and supporting client control over the issuance process.

8. Additional Costs Associated with Making and Preserving Books & Records

An analysis, economic-related or otherwise, with respect to any MSRB rule derived from a SEC Municipal Advisor rule is only necessary where the MSRB rule modifies the corresponding SEC rule, or where the MSRB rule relates to a matter that has not been addressed by the SEC. In all other instances, because the MSRB will be unable to vary the terms of any such rule, any exercise in an economic analysis of such rule's impact would seem to be of little value.

9. Effects on Competition, Efficiency and Capital Formation

If G-42 places a significant burden on Municipal Advisors, small Municipal Advisor firms could merge with other firms, retire or simply exist the market.[3] This will reduce competition, increase costs of issuance, and hurt capital formation, particularly in the small rural areas most in need of advice.

10. Barriers to Entry

We believe that a significant barrier to entry will be created as a result of the insurance-related disclosures. This barrier will only be exacerbated if the MSRB imposes professional liability insurance requirements upon Municipal Advisor firms. Currently, there is a lack of available insurance providers nationally who are willing/able to provide coverage for Municipal Advisors and, as of today, insurance is not readily available that will sufficiently cover the activities of Municipal Advisors. We have begun the process of identifying insurance companies which may be willing/able to cover Municipal Advisors; however, they are few in number. We have as of the date of this letter received an estimate of what this coverage may cost, which is as follows:

For a $1,000,000 aggregate claims policy for a firm of 1 to 4 professionals that carries both civil and regulatory coverage, the premium is estimated at $19,000 to $24,000 per year with a minimum deductible of $75,000; provided, however, that these terms can vary (presumably upward) depending on the risk attributed to the Municipal Advisor firm by the insurer. For small firms the premium alone may represent upwards of 10 to 15% of their annual gross revenue. Thus, if new firms were to try to enter the market, we believe coverage may be very difficult to afford or even acquire since such firms will have no operating history upon which the insurance provider could assess risk and may not have sufficient funds available.

11. Costs of Training & Compliance

The cost of training and compliance will depend upon the number of Municipal Advisor representatives each firm employs, but as the number of employees increases, so do the costs of

[3] Notwithstanding, NAIPFA is unaware of any discussions among firms regarding potential consolidations resulting from regulation. We find that it is more likely that firms, certain employees, and sole proprietors will predominantly choose to retire or not provide services as Municipal Advisors rather than attempting to carry on their work in an overly burdensome regulatory environment.

training and compliance. That being said, we believe on average that the cost of training and compliance will be approximately $2,500 to $4,500 per person, or, depending upon the firm, the equivalent of 5% to 20% of firm revenue annually.

Conclusion

NAIPFA believes that much of the Notice is acceptable. However, we also believe that revisions should be made in order to adequately regulate Municipal Advisors. Currently the proposed rules are overly broad in several key respects as noted above. The unnecessary provisions identified will place significant burdens on current and future Municipal Advisors, particularly IRMAs and even more so with respect to small firms, and will increase costs of issuance without achieving any appreciable benefit. Therefore, NAIPFA strongly urges the MSRB to consider revising G-42 in accordance with the foregoing comments.

Sincerely,

Jeanine Rodgers Caruso, CIPFA
President, National Association of Independent Public Finance Advisors

cc: The Honorable Mary Jo White, Chairman
The Honorable Kara Stein, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Michael Piwowar, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
Lynnette Kelly, Executive Director, Municipal Securities Rulemaking Board

New York State Bar Association
One Elk Street
Albany, NY 12207
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Business Law Section
Securities Regulation Committee

August 27, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Suite 600
Alexandria, VA 22314

Re : Regulatory Notice 2014-12
Request for Comment on Revised Draft MSRB Rule G-42,
on Duties of Non-Solicitor Municipal Advisors

The Securities Regulation Committee of the Business Law Section of the New York State Bar Association appreciates the invitation from the Municipal Securities Rulemaking Board ("MSRB" or "Board") in Regulatory Notice 2014-12 to comment on the MSRB's revised draft Rule G-42 (Duties of Non-Solicitor Municipal Advisors).

The Committee is composed of members of the New York State Bar Association, a principal part of whose practice is in securities regulation. The Committee includes lawyers in private practice and corporation law departments. A draft of this letter was reviewed by certain members of the Committee. The views expressed in this letter are generally consistent with those of the majority of members who reviewed and commented on the letter in draft form. The views set forth in this letter, however, do not necessarily reflect the views of the organizations with which its members are associated, the New York State Bar Association or its Business Law Section.

Introduction

As the Securities and Exchange Commission ("SEC") noted in the release adopting final rules for municipal advisors (SEC Release No. 34-70462[1])("Adopting Release"), citing the Senate report related to the Dodd-Frank Act, the municipal securities market has been

[1] www.sec.gov/rules/final/2013/34-70462.pdf.

significantly less regulated than the corporate securities market, and during the financial crisis a number of municipalities suffered losses from complex derivatives products marketed by unregulated financial intermediaries.[2] We support the efforts of Congress and the SEC to regulate those financial intermediaries as municipal advisors, and we generally support the Board's effort to impose standards of conduct on municipal advisors. We also support many of the changes the Board has made in response to comments on the original proposal in Regulatory Notice 2014-01. However, we would like to take this opportunity to comment specifically on the amended prohibition on principal transactions, which we believe still does not provide adequate flexibility to accommodate special circumstances.

As we noted in our comment latter, dated March 12, 2014, on Regulatory Notice 2014-01, the definition of "municipal advisor" in Section 15B(e) of the Securities Exchange Act of 1934 ("Exchange Act"), as interpreted by the SEC, encompasses a wide variety of persons and activities, including persons that advise municipal entities on the issuance of municipal securities or act as intermediaries or finders between municipal entities and municipal underwriters, and also persons that advise municipal entities and obligated persons with respect to municipal financial products – municipal derivatives, guaranteed investment contracts and investment strategies, including plans or programs for the investment of the proceeds of municipal securities.

The definition of municipal advisor as interpreted by the SEC may include other categories of persons who may not consider themselves to be in the business of acting as municipal advisors, including providers of guaranteed investment contracts and counterparties in municipal derivatives. If those persons provide advice about their products, in addition to selling them, they may be considered municipal advisors.

Comments on Prohibition on Principal Transactions

Permitting Exceptions in Appropriate Circumstances. Section (e)(ii) of proposed MSRB Rule G-42, as revised, would provide as follows:

> A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice.

For the reasons stated below, we believe Paragraph (e)(ii) of proposed Rule G-42 should be revised to permit principal transactions where (1) the municipal advisor does not make a recommendation to the municipal advisory client to enter into a transaction with the municipal advisor or its affiliate, (2) the municipal advisor discloses the potential conflict of interest and (3) the municipal advisor receives written acknowledgement from te municipal entity client of the conflict prior to the transaction.

[2] Adopting Release text at n. 3.

We continue to believe that there are circumstances in which a municipal advisor or its affiliate should not be barred from engaging in a principal transaction with the municipal entity client, notwithstanding the fact that the transaction is directly related to the municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice, if there is adequate disclosure of the potential conflict of interest and written consent and acknowledgment by the municipal entity client. Those circumstances may arise in the following situations, among others:

- The municipal entity client comes to the municipal advisor and, if applicable, its affiliate, specifically to purchase a municipal financial product and to obtain advice about the use of that product.
- The municipal advisor provides advice about a municipal securities transaction or municipal financial product and the decision to enter into a principal transaction with the municipal advisor or its affiliate is made by the municipal entity client on the basis of advice by an independent advisor, such as another municipal advisor, an investment adviser or a broker-dealer.
- The municipal advisor provides advice about a municipal securities transaction or municipal financial product, but not including a recommendation to use the advisor or its affiliate as a counterparty, and the client makes an independent determination to use the advisor or its affiliate.

In those and other situations in which the municipal advisor is providing advice about the municipal securities transaction or municipal financial product but not making a recommendation that it or its affiliate should be the counterparty, the transaction should not be prohibited so long as the municipal advisor provides disclosure concerning the potential conflict of interest and obtains prior written acknowledgment from the municipal entity client of the conflict and of the fact that the advisor has not made a recommendation that it or its affiliate act as principal in the transaction.

Section 206(3) of the Investment Advisers Act of 1940 does not contain a blanket prohibition on principal transactions but instead prohibits investment advisers from engaging in principal transactions "without disclosing to such client in writing before the completion of such transaction the capacity in which he is acting and obtaining the consent of the client to such transaction." The SEC has provided further guidance concerning the nature of the disclosure and client consent in temporary rule 206(3)-3T. Similarly, Congress, in the Dodd-Frank Act, recognized that there may be circumstances where principal transactions by a fiduciary should be permissible with adequate disclosure. Section 913(g) of the Dodd-Frank Act added Section 15(k) of the Exchange Act, authorizing the SEC to establish a standard of fiduciary duty for brokers and dealers. Section 15(k)(2) of the Exchange Act authorizes the SEC to adopt standards of conduct for brokers and dealers that permit brokers or dealers that sell only proprietary or other limited range of products to sell those products without violation of the standards, on the condition that the broker or dealer provides notice to each retail customer and obtains the consent or acknowledgment of the customer.

Paragraph (e)(ii) of proposed Rule G-42 should be revised to permit principal transactions where (1) the municipal advisor does not make a recommendation to the municipal

entity client to enter into a transaction with the municipal advisor or its affiliate, (2) the municipal advisor discloses the potential conflict of interest and (3) the municipal advisor receives written acknowledgement of the conflict prior to the transaction. We believe that this will give municipal entities the freedom to choose the parties with whom they wish to enter into transactions while providing adequate protection against self-dealing by municipal advisors.

Clarification of Definition of "Engaging in a Principal Transaction". Proposed Rule G-42(f)(i) would define "engaging in a principal transaction" to include, when acting for one's own account, "entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client." The phrase "other similar financial product" is somewhat open-ended and capable of varying interpretations. We suggest that the phrase be changed to: "or other municipal financial product," since that term is defined in the statute. Alternatively, because derivatives and guaranteed investment contracts are included within the definition of municipal financial product, the quoted portion of the proposed definition could be revised and shortened to say: "entering into any municipal financial product with the municipal entity client.

The definition, or the supplementary material, should further clarify that the definition of "engaging in a principal transaction" does not include any of the banking activities about which a bank may provide advice without being registered as a municipal advisor, pursuant to the exemption in SEC Rule 15Ba1-1(d)(3)(iii). Those activities include:

- Holding investments in a deposit account, savings account, certificate of deposit or other deposit instrument issued by a bank;
- Extensions of credit by a bank to a municipal entity or obligated person, including the issuance of a letter of credit, the making of a direct loan, or the purchase of a municipal security by the bank for its own account;
- Holding funds in a sweep account; or
- Investments made by a bank acting in the capacity of an indenture trustee or similar capacity.

* * * * *

We are grateful for the opportunity to provide these comments on the revised draft Rule and for the Board's attention and consideration. We hope that our comments, observations, and recommendations contribute to the important work of the Board in carrying out the regulatory initiatives under the Dodd-Frank. We would be happy to discuss these comments further with the Board and its staff.

Respectfully submitted,

SECURITIES REGULATION COMMITTEE

By: /s/
Peter W. LaVigne
Chair of the Committee

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August 25, 2014

SENT VIA ELECTONIC MAIL

Mr. Ronald Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Arlington, VA 22314

Dear Mr. Smith:

I am pleased to submit this letter on behalf of Piper Jaffray in response to the request for comment on the MSRB's revised draft of Rule G-42 which specifies duties and responsibilities of municipal advisors.

I am responding as the Head of Public Finance for a firm that has a meaningful and varied public finance business. We serve many municipal issuers each year, including issuers of all sizes. We are among the leaders in both the number of senior managed underwritings that we complete each year as well as the number of issuers that we serve as a financial advisor. As a result, we bring a unique and broad perspective to the issues covered under proposed rule G-42.

General Perspective on the Revisions to the Proposed Rule

First, I want to thank the MSRB for a number of the changes that were made to the initial draft of Rule G-42. It is clear that you listened to and evaluated many of the comments that were made relative to the concerns expressed about the initial draft. In particular, I appreciate the direction of the MSRB's change to the prohibition on principal transactions when serving as a municipal advisor which limits this prohibition only to the transactions directly related to the transaction on which advice is being provided. While I still have some concerns and comments relative to this section of the rule and the term "directly related to", this change more closely aligns Rule G-42 with the interpretive guidance from the SEC's municipal advisor rule. I also agreed with and appreciated the MSRB's decision not to extend the fiduciary duty of a municipal advisor to obligated persons.

I do still have some comments, questions and areas of uncertainty about the revised draft of the rule that are shared below for your consideration.

Obligated Persons

As I stated above, I agree with and appreciate the MSRB's decision to limit the duty of a municipal advisor to an obligated person to a "duty of care" rather than a "fiduciary duty". We view obligated persons as fundamentally different entities from municipal entities in many respects and believe that this difference in duty when serving as an advisor makes sense.

Limitations on Principal Transactions

While the changes that the MSRB has made related to the prohibition on principal transactions in G-42 (e) (ii) are an improvement, I still believe that there is significant confusion related to using the term "directly related to" in defining the transactions that are subject to this prohibition. The SEC in its interpretive guidance on "role switching" stated that the fiduciary duty (and therefore the prohibition on role switching) is related to the transaction or issuance where the broker dealer served as a municipal advisor. I believe that it would make most sense for the revised version of G-42 to be in synch with the SEC guidance and limit its prohibition to a transaction or issuance where a firm served as a municipal advisor and about which advice was rendered.

The language in the revised G-42 (e) (ii) contains a prohibition on not only the transaction for which a municipal advisor gave advice but also to any "directly related" transactions. I am not sure what a "directly related" transaction is and this broader language could prohibit a variety of different principal transactions where I do not believe there is any conflict of interest.

For example, many comments were made about the initial draft of G-42 regarding concerns over the principal transaction ban preventing a firm who serves as a municipal advisor to an issuer from providing investments as a principal to the issuing entity. Does the term "directly related" transaction include selling investments as a principal to an issuer of their bond proceeds after serving as an advisor on that issue even if no advice was provided related to investments? Does the answer differ if the investments are being sold shortly after closing as opposed to being sold a year after the issue was closed? Does the answer vary if the investments are being bid out by a third party advisor?

If the scenario on investment of bond proceeds were reversed and a broker dealer served as an underwriter of the bonds and then was selected in an advisory capacity on a separate transaction to bid out the investment of an escrow or serve as an investment advisor for bond proceeds, does this result in a prohibition? Is this true even if the firm was not selected until after the bond transaction was closed or completed or even if the selection was through a competitive process?

Another example of potential confusion would include two separate issues of bonds for a school district that are completed several years apart but were authorized under the same voter authorization. Would these issues be considered "directly related" because they are part of the same voter authorization even though they are completely different issues separated by multiple years? Would a refunding of an issue that is completed a number of years after the initial issuance be considered "directly related" to the initial issue? I would hope that the answer to these questions would be no, that these issues were not "directly related" to the initial issue and would not create a prohibition on a principal transaction if a firm had served as an advisor for that issuer previously.

As stated above, I believe that the prohibition should be limited to an issue or transaction on which advice was rendered by a firm while serving as a municipal advisor. If the board feels that this prohibition needs to use the term "directly related", it is important to more fully define this term and to limit its definition. It would make more sense and be more clear to use the term "directly related" in connection with transactions directly related to the advice given rather than directly related to the transaction itself (which is more ambiguous). It would be a mistake to create prohibitions or uncertainty

about potential prohibitions on transactions that are completely separate from the advice that was given by the firm as a municipal advisor and do not present any particular conflict of interest.

Disclosure of Conflicts of Interest & Documentation of a Municipal Advisory Relationship

The proposed rule calls separately for a disclosure of conflicts of interest and for the documentation of each municipal advisory relationship. It appears that the rule has intentionally set forth these two requirements as separate disclosures because the requirement for each of these disclosures may "kick in" at different stages in the communication of a municipal advisor with an issuer. I think that I understand the differences in these two requirements and the possible rationale for these differences, but it might be simpler and less confusing if a these requirements were combined into the written agreement at the establishment of the municipal advisory relationship.

Let me provide an example and you can determine if I understand the rule and its intention correctly. In preliminary discussions with an issuer, a municipal advisor may provide analysis or recommendations that would be considered "advice". A municipal advisor is permitted to do even if not yet engaged by that issuer but under G-42 must provide appropriate conflict disclosures along with this "advice" that are consistent with the requirements under G-42 (b). In this case, disclosure related to compensation under G-42 (b) (i) (F) would not make sense because the municipal advisor has not yet been hired and may not yet have talked about a fee arrangement.

If and when the municipal advisor is actually hired by the issuer, then the municipal advisor would have to evidence this "municipal advisory relationship" in writing in compliance with G-42 (c) and may have to supplement its conflict disclosures under G-42 (b) to reflect any additional information not known when the initial conflict disclosure was provided (such as any conflicts related to compensation).

Ultimately, my question is whether it is the intention of the board to assure that municipal advisors must provide conflicts disclosure when providing information that would constitute "advice" prior to be engaged. In general, I believe that it would be simpler and less confusing to issuers to require municipal advisors to provide both the conflict disclosures and the documentation of the municipal advisory relationship at the same time when the advisor is selected by the issuer to provide it with advice. The issuer would have the opportunity to review and discuss these conflicts before proceeding to enter into its written agreement.

Lastly, I still do not believe that it is beneficial or appropriate to single out a written conflict disclosure requirement related to compensation that is contingent on the closing or size of a transaction. I believe that all forms of compensation have some theoretical form of conflict. As an example, hourly fees have the potential conflict that an advisor may have incentive to spend more time than necessary related to its duties. I believe that the potential conflicts of different fee arrangements are generally knowable and that there is no good reason to require their written disclosure or to require disclosure related to only one form of compensation (which happens to be the most common form used by municipal advisors).

Recommendations and Review of Recommendations of Other Parties

I believe that the changes that have been made to G-42 (d) are improvements over the initial draft, however, I am still trying to determine exactly what our firm will need to do as a municipal advisor to

make a suitability determination and what documentation we will need as part of our obligation to "inform the client" of the various material risks and alternatives to a particular transaction.

As I commented in my previous letter, these requirements all make more sense when contemplating a "product" such as a variable rate financing or a synthetic fixed rate issuance as an alternative to a more standard fixed rate issue. It is easier in this instance to determine how to think through whether the features of the proposed transaction are appropriate for an issuer and to walk the issuer through risks and potential benefits versus potential alternatives including the use of a fixed rate issuance structure.

However, most financings do utilize a fixed rate structure. While there are usually (but not always) far less concerns about suitability and risks related to a fixed rate financing, there are many smaller decisions including such items as the trade-offs in marketing the bonds of using a ten year par call rather than a ten year call at 102, or whether to utilize a premium bond structure that has a lower yield to call as opposed to a par bond structure that has a higher yield to call but a lower yield to maturity. There are many other examples of decisions that are routinely made on many fixed rate issues. It is not clear to me what G-42 (d) is requiring relative to decisions about, communication of and documentation of all of these various types of "smaller" decisions that are made on every issue.

Specified Prohibitions

Although you did not include the two "troublesome practices" that I mentioned in my comment letter on the initial draft of Rule G-42, I will again recommend consideration of inclusion in G-42 (e) of one of these two items that has concerned me over the years in the marketplace. I believe that it should be spelled out as a prohibited activity for any municipal advisor to take into account whether it competes with other firms in its recommendations to an issuer about who they should hire as an underwriter.

As a broker dealer who does a meaningful volume of both underwriting and financial advisory work for issuers, we have had many instances in the past where other advisory firms have threatened us or told us directly that they would not recommend that their issuer clients hire us as an underwriter because we compete with them for various advisory engagements. I believe that this practice is wrong, not aligned with the duty of a municipal advisor to its client and should be specifically prohibited.

Summary

I have again attempted to provide thoughtful and practical comments related to the revised draft of Rule G-42. I hope that these comments are helpful to you as you work to finalize this rule.

Sincerely,

Frank Fairman
Managing Director
Head of Public Finance Services

sifma
Invested in America

August 25, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Request for Comment on Revised Draft MSRB Rule G-42 on Duties of Non-Solicitor Municipal Advisors; MSRB Regulatory Notice 2014-12

Dear Mr. Smith:

The Securities Industry and Financial Markets Association ("**SIFMA**")[1] appreciates the opportunity to provide comments on the Municipal Securities Rulemaking Board ("**MSRB**") Regulatory Notice 2014-12 containing a revised draft proposal for MSRB Rule G-42 ("**Re-Proposed Rule G-42**") on the standards of conduct and duties of municipal advisors when engaging in municipal advisory activities other than solicitations.

I. Executive Summary

SIFMA applauds the MSRB's efforts in revising its original proposal in light of comments received.[2] SIFMA believes that the MSRB made great strides in making Re-Proposed Rule G-42 workable without compromising protections to municipal entities, obligated persons or investors. However, SIFMA still has significant concerns regarding certain aspects of Re-Proposed Rule G-42. In particular:

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

[2] SIFMA commented in detail on the original proposal. *See* Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated March 10, 2014, *available at* http://www.msrb.org/RFC/2014-01/SIFMA.pdf.

- The proposed prohibition on principal transactions should only apply to transactions that are directly related to the advice provided by the municipal advisor, rather than transactions that are unrelated to the municipal advisory relationship.

- The proposed prohibition on principal transactions should not apply to all business units of a municipal advisor and its affiliates. Most financial institutions have businesses and affiliates that are completely unconnected with their municipal advisor business, and the activities of such "remote" businesses should not be subject to the prohibition on principal transactions. Instead, the prohibition should apply only to businesses at the municipal advisor and its affiliates that have significant connection with a municipal advisory engagement.

- The proposed prohibition on principal transactions should provide an exception for municipal advisors that are broker-dealers providing incidental advice in connection with brokerage/securities execution services, particularly with respect to fixed-income securities.

- The documentation and disclosure requirements under Re-Proposed Rule G-42 should be revised so that they do not inappropriately apply to incidental advice provided in connection with brokerage/securities execution services.

- The safe harbor for inadvertent advice in Supplementary Material .06 should be expanded to provide an exception from the prohibition on principal transactions and certain other requirements under Re-Proposed Rule G-42.

II. Comments on Content of Re-Proposed Rule G-42

A. Principal Transactions

Re-Proposed Rule G-42(e)(ii) prohibits a municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, from "engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice." While SIFMA believes that the prohibition as reformulated in Re-Proposed Rule G-42 is vastly more workable for municipal entities and municipal advisors than under the original proposal, there are a number of technical problems and ambiguities in the proposed rule text that the MSRB should rectify.

1. The MSRB Should Clarify That the Principal Transaction Ban does Not Apply to Transactions that are Not Directly Related to the Advice Rendered by a Municipal Advisor

Pursuant to Re-Proposed Rule G-42(e)(ii), the prohibition on principal transactions is triggered only when a municipal advisor or its affiliate engages in a transaction as principal "directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice."

The MSRB should clarify that the prohibition only applies to principal transactions that are directly related to the *advice* the municipal advisor is providing, not merely the same municipal securities *transaction* in connection with which the advice is provided. For example, a municipal advisor may have an advisory relationship with respect to a client's investment activities. In that context, a municipal advisor may be asked to provide advice with respect to the investment of the potential proceeds of an issuance of municipal securities. The MSRB should confirm that acting as a municipal advisor in such a context would not result in the municipal advisor (or its affiliates) being prohibited from acting as a principal in a municipal securities offering that client ultimately decides to engage in—such as acting as an underwriter of that transaction or an affiliate engaging in a direct purchase of the resulting municipal securities.

Similarly, consider a situation where a firm is engaged as an underwriter on a municipal securities transaction. During the course of the transaction, the issuer contacts a separate division of the same firm to seek its assistance in acting as a guaranteed investment contract broker with respect to the anticipated proceeds. The MSRB should clarify that such a tangential municipal advisory engagement conducted by separate personnel from the underwriting engagement would not be prohibited under the rule, as the underwriting is not directly related to the advice provided under the municipal advisory relationship.

Although not entirely clear from the proposed language, SIFMA believes that, in these cases, a municipal advisor or its affiliate acting as an underwriter should not be viewed as engaging as principal with respect to the "same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice," even if all or a portion of the proceeds of an issue of municipal securities are included within the funds as to which the municipal advisor is providing advice. Moreover, a bank that is affiliated with a municipal advisor should not be precluded from engaging in a direct purchase of municipal securities from an issuer where its affiliate (*e.g.*, an asset manager) has provided, or provides, investment advice with respect to proceeds of those securities, as the transaction has no relation to the advice.

Accordingly, Re-Proposed Rule G-42(e)(ii) should be revised as follows: "A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the *advice rendered by such municipal advisor*."

2. The Principal Transaction Ban Should Be Limited to Areas of a Municipal Advisor and its Affiliates That Have Actual Knowledge of the Municipal Advisory Relationship and its Scope

The principal transaction ban in Re-Proposed Rule G-42(e)(ii) is currently drafted in a manner that could be read to prohibit principal transactions by areas of a municipal advisor and its affiliates ("**Remote Business Units"**) that have no knowledge of the advisory engagement or its scope and where the municipal advisory business: (i) has not advised, directed or encouraged the municipal entity to engage in the principal transaction with such other area or affiliate and (ii) has no direct economic interest in any such principal transaction. In effect, the ban, as drafted, imposes a strict liability standard on the legal entity that is acting as a municipal advisor and its affiliates. In SIFMA's view, the purpose of a principal transaction ban is to ensure that the municipal advisor, through its advisory personnel, provides disinterested advice that is not influenced by the potential for profiting through self-dealing. No policy is furthered by a ban that purports to extend to Remote Business Units. If such a strict liability standard were extended to Remote Business Units, multi-service firms that consist of numerous departments and corporate affiliates would need to implement extensive internal processes to ensure that Remote Business Units and their personnel did not inadvertently violate the principal transaction ban.[3] Not only would such processes be costly and burdensome to implement, and serve no practical benefit, but they would potentially result in inappropriate sharing of customer information and leakage of material nonpublic information around an extensive organization, which would run contrary to the information barriers and other informational safeguards that are at the core of most financial institutions' compliance programs and cultures and which are in many cases legally mandated. [4]

Accordingly, Re-Proposed Rule G-42(e)(ii) should be revised to exclude from its ambit principal transactions by Remote Business Units. The MSRB could address this concern by revising Re-Proposed Draft Rule G-42(e)(ii) to include a knowledge qualifier, as follows: "A municipal advisor to a municipal entity client, and any affiliate of such

[3] If the MSRB were to accept SIFMA's proposed clarification in Section II.A.1, to limit the prohibition to transactions directly related to the municipal advice provided, it would also be less likely that a Remote Business Unit could inadvertently engage in a prohibited transaction.

[4] *See e.g.*, Exchange Act Section 15(g) (requiring registered broker-dealers to establish, maintain and enforce written policies and procedures reasonably designed, taking into consideration the nature of the business, to prevent the misuse of material nonpublic information by the firm or its associated persons in violation of the Exchange Act).

municipal advisor, is prohibited from *knowingly* engaging in a [prohibited][5] principal transaction …"[6]

3. The MSRB Should Carve Out an Exception for Incidental Advice to Brokerage/Securities Execution Services Customers of Fixed-Income Securities

As discussed further below, a number of proposed requirements in Re-Proposed Rule G-42 (such as the requirement to evidence a municipal advisory relationship in a written document and to provide certain disclosures) are highly impractical in the context of ordinary securities or brokerage/securities execution services relationships, where a certain amount of discussion takes place between a broker and his or her clients that may amount to "advice." A corollary to these concerns is that if the principal transaction ban were to extend to this type of informal advice, the ban would potentially exclude or limit the possibility of municipal advisors engaging as principal in securities transactions with municipal entity customers unless the municipal advisor refrained from providing any such informal advice (except where the firm has determined that such advice does not extend to the proceeds of an issue of municipal securities or municipal escrow investments), or execution is effected on an agency basis. Since nearly all transactions in fixed-income securities are effected on a principal basis, the problem is particularly acute with respect to that market.

When a municipal advisor is providing advice on investments incidental to its brokerage/securities execution services activities, rather than advising on a municipal securities offering, the municipal advisor and its affiliates should not be prohibited from transacting as principal.[7] At a minimum, however, there should be an exclusion for transactions in fixed-income securities by broker-dealers whose advice to a municipal entity that would otherwise trigger the ban is limited to providing advice on investments incidental to its brokerage/securities execution services that are not part of a formal mandate or engagement.[8]

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[5] As noted in Section II.A.1 above, SIFMA believes that the prohibition should in any case be clarified to only apply to a transaction directly related to the advice that the municipal advisor provides.

[6] The MSRB has shown sensitivity to the problem of inadvertent violations in proposing Supplementary Material .06 concerning inadvertent advice. Similar considerations are present in this situation, but would not be addressed by Supplementary Material .06 as proposed.

[7] We also observe that the proceeds of municipal securities issuances are generally required to be invested in limited types of assets with limited duration and of high quality, reducing the risks raised by this type of advisory relationship.

[8] We note that a similar consideration gave rise to the SEC promulgating a temporary rule to permit broker-dealers that have non-discretionary advisory accounts to engage in principal transactions in certain fixed-income securities, subject to conditions. *See* Advisers Act Rule 206(3)-3T; Temporary Rule Regarding Principal Trades with Certain Advisory Clients, Advisers Act Release No. 2653 (Sept. 24, 2007) (noting, in particular, the fact that fixed-income securities are generally "traded by firms on a principal (…continued)

We note that, in another context (when providing personalized investment advice to retail customers), the SEC is already considering whether broker-dealers should be subject to a fiduciary duty and related restrictions on principal trading.[9] The SEC has not yet decided either (i) to subject a broker-dealer to a fiduciary duty in such a context, or (ii) if it did, whether the broker-dealer would be permitted to transact with its customer as principal. However, the SEC's most recent request for data on the topic asked commenters to assume for those purposes that "[b]roker-dealers also would continue to be permitted to engage in, and receive compensation from, principal trades," with appropriate disclosure, notwithstanding a fiduciary duty.[10] In light of the SEC's pending consideration of whether a broker-dealer fiduciary duty would prohibit principal transactions and, at least preliminary view that it would not, the MSRB should not at this stage take a more stringent view than the SEC on the question of what a fiduciary duty would entail in regard to limitations on principal transactions, and should clarify in Rule G-42 that advice informally given in the context of ordinary brokerage/securities execution business would not trigger the proposed prohibition on principal transactions.

4. The MSRB Should Clarify the Proposed Exemption for Transactions Complying with MSRB Rule G-23

Supplementary Material .07 notes, in relevant part, that the prohibition on principal transactions "shall not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities, provided that the municipal advisor complies with all of the provisions of Rule G-23." The limitation on the scope of the principal transaction prohibition provided by this section of Supplementary Material .07 is not entirely clear.

Supplementary Material .07 seems to contemplate that, under certain circumstances, Rule G-23 would permit, notwithstanding the general prohibition under Rule G-23(d)(i), a municipal advisor to purchase an issuance of municipal securities from an issuer as principal. SIFMA requests that the MSRB clarify (perhaps by providing pertinent examples) what activity—permissible when conducted in compliance with Rule G-23—the MSRB intends Supplementary Material .07 to permit under Rule G-42(e)(ii).

(continued…)
basis" was one of the factors that led to the promulgation of this rule.) *See* Advisers Act Release No. 2653 at 36-38.

[9] *See, e.g.*, Duties of Brokers, Dealers, and Investment Advisers, Exchange Act Release No. 69013 (Mar. 1, 2013).

[10] *Id.* at 26-27.

5. The MSRB Should Clarify That Investment Vehicles Advised by Municipal Advisors and Their Affiliates are not Themselves Affiliates for Purposes of the Principal Transaction Ban

The MSRB should confirm that an investment vehicle, such as a mutual fund, that is advised by a municipal advisor or its affiliate is not itself an affiliate of the municipal advisor, such that if a municipal advisor recommends that a municipal entity or obligated person invest bond proceeds in the fund, the subsequent sale of the vehicle's shares to the municipal entity by the municipal advisor or an affiliated broker-dealer on an agency basis is not regarded as a principal transaction by an affiliate of that municipal advisor. As an example, mutual funds and other similar vehicles have independent boards, and their affiliates do not have significant equity stakes in the funds that they advise. Therefore, the same types of conflict of interest considerations that generally are raised by principal transactions by a municipal advisor or its corporate affiliates are not present, particularly where the fund has an independent board.

B. Required Disclosures

1. The MSRB Should Exclude Remote Business Units and Other Items From Certain Proposed Disclosure Requirements

Re-Proposed Rule G-42(b)(i)(B) would require municipal advisors to disclose "any affiliate . . . that provides any advice, service, or product to or on behalf of the client that is directly or indirectly related" to the services to be provided.

As noted above, many municipal advisors are part of large, multi-service organizations that have distant and organizationally separate business units that conduct business in the same legal entity as the municipal advisory business and in affiliated entities. While SIFMA does not object to the general principal of disclosure concerning compensation by other business units as a prophylactic measure, Re-Proposed Rule G-42(b)(i)(B) should be revised to exclude compensation of Remote Business Units of the municipal advisor and its affiliates. SIFMA also urges the MSRB to exclude compensation that is immaterial in amount. In addition, the MSRB should either eliminate the term "indirect compensation" or clearly define the term.

2. Municipal Advisors and Their Affiliates Should Not Have Disclosure Obligations to Investors

Supplementary Material .08 to Re-Proposed Rule G-42 would require that, where an affiliate of a municipal advisor prepared any material that is included, in whole or part, in an official statement, the municipal advisor must provide written disclosure to investors (which may be in the Official Statement) if any of its affiliates provided services that are directly or indirectly related to its municipal advisory activities. This disclosure requirement would also be deemed satisfied if the relevant affiliate provides

the written disclosure to investors. Mandating the municipal advisor or its affiliates to provide such disclosure is inappropriate and impractical, and the MSRB should eliminate this proposed requirement.

Municipal advisors and their affiliates may have no contractual or other relationships (and in many cases have no form of privity) with investors, nor do they control the content of the Official Statement. Rather, it is the obligation of the issuer under federal securities laws and other applicable law to make sure that its disclosure is materially accurate and complete and the responsibility of broker-dealers to comply with their obligations under applicable law. A municipal advisor may be engaged to advise and assist an issuer in connection with the preparation of the issuer's disclosure—but it remains the issuer's disclosure, not the municipal advisor's. Re-Proposed Rule G-42(b)(i)(B) would already otherwise require that municipal advisors provide this same conflict information to the issuer; with the information in the issuer's possession, the MSRB should leave it to the issuer to determine whether or not such information is material to investors and warrant disclosure.

C. Specified Prohibitions

1. Affiliates of Municipal Advisors Should Not Be Prohibited from Receiving Certain Payments to Obtain or Retain Municipal Advisory Business

Re-Proposed Rule G-42(e)(i)(E) would prohibit "payments made for the purpose of obtaining or retaining municipal advisory business" except for reasonable fees paid to another registered municipal advisor. As SIFMA previously commented, the rule should be modified to permit payments to affiliates in preparing responses to RFPs or RFQs, normal business entertainment expenses, and other unobjectionable expenditures made in the ordinary course of marketing and sales activities.

2. If Properly Disclosed, Fee-Splitting Arrangements with Affiliates Should Be Permitted

Re-Proposed Rule G-42(e)(i)(E) would prohibit "making, or participating in, any fee-splitting arrangements with underwriters on any municipal securities transaction for which it is acting as municipal advisor, and any undisclosed fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client of the municipal advisor." If properly disclosed, fee-splitting arrangements to affiliates of a municipal advisor should not be prohibited. There may be legitimate reasons for fee-splitting arrangements, including fee structures requested by clients of an affiliate. If a client receives full and fair disclosure regarding the arrangements and any conflicts of interest it may entail, the parties should be free to agree to the fee arrangement that it believes is most economical and efficient under the circumstances.

D. Documentation of Municipal Advisory Relationship

1. The MSRB Should Not Require Written Documentation of a Municipal Advisory Relationship in the Case of Brokerage/Securities Execution Services

Re-Proposed Rule G-42(c) requires that a "municipal advisor must evidence each of its municipal advisory relationships by a writing entered into prior to, upon or promptly after the establishment of the municipal advisory relationship" and include a number of elements related to the municipal advisory relationship, including, among others, the (i) form and basis of direct or indirect compensation; (ii) information required to be disclosed under Re-Proposed Rule G-42(b); and (iii) the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement. Re-Proposed Rule G-42(f)(vi) notes that a "municipal advisory relationship" is "deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for or on behalf of a municipal entity or obligated person."

The requirement to evidence a municipal advisory relationship in a written document and to provide certain disclosures are highly impractical in the context of ordinary securities or brokerage/securities execution services relationships, where a certain amount of discussion takes place between a broker and its clients that may amount to "advice" and given the potentially significant number of transactions involved and timing considerations. Moreover, according to common industry-wide practice, a municipal advisor would not "enter into an agreement to engage in municipal advisory services" when providing incidental brokerage/securities execution services.

Therefore, the MSRB should clarify that informal advice that is incidental to providing brokerage/securities would not, alone, trigger a written documentation requirement under Re-Proposed Rule G-42(c), since there would be no "municipal advisory relationship." Similarly, the MSRB should clarify that the disclosure requirements under Re-Proposed Rule G-42(b) also would not be required for the same reasons.[11]

[11] We note that there are other contexts in which minor or incidental municipal advisory services, outside the context of a municipal securities transactions, should not trigger the full proposed documentation requirements. For example, a municipal entity that previously issued municipal securities may contact a firm, on a very informal telephone basis, seeking its view of the materiality of an event and whether disclosure would be required. While providing this type of advice could constitute municipal advisory activities, it would be impractical (and indeed prohibitive) to require that such informal and relatively short-lived relationship be fully documented in accordance with Re-Proposed Rule G-42(c).

2. The MSRB Should Not Require Specific Disclosure of the Legal and Disciplinary Events That Are Already Listed in Forms MA and MA-I

Re-Proposed Rule G-42(b)(ii) would require a municipal advisor to disclose to clients legal or disciplinary events that are "material to the client's evaluation or integrity of its management or advisory personnel." While the MSRB helpfully revised certain of the disclosure requirements related to a municipal advisor's legal or disciplinary history contained in Re-Proposed Rule G-42(c), requiring in Re-Proposed Rule G-42(b)(ii) duplicate disclosure of specific events that are already disclosed in Forms MA and MA-I provides little, if any, benefit to municipal entities or obligated persons, while it imposes unnecessary additional burdens on municipal advisors. A municipal advisor is also not in the position to determine the manner in which a client evaluates potential municipal advisors or how a client may view the integrity of the advisor's personnel. Providing clients and prospective clients with the information in relevant agreements regarding how to obtain electronic access to a municipal advisor's legal and disciplinary history on Forms MA and MA-I should sufficiently achieve the MSRB's goal of providing clients with access to the municipal advisor's legal and disciplinary history.

Further, the MSRB should remove the requirement in Re-Proposed Rule G-42(c)(iv), which would require municipal advisors to document the date of the last material change to a legal or disciplinary event on Form MA or MA-I. As a result, municipal advisors would need to update their written disclosures and documentation with each of their municipal advisory clients whenever a material change to a legal or disciplinary event was made to Form MA or MA-I. This requirement to continuously update form documents would be burdensome and effectively be a technical "trap for the unwary" for municipal advisors, but would provide little benefit to clients.

3. The MSRB Should Define "Indirect Compensation"

Re-Proposed Rule G-42(c)(i) would require municipal advisors to include in their relationship documentation "the form and basis of direct and indirect compensation" for the services. As noted above, the MSRB should clarify what it believes would need to be included within the form and basis of "indirect" compensation. While it is customary to set out the form and basis of direct compensation in engagement documentation, it is not clear what indirect compensation must be disclosed.

4. The MSRB Should Limit Required Conflict Disclosure to Those Conflicts That Could Reasonably Impair Fiduciary Standard of Advice or Conduct

Re-Proposed Rule G-42(b)(i)(A) would require disclosure of "any . . . potential conflicts of interest . . . that might impair" a municipal advisor's advice or its ability to act as a fiduciary. If this requirement is retained, it should be limited to conflicts "that could reasonably be anticipated to impair" such matters.

5. The MSRB Should Clarify the Application of the Documentation and Disclosure Requirements to Existing Relationships

Re-Proposed Rule G-42(c) requires certain relationship documentation be entered into "upon or promptly after the establishment of" a municipal advisory relationship" and Re-Proposed Rule G-42(b) would require certain disclosures be provided "upon or prior to engaging in municipal advisory activities."

Municipal advisors will likely have existing ongoing municipal advisory relationships in place (in some cases documented in accordance with Rule G-23) at the time Rule G-42 is ultimately approved by the SEC and becomes effective. Re-documenting these existing relationships may be overly burdensome both for municipal advisors and clients. In addition, as the relationships are already in existence, new disclosures will likely not impact the client's decision to engage the municipal advisor. The MSRB should therefore limit the extent to which existing ongoing relationships would need to be re-documented and new disclosures provided.

E. Municipal Advisor Standards of Conduct

1. The MSRB Should Clarify Duty of Care As Applied to Brokerage/Securities Execution Services

As noted in Sections II.A.3 and II.D.1 above, the application of certain aspects of Re-Proposed Rule G-42 to advice to municipal entities in the brokerage/securities execution services context are impractical or unclear. For example, proposed Supplementary Material .01 would require that a municipal advisor make a reasonable inquiry regarding the facts that are relevant to a client's determination to pursue a particular course of action. While this requirement may be appropriate in the context of arranging a municipal securities issuance, it could be prohibitive in the case of ordinary brokerage and related advice, given the number of trades potentially involved, timing considerations and the general context of broker-related advice. SIFMA does not believe that such a standard should be applied in addition to otherwise applicable suitability requirements that would attach to recommendations made in the context of brokerage/securities execution services.

2. The MSRB Should Expand Supplementary Material .06 to Include in its Scope the Prohibition on Principal Transactions and Other Requirements Under Re-Proposed Rule G-42

Supplementary Material .06 of Re-Proposed Rule G-42 helpfully provides a limited and conditional safe harbor for inadvertent advice and specifies the steps that may be taken if a party inadvertently engaged in municipal advisory activities does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship and elects to seek a safe harbor from the requirements of sections (b) and (c)

of Re-Proposed Rule G-42 relating to disclosure of conflicts of interest and documentation of the municipal advisory relationship.

While Supplementary Material .06 would protect a municipal advisor from the disclosure and documentation requirements of Re-Proposed Rule G-42, it would not protect municipal advisors from other requirements under Re-Proposed Rule G-42, such as the principal transaction prohibition under Re-Proposed Rule G-42(e)(ii). Without explicitly including a safe harbor for providing inadvertent advice from the prohibition on principal transactions, it is unlikely that firms will go through the process that is required under Supplementary Material .06, given that retracting the inadvertent advice will not permit the municipal advisor to engage in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing advice.

Moreover, the MSRB should extend the safe harbor under Supplementary Material .06 so that a municipal advisor would also not be required to comply with the requirements related to making recommendations and reviewing third party recommendations under Re-Proposed Rule G-42(d) if it inadvertently provided advice to a municipal entity or obligated person. Without explicitly including a safe harbor for providing inadvertent advice from the requirement to recommend and review third party recommendations, municipal advisors will still be required to undergo a detailed suitability analysis and investigate or consider other reasonably feasible alternatives with respect to the municipal financial product or municipal securities transaction to which the municipal advisor inadvertently provided such advice.

We therefore believe that Supplementary Material .06 should be revised as follows: "A municipal advisor is not required to comply with sections (b), *(c), (d) and (e)(ii)* of this rule if the advisor meets all of the following requirements."

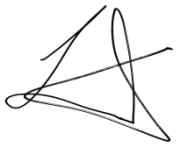
3. The MSRB Should Clarify the Required Disclaimer Under Proposed Supplementary Material .06

In order for a municipal advisor to avail itself of the safe harbor for inadvertent advice under proposed Supplementary Material .06, condition (A) would require that the municipal advisor provide "a disclaimer that the advisor did not intend to provide advice and that, effective immediately, it has ceased engaging in municipal advisory activities." A firm may be a registered municipal advisor engaged in municipal advisory activities for some clients, but inadvertently provided advice to another client. As a result, it could not state that it "has ceased engaging in municipal advisory activities." Rather, the MSRB should clarify that a municipal advisor need not cease *all* municipal advisory activities, but rather those undertaken for the particular client in relation to a particular matter. Specifically, condition (A) could be modified as follows: "a disclaimer that the advisor did not intend to provide advice and that, effective immediately, it has ceased engaging in municipal advisory activities *with respect to that municipal entity or obligated person in regard to the matter on which advice was inadvertently provided*."

* * *

Please do not hesitate to contact me at (212) 313-1130, or our counsel, Lanny A. Schwartz of Davis Polk & Wardwell LLP, at (212) 450-4174 with any questions.

Sincerely yours,



Leslie M. Norwood
Managing Director and
Associate General Counsel

cc: Lynnette Kelly, Executive Director, MSRB
Michael L. Post, Deputy General Counsel, MSRB
John Cross, Director, Office of Municipal Securities, SEC

SMA
Southern Municipal Advisors, Inc.

August 25, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314.

Re: Request for Comment on Revised Draft MSRB Rule 42

Dear Mr. Smith:

Southern Municipal Advisors, Inc. ("SMA") is a woman owned business enterprise specializing exclusively in providing independent financial advisory services to governmental entities. SMA does not participate in the underwriting or selling of municipal securities. SMA serves as an independent financial advisor to governmental entities including municipalities, counties, public authorities and districts. SMA professionals have combined over 60 years experience in public finance throughout the Southeast, in general, and in South Carolina, in particular. It is based upon this experience that the following thoughts regarding Revised Draft MSRB Rule 42 are offered for your consideration.

The Initial and the Revised Draft Rules require in G-42(d) that a municipal advisor must not recommend a municipal securities transaction or financial product unless the advisor "has a reasonable basis for believing that the transaction or product is suitable for the client[.]" (sometimes referred to as the "suitability finding"). We wish to provide two comments regarding this requirement. The first relates to the facts and circumstances the advisor will be permitted to rely upon for having a reasonable basis for believing the transaction or product is reasonable. The second relates to the need to clarify that the suitability finding is based solely upon the facts and circumstances at the time it is made and is limited thereto.

(1) Often it is the client, not the advisor, who initiates a transaction. For instance, the policy making authority (Council or Manager) may determine it is in the municipality's best interest to provide additional administrative or educational facilities. Similarly, a municipality may determine it needs to expand or upgrade its water and or wastewater system either due to population increases or regulatory demands. It may be that as a result of a public referendum, a municipality must proceed with a financing in order to address the will of its citizens. Once these determinations are made, the advisor is then involved to assist in planning for and implementing whatever financing is necessary to accomplish the goals.

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E-mail smafla@bellsouth.net

In many cases the financing options are limited by state law, as determined either by the municipality's counsel or bond counsel. In effect, suitability has already been determined by the state legislature and the municipality is merely choosing among the statutorily permitted options.

Further, most municipal policy makers are familiar with all manner of financial instruments permitted by state law – general obligation bonds, revenue bonds, certificates of participation, master leases, and refunding of all of these, as well as bond/tax/grant anticipation notes to name those most often employed. Most, if not all, municipal entities of any size have used all or some of the above listed approaches in the past and will in all likelihood continue to do so to fund their capital and cash flow needs. These are "plain vanilla" transactions familiar to all public officials responsible for capital improvement programs.

Most of the facts or circumstances upon which a suitability determination must be based according to Supplementary Material 09 of the Revised Draft Rules are currently provided for in closing documents prepared by bond counsel. Among material facts provided in closing documents are:

- the issuer's historical financial statements;
- borrowing needs and historical debt;
- issuer's objectives specifically expressed in the resolutions/ordinances publicly voted on by the authorizing policy body;
- the fact all laws and regulations precedent to the issuance of the particular debt have been satisfied;
- projections which demonstrate the associated debt service and coverage requirements, if any, will be satisfied, along with any prior debt; and,
- in the case of general obligation bonds, certification that state requirements limiting the issuance of such debt are satisfied.

Where a transaction (a) is related to a project or event determined by the governing body of the municipal entity or its citizens to be in its interest and consistent with its goals; (b) is permitted by state statute as determined by municipal or bond counsel; and, (c) involves one which the municipality has employed in the past, then it seems suitability has been determined and the advisor ought to be able to rely on these facts and the closing documents as establishing a reasonable basis for suitability. The advisor ought not be put in the position of substituting its judgment as to suitability for that of the municipal policy makers, citizens or state lawmakers.

In contrast to the above, if a municipality were to decide to enter into a swap arrangement for instance in connection with the revenue bond issued to finance a water or wastewater system upgrade, then an investigation into suitability would be in order. This "add on" to a traditional financial arrangement clearly calls for a suitability determination.

(2) The regulations ought to make clear that the suitability finding relates only to the facts and circumstances as they exist at the time the client enters into the transaction. Should those facts and circumstances change over the course of time the advisor should not be subject to censure or criticism if, under future facts and circumstances, the transaction might be seen as unsuitable.

Nor should there be perceived to be a continuing responsibility imposed upon the advisor to update the suitability finding. It is made at a very specific point in time and it would be burdensome to require that the advisor monitor the client's activities with respect to a completed transaction and adjust the suitability finding if necessary. New factors may arise or emerge from time to time and it is not possible for the advisor to predict how such future factors may impact any specific suitability finding. It is the advisor's responsibility to be as informed as possible regarding the client's financial condition in anticipation of future transactions; however, this responsibility does extend to past transactions.

We recognize the difficulties and challenges the MSRB faces in implementing Dodd-Frank Act and appreciate that the MSRB has reached out to municipal advisors as it crafts the regulatory framework. I hope that you will consider these comments.

Sincerely,

Michael C. Cawley

Michael C. Cawley
Senior Consultant

MCC:nn

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August 25, 2014

Via online at http://www.msrb.org/CommentForm.aspx

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314

RE: MSRB Notice 2014-12 Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Smith:

Wells Fargo Advisors, LLC ("WFA") appreciates the opportunity to comment on the Municipal Securities Rulemaking Board's ("MSRB" or "the Board") Revised Draft Rule G-42, on Duties of Non-Solicitor Municipal Advisors ("Draft Rule G-42").[1] WFA commends the Board for its continued efforts to elaborate on the duties of municipal advisors and appreciates its consideration of comments received on the initial proposal and subsequent modifications reflected in Revised Draft Rule G-42.

WFA consists of brokerage operations that administer almost $1.4 trillion in client assets. It employs approximately 15,189 full-service financial advisors in branch offices in all 50 states and 3,472 licensed financial specialists in retail bank branches across the United States. [2] WFA offers a range of fixed income solutions, including municipal securities, to its clients.

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[1] MSRB Notice 2014-12 Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors, July 23, 2014, http://www.msrb.org/~/media/Files/Regulatory-Notices/RFCs/2014-12.ashx?n=1.

[2] WFA is a non-bank affiliate of Wells Fargo & Company ("Wells Fargo"), a diversified financial services company providing banking, insurance, investments, mortgage, and consumer and commercial finance across the United States of America and internationally. Wells Fargo has 275,000 team members across more than 80 businesses. Wells Fargo's brokerage affiliates also include Wells Fargo Advisors Financial Network, LLC ("WFAFN") and First Clearing, LLC, which provides clearing services to 77 correspondent clients, WFA and WFAFN. For ease of discussion, this letter will use WFA to refer to all of those brokerage operations.

WFA appreciates the Board's consideration of earlier comments regarding the potential breadth of the principal transaction prohibition, but remains concerned that the prohibition will have unintended consequences for certain affiliate transactions. Although WFA is not a municipal advisor, it offers this brief comment to reiterate its view that the principal trading prohibition should not apply to municipal advisor affiliates.[3]

Rule G-42 Should Not Prohibit Principal Transactions by Affiliates of a Municipal Advisor.

Revised Draft Rule G-42 clarifies that an affiliate of a municipal advisor to a municipal entity client is prohibited from "engaging in a principal transaction directly related to the same municipal transaction or financial product as to which the municipal advisor is providing advice." [4] Although this modification mitigates the impact of such prohibition by narrowing the application to a transaction for which the municipal advisor is engaged, WFA believes the prohibition could still cover certain non-municipal advisor transactions resulting in fewer choices for municipal entity clients.

Large financial institutions, such as Wells Fargo, may have numerous affiliates conducting business with municipal entities. Affiliates of large financial institutions often offer substantially different services, operate with distinct governance structures and employ information barriers. If, based on such factors, a non-municipal advisor affiliate is not connected to the municipal advisor relationship, the risk of a conflict of interest in a principal transaction between a municipal advisor client and the non-municipal advisor affiliate is significantly diminished.

Despite the MSRB's attempt to narrow the application of the principal trading prohibition, WFA is concerned that certain affiliate transactions could still be implicated by the rule. This may be true even in instances where a non-municipal advisor affiliate is unaware of the existence of a municipal advisory engagement between a municipal entity and the municipal advisor.

For example, a municipal advisor may engage with a municipal entity to provide advice relating to the investment of proceeds. Due to information barriers and separate governance structures, non-municipal advisor affiliates may be unaware of the existence of such a municipal advisory relationship. That same municipal entity client, however, may have an existing relationship with a separate, non-municipal advisor broker-dealer affiliate. Consistent with SEC staff guidance, the non-municipal advisor broker-dealer affiliate could provide the municipal entity client "information regarding a financial institution's currently-available investments (e.g., the terms, maturities and interest rates at which the financial institution offers these investments)" in response to the same municipal entity's inquiry about investment alternatives for those proceeds.[5]

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[3] *See* Correspondence from Robert J. McCarthy to Ronald W. Smith, dated March 10, 2014, regarding MSRB 2014-01 Request for Comment on Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors, http://www.msrb.org/RFC/2014-01/WellsFargo.pdf

[4] Notice at 14.

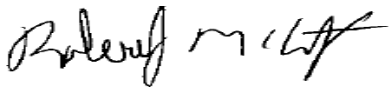
[5] SEC Registration of Municipal Advisors, Frequently Asked Questions, updated May, 19, 2014, http://www.sec.gov/info/municipal/mun-advisors-faqs.shtml

If a transaction were to arise out of this activity, which is permissible under the general information exclusion from the advice provision of the SEC Municipal Advisor rule, the non-municipal advisor affiliate would be in violation of the principal transaction prohibition. This would be true despite the fact that the non-municipal advisor affiliate is unaware of the existence of the municipal advisor's relationship with the municipal entity client regarding the same transaction. Consequently, the effect of the principal prohibition will be to discourage non-municipal advisor broker-dealers affiliated with a municipal advisor from continuing to conduct business with municipal entity clients to avoid the risk of an inadvertent violation. Accordingly, WFA believes the MSRB should exempt municipal advisor affiliates operating with information barriers from the principal transaction prohibition.

CONCLUSION

WFA appreciates the opportunity to share its views regarding the duties of non-solicitor municipal advisors and applauds the Board's effort to tailor the application of the proposed rule's principal transaction prohibition. For the foregoing reasons, WFA respectfully requests that MSRB revisit the principal trading prohibition to remove the restriction for affiliates of a municipal advisor when information barriers are present. If you would like to further discuss WFA's position on this matter, please do not hesitate to contact me.

Sincerely,



Robert J. McCarthy
Director of Regulatory Policy

WM Financial Strategies

11710 ADMINISTRATION DRIVE
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ST. LOUIS, MISSOURI 63146
(314) 423-2122

August 25, 2014

Municipal Securities Rulemaking Board
Attention: Ronald W. Smith
Corporate Secretary
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Request for Comments to Draft Rule G-42

Ladies and Gentlemen:

I am a sole proprietor doing business as WM Financial Strategies. I have a career devoted entirely to public finance and have been an independent financial advisor (now known as a Municipal Advisor) since 1989. In my capacity as an independent Municipal Advisor, I am writing to set forth my comments relating to the Municipal Securities Rulemaking Board's Draft Rule G-42.

In general, I appreciate the changes made to the first version of the rule; however, some provisions continue to concern me as noted below:

1. Draft Rule G-42 Imposes Excessive Burdens on Municipal Advisors

Draft Rule G-42 includes "Supplementary Material: .01 Duty of Care" which requires a municipal advisor to "undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information." I concur that a municipal advisor should make a reasonable investigation in order that recommendations reflect a municipal securities transaction or municipal financial product that the advisor reasonably believes is in the client's best interest. The investigation should include a review of budgets, audits, other publicly available documentation (when appropriate), and discussions with the client. However, a financial advisor should not be required to determine whether the information provided to it by the municipal entity is "materially inaccurate or incomplete." The municipal advisor should be able to rely on publicly available documents as being true and accurate and should be able to assume that any additional information provided to it by the municipal entity is also true and accurate.

2. Draft Rule G-42 Negates Rule G-23 and the Intent of SEC's Definition of Municipal Advisor

Draft Rule G-42 includes "Supplementary Material: .06 Inadvertent Advice" which creates a loophole that will allow broker-dealers to serve as financial advisors (without a fiduciary duty) and then switch to serving as an underwriter by claiming that such advice was inadvertent. This loophole negates the current Rule G-23 and allows broker-dealers to effectively serve as a financial advisor and then switch to serving as an underwriter. As written, the draft Rule G-42 permits a return to the historical bad business practice that created conflicts of interest that were not in the issuers' best interest. The

proposed provision blurs the lines between the roles of financial advisors and underwriters and undermines the definition of Municipal Advisor and the exemptions provided by the SEC.

3. Contingent Fees that are based on the completion of a transaction, but not on the size of a transaction, are not a conflict of interest

Just as a particular bond structure should reflect the municipal entity's best interest, so should the fee arrangement selected. Unlike underwriters that must disclose their contingent fee arrangements, a Municipal Advisor is required to act in the best interest of their clients. Accordingly good advice will prevent a fee arrangement from creating a "conflict."

Financial advisors are often engaged to structure and arrange the sale of municipal securities **after** a determination has already been made by the municipality to issue securities to finance a specific capital project (e.g. voters have approved general obligation bonds). Municipal issuers rely on the expertise of their financial advisor to develop marketable bond structures and to actively locate broker-dealers willing to underwrite the issue. A conflict of interest does not exist when payment of fees is based on the success of services to be provided (the sale of securities is completed). Should a financial advisor be compensated when it fails to successfully provide the services for which it was engaged?

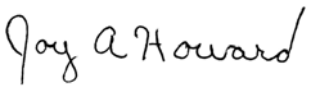
Furthermore, many municipal entities are small with limited budgets. Costs of issuance, including financial advisory fees, are to be paid from the proceeds of the securities. If the issue is not successfully completed, payment of fees would have an adverse effect on these entity's operating budget. Contingent fee arrangements benefit Municipal Entities by insuring that their governmental funds will not be drawn upon for payment of fees if the transaction is not completed.

Based on the foregoing, the MSRB should not require a "conflict of interest" disclosure of fee arrangements that do not inherently create conflicts of interest.

4. Summary

I appreciate many of the changes made by the MSRB to the first draft of Rule G-42 and respectfully request that the MSRB further modify the draft Rule G-42 as described herein.

Sincerely,



Joy A. Howard
Principal

ZIONS BANK

August 25, 2014

Mr. Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors: MSRB Regulatory Notice 2014-12

Dear Mr. Smith:

Zions First National Bank ("Zions Bank") appreciates this opportunity to provide comments to the Municipal Securities Rulemaking Board ("MSRB") pertaining to revised draft Rule G-42 regarding enhanced standards of conduct and duties of municipal advisors when engaged in municipal advisory activities (the "Re-proposed Rule"). We would like to focus our comments on the prohibition contained in the Re-proposed Rule against principal transactions between municipal entities and their municipal advisors and transitional provisions for the implementation of the Re-proposed Rule.

We recognize that the purpose of imposing a fiduciary duty on municipal advisors is to ensure that municipal entities are adequately served and represented by their advisors. We believe that such a standard is satisfied in situations where (1) the municipal advisor provides full disclosure of the nature of its arm's-length role in the principal transaction prior to the time that the municipal entity agrees to engage in the principal transaction; and (2) the municipal entity consents to engaging in the principal transaction. Similarly, we note that registered investment advisers ("RIAs") are permitted to engage in principal transactions with disclosure to and consent by their advisory clients and that bank fiduciaries are, in certain situations, permitted to engage in principal transactions with their fiduciary clients. We would suggest that the disclosure and consent model applicable to RIAs be adopted regarding principal transactions between municipal advisors or their affiliates and the clients of the municipal advisors.

We also urge the MSRB to provide a transitional provision in the Re-proposed Rule to permit advisors to honor their existing financial advisory agreements with advised clients. Many of these agreements are multi-year contracts. Many financial advisory firms have a large number of existing financial advisory agreements, and a significant amount of time and expense would be required to supplement or amend these agreements with the additional content and disclosures required by paragraph (c) of the Re-proposed Rule. In addition, municipal entities may conclude under the particular state and/or local procurement laws applicable to them that an amendment to an existing municipal advisory agreement made to comply with provisions of the Re-proposed Rule might require the reopening of the request for proposal process for issuers to hire municipal advisors. Such a process could require a significant amount of time, effort and expense for

municipal advisors and their clients to implement, sometimes requiring publications of public notices and public hearings.

Accordingly, we ask the MSRB to allow firms to continue to operate under existing advisory agreements until they expire and then to enter into new agreements that meet all of the Rule G-42 requirements. We would propose that the MSRB allow firms to continue to operate under existing advisory agreements until they expire and then to enter into new agreements that meet all of the Rule G-42 requirements. As part of such a transition, municipal advisors could provide to their advisory clients, within a reasonable period of time such as sixty days after the effective date of a final rule, appropriate disclosures of material conflicts and disciplinary actions required by the Re-proposed Rule. Other than such disclosures, we believe that contracts in place on the effective date of a final rule should be honored and allowed to run their course until termination in accordance with their terms, whereupon the required contractual provisions of the Re-proposed Rule would be required in all new municipal advisory agreements between the parties.

We believe our position on these matters would be beneficial to all interested parties and we would welcome an opportunity to discuss these issues further. We hope our comments will provide additional context and insight into an important and challenging issue.

If you have any questions concerning this letter or would like to discuss these observations further, please feel free to contact Gary Hansen at Zions First National Bank, Investment Division, One South Main, 17th Floor, Salt Lake City, Utah 84133; Telephone: 801-844-7762; E-Mail: Gary.Hansen@zionsbank.com.

Very truly yours,

ZIONS FIRST NATIONAL BANK

By _____
W. David Hemingway
Executive Vice President

EXHIBIT 5

Rule G-42: Duties of Non-Solicitor Municipal Advisors

(a) *Standards of Conduct*.

(i) A municipal advisor to an obligated person client shall, in the conduct of all municipal advisory activities for that client, be subject to a duty of care.

(ii) A municipal advisor to a municipal entity client shall, in the conduct of all municipal advisory activities for that client, be subject to a fiduciary duty that includes, without limitation, a duty of loyalty and a duty of care.

(b) *Disclosure of Conflicts of Interest and Other Information*. A municipal advisor must, prior to or upon engaging in municipal advisory activities, provide to the municipal entity or obligated person client full and fair disclosure in writing of:

(i) all material conflicts of interest, including:

(A) any actual or potential conflicts of interest of which it is aware after reasonable inquiry that could reasonably be anticipated to impair its ability to provide advice to or on behalf of the client in accordance with the standards of conduct of section (a) of this rule, as applicable;

(B) any affiliate of the municipal advisor that provides any advice, service, or product to or on behalf of the client that is directly related to the municipal advisory activities to be performed by the disclosing municipal advisor;

(C) any payments made by the municipal advisor, directly or indirectly, to obtain or retain an engagement to perform municipal advisory activities for the client;

(D) any payments received by the municipal advisor from a third party to enlist the municipal advisor's recommendation to the client of its services, any municipal securities transaction or any municipal financial product;

(E) any fee-splitting arrangements involving the municipal advisor and any provider of investments or services to the client;

(F) any conflicts of interest arising from compensation for municipal advisory activities to be performed that is contingent on the size or closing of any transaction as to which the municipal advisor is providing advice; and

(G) any other engagements or relationships of the municipal advisor that could reasonably be anticipated to impair the municipal advisor's ability to provide advice to or

on behalf of the client in accordance with the standards of conduct of section (a) of this rule, as applicable.

If a municipal advisor concludes that it has no known material conflicts of interest based on the exercise of reasonable diligence by the municipal advisor, the municipal advisor must provide a written statement to the client to that effect.

(ii) any legal or disciplinary event that is material to the client's evaluation of the municipal advisor or the integrity of its management or advisory personnel.

Information regarding legal or disciplinary events may be disclosed for purposes of this subsection by identification of the specific type of event and specific reference to the relevant portions of the municipal advisor's most recent Forms MA or MA-I filed with the Commission if the municipal advisor provides detailed information specifying where the client may electronically access such forms.

(c) *Documentation of Municipal Advisory Relationship*. A municipal advisor must evidence each of its municipal advisory relationships by a writing or writings created and delivered to the municipal entity or obligated person client prior to, upon or promptly after the establishment of the municipal advisory relationship. The writing(s) must be dated and include, at a minimum,

(i) the form and basis of direct or indirect compensation, if any, for the municipal advisory activities to be performed;

(ii) the information required to be disclosed by section (b) of this rule;

(iii) a description of the specific type of information regarding legal and disciplinary events requested by the Commission on Form MA and Form MA-I, which includes information about any criminal actions, regulatory actions, investigations, terminations, judgments, liens, civil judicial actions, customer complaints, arbitrations and civil litigation, and detailed information specifying where the client may electronically access the municipal advisor's most recent Form MA and each most recent Form MA-I filed with the Commission;

(iv) the date of the last material change or addition to the legal or disciplinary event disclosures on any Form MA or Form MA-I filed with the Commission by the municipal advisor;

(v) the scope of the municipal advisory activities to be performed and any limitations on the scope of the engagement;

(vi) the date, triggering event, or means for the termination of the municipal advisory relationship, or, if none, a statement that there is none; and

(vii) any terms relating to withdrawal from the municipal advisory relationship.

During the term of the municipal advisory relationship, the writing(s) must be promptly amended or supplemented to reflect any material changes or additions, and the amended writing(s) or supplement must be promptly delivered to the client. This amendment and supplementation requirement applies to any changes and additions that are discovered, or should have been discovered, based on the exercise of reasonable diligence by the municipal advisor.

(d) *Recommendations and Review of Recommendations of Other Parties*. If a municipal advisor makes a recommendation of a municipal securities transaction or municipal financial product to a municipal entity or obligated person client, or if the review of a recommendation of another party is requested by the municipal entity or obligated person client and within the scope of the engagement, the municipal advisor must determine, based on the information obtained through the reasonable diligence of such municipal advisor, whether the municipal securities transaction or municipal financial product is suitable for the client. In addition, the municipal advisor must inform the client of:

(i) the municipal advisor's evaluation of the material risks, potential benefits, structure, and other characteristics of the recommended municipal securities transaction or municipal financial product;

(ii) the basis upon which the municipal advisor reasonably believes that the recommended municipal securities transaction or municipal financial product is, or is not, suitable for the client; and

(iii) whether the municipal advisor has investigated or considered other reasonably feasible alternatives to the recommended municipal securities transaction or municipal financial product that might also or alternatively serve the client's objectives.

(e) *Specified Prohibitions*.

(i) A municipal advisor is prohibited from:

(A) receiving compensation that is excessive in relation to the municipal advisory activities actually performed;

(B) delivering an invoice for fees or expenses for municipal advisory activities that do not accurately reflect the activities actually performed or the personnel that actually performed those activities;

(C) making any representation or the submission of any information that the municipal advisor knows or should know is either materially false or materially misleading due to the omission of a material fact about the capacity, resources or knowledge of the municipal advisor, in response to requests for proposals or qualifications or in oral presentations to a client or prospective client, for the purpose of obtaining or retaining an engagement to perform municipal advisory activities;

(D) making, or participating in, any fee-splitting arrangement with underwriters on any municipal securities transaction as to which it has provided or is providing advice, and any undisclosed fee-splitting arrangements with providers of investments or services to a municipal entity or obligated person client of the municipal advisor; and

(E) making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities other than: (1) payments to an affiliate of the municipal advisor for a direct or indirect communication with a municipal entity or obligated person on behalf of the municipal advisor where such communication is made for the purpose of obtaining or retaining an engagement to perform municipal advisory activities; (2) reasonable fees paid to another municipal advisor registered as such with the Commission and the Board for making such a communication as described in subparagraph (e)(i)(E)(1); and (3) payments that are permissible "normal business dealings" as described in Rule G-20.

(ii) A municipal advisor to a municipal entity client, and any affiliate of such municipal advisor, is prohibited from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice.

(f) *Definitions*.

(i) "Engaging in a principal transaction" shall mean, for purposes of this rule, when acting as principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client.

(ii) "Advice" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(4)(A)(i) of the Act, 17 CFR 240.15Ba1-1(d)(1)(ii) and other rules and regulations thereunder.

(iii) "Affiliate of the municipal advisor" shall mean, for purposes of this rule, any person directly or indirectly controlling, controlled by, or under common control with such municipal advisor.

(iv) "Municipal advisor" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(4) of the Act, 17 CFR 240.15Ba1-1(d)(1)-(4) and other rules and regulations thereunder; provided that it shall exclude a person that is otherwise a municipal advisor solely based on activities within the meaning of Section 15B(e)(4)(A)(ii) of the Act and rules and regulations thereunder or any solicitation of a municipal entity or obligated person within the meaning of Section 15B(e)(9) of the Act and rules and regulations thereunder.

(v) "Municipal advisory activities" shall, for purposes of this rule, mean those activities that would cause a person to be a municipal advisor as defined in subsection (f)(iv) of this rule.

(vi) A "municipal advisory relationship" shall, for purposes of this rule, be deemed to exist when a municipal advisor enters into an agreement to engage in municipal advisory activities for a municipal entity or obligated person. The municipal advisory relationship shall be deemed to have ended on the date which is the earlier of (i) the date on which the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship required in section (c) of this rule or (ii) the date on which the municipal advisor withdraws from the municipal advisory relationship.

(vii) "Municipal entity" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(8) of the Act, 17 CFR 240.15Ba1-1(g) and other rules and regulations thereunder.

(viii) "Obligated person" shall, for purposes of this rule, have the same meaning as in Section 15B(e)(10) of the Act, 17 CFR 240.15Ba1-1(k) and other rules and regulations thereunder.

(ix) "Official statement" shall, for purposes of this rule, have the same meaning as in Rule G-32(d)(vii).

---Supplementary Material:

.01 Duty of Care. Municipal advisors must exercise due care in performing their municipal advisory activities. The duty of care includes, but is not limited to, the obligations discussed in this paragraph. A municipal advisor must possess the degree of knowledge and expertise needed to provide the municipal entity or obligated person client with informed advice. A municipal advisor also must make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client. A municipal advisor must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. Among other matters, a municipal advisor must have a reasonable basis for:

(a) any advice provided to or on behalf of a client;

(b) any representations made in a certificate that it signs that will be reasonably foreseeably relied upon by the client, any other party involved in the municipal securities transaction or municipal financial product, or investors in the municipal entity client's securities or securities secured by payments from an obligated person client; and

(c) any information provided to the client or other parties involved in the municipal securities transaction in connection with the preparation of an official statement for any issue of municipal securities as to which the municipal advisor is advising.

.02 Duty of Loyalty. Municipal advisors must fulfill a duty of loyalty in performing their municipal advisory activities for municipal entity clients. The duty of loyalty includes, but is not limited to, the obligations discussed in this paragraph. A municipal advisor must deal honestly and with the utmost good faith with a municipal entity client and act in the client's best interests without regard to the financial or other interests of the municipal advisor. A municipal advisor must not engage in municipal advisory activities for a municipal entity client if it cannot manage or mitigate its conflicts of interest in a manner that will permit it to act in the municipal entity's best interests.

.03 Action Independent of or Contrary to Advice. If a municipal entity or obligated person client of a municipal advisor elects a course of action that is independent of or contrary to advice provided by the municipal advisor, the municipal advisor is not required on that basis to disengage from the municipal advisory relationship.

.04 Limitations on the Scope of the Engagement. Nothing contained in this rule shall be construed to permit the municipal advisor to alter the standards of conduct or impose limitations on any of the duties prescribed herein. If requested or expressly consented to by the municipal entity or obligated person client, however, a municipal advisor may limit the scope of the municipal advisory activities to be performed to certain specified activities or services. If the municipal advisor engages in a course of conduct that is inconsistent with any such agreed upon limitations, it may result in negating the effectiveness of such limitations.

.05 Conflicts of Interest. Disclosures of conflicts of interest by a municipal advisor to its municipal entity or obligated person client must be sufficiently detailed to inform the client of the nature, implications and potential consequences of each conflict. Such disclosures also must include an explanation of how the municipal advisor addresses or intends to manage or mitigate each conflict.

.06 Inadvertent Advice. A municipal advisor is not required to comply with sections (b) and (c) of this rule if the municipal advisor meets all of the following requirements. In the event that a municipal advisor inadvertently engages in municipal advisory activities for a municipal entity or obligated person and does not intend to continue the municipal advisory activities or enter into a municipal advisory relationship, the municipal advisor must, as promptly as possible after discovery of the provision of inadvertent advice, provide a document to such municipal entity or obligated person that is dated and includes:

(a) a disclaimer that the municipal advisor did not intend to provide advice and that, effective immediately, it has ceased engaging in municipal advisory activities with respect to that

municipal entity or obligated person in regard to all transactions and municipal financial products as to which advice was inadvertently provided;

(b) a notification that such municipal entity or obligated person should be aware that the disclosure of material conflicts of interest and other information required by section (b) of this rule has not been provided;

(c) an identification of all of the advice that was inadvertently provided, based on a reasonable investigation; and

(d) a request that the municipal entity or obligated person acknowledge receipt of the document.

A municipal advisor utilizing this alternative must promptly conduct a review of its written supervisory and compliance policies and procedures to ensure they are reasonably designed to prevent the provision of inadvertent advice to municipal entities and obligated persons. The use of this alternative has no effect on the applicability of any provisions of this rule other than sections (b) and (c) or any other legal requirements applicable to municipal advisory activities.

.07 Applicability of State or Other Laws and Rules. Municipal advisors may be subject to fiduciary or other duties under state or other laws. Nothing contained in this rule shall be deemed to supersede any more restrictive provision of state or other laws applicable to municipal advisory activities. In addition, the specific prohibition in subsection (e)(ii) of this rule shall not apply to an acquisition as principal, either alone or as a participant in a syndicate or other similar account formed for the purpose of purchasing, directly or indirectly, from an issuer all or any portion of an issuance of municipal securities on the basis that the municipal advisor provided advice as to the issuance because that is a type of transaction that is addressed and prohibited in certain circumstances by Rule G-23.

.08 Suitability. A determination of whether a municipal securities transaction or municipal financial product is suitable must be based on numerous factors, as applicable to the particular type of client, including, but not limited to, the client's financial situation and needs, objectives, tax status, risk tolerance, liquidity needs, experience with municipal securities transactions or municipal financial products generally or of the type and complexity being recommended, financial capacity to withstand changes in market conditions during the term of the municipal financial product or the period that municipal securities to be issued in the municipal securities transaction are reasonably expected to be outstanding and any other material information known by the municipal advisor about the client and the municipal securities transaction or municipal financial product, after reasonable inquiry.

.09 Know Your Client. A municipal advisor must use reasonable diligence, in regard to the maintenance of the municipal advisory relationship, to know and retain the essential facts

concerning the client and concerning the authority of each person acting on behalf of such client. The facts "essential" to "knowing a client" include those required to:

(a) effectively service the municipal advisory relationship with the client;

(b) act in accordance with any special directions from the client;

(c) understand the authority of each person acting on behalf of the client; and

(d) comply with applicable laws, regulations and rules.

.10 Excessive Compensation. Depending on the specific facts and circumstances of the engagement, a municipal advisor's compensation may be so disproportionate to the nature of the municipal advisory activities performed as to constitute an unfair practice in violation of Rule G-17. Among the factors relevant to whether a municipal advisor's compensation is disproportionate to the nature of the municipal advisory activities performed are the municipal advisor's expertise, the complexity of the municipal securities transaction or municipal financial product, whether the fee is contingent upon the closing of the municipal securities transaction or municipal financial product, the length of time spent on the engagement and whether the municipal advisor is paying any other relevant costs related to the municipal securities transaction or municipal financial product.

.11 Principal Transactions - Other Similar Financial Products. For purposes of subsection (f)(i) of this rule, which defines the term "engaging in a principal transaction," the phrase "other similar financial product" includes a bank loan, but only if it is in an aggregate principal amount of $1,000,000 or more and it is economically equivalent to the purchase of one or more municipal securities.

.12 529 College Savings Plans and Other Municipal Fund Securities. This rule applies equally to municipal advisors to sponsors or trustees of 529 college savings plans and other municipal fund securities. All references in this rule to an "official statement" include the plan disclosure document for a 529 college savings plan and the investment circular or information statement for a local government investment pool.

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Rule G-8: Books and Records to be Made by Brokers, Dealers, Municipal Securities Dealers, and Municipal Advisors

(a) - (g) No change.

(h) *Municipal Advisor Records*. Every municipal advisor that is registered or required to be registered under Section 15B of the Act and the rules and regulations thereunder shall make and keep current the following books and records:

(i) No change.

(ii) Reserved.

(iii) Reserved.

(iv) *Records Concerning Duties of Non-Solicitor Municipal Advisors pursuant to Rule G-42*.

(A) A copy of any document created by a municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any determination as to suitability.

(v) No change.