MSRB
Municipal Securities Rulemaking Board

Regulatory Notice

2017-19

Publication Date
September 14, 2017

Stakeholders
Municipal Securities Dealers, Municipal Advisors, Issuers, Investors

Notice Type
Concept Proposal

Comment Deadline
November 13, 2017

Category
Fair Practice; Uniform Practice; Market Transparency

Affected Rules
Rule G-11, Rule G-32

Request for Comment on a Concept Proposal Regarding Amendments to Primary Offering Practices of Brokers, Dealers and Municipal Securities Dealers

Overview

The Municipal Securities Rulemaking Board (MSRB) is requesting comment on a concept proposal regarding possible amendments to existing rules related to primary offerings of municipal securities by brokers, dealers and municipal securities dealers (collectively, "dealers"). As part of its regulatory mission, the MSRB periodically revisits its rules over time to help ensure that they continue to achieve their purposes and reflect the current state of the municipal market. After engaging in informal discussions with market participants regarding the MSRB's rules pertaining to primary offering practices, the MSRB now formally seeks comment from all interested parties on the benefits and burdens, including the costs and possible alternatives, of potential changes to MSRB rules related to the primary offering practices of dealers in the municipal securities market. The comments will assist the MSRB in determining whether to propose amendments to MSRB rules pertaining to primary offerings in the municipal securities market or to not make changes, or proceed with an alternative approach.

Comments should be submitted no later than November 13, 2017, 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, MSRB, 1300 I Street NW, Washington, DC 20005. Generally, all comments will be made available for public inspection on the MSRB's website.[1]

[1] Comments generally are posted on the MSRB website without change. For example, 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.

Questions about this concept proposal should be directed to John Bagley, Chief Market Structure Officer, Margaret Blake, Associate General Counsel, or Saliha Olgun, Assistant General Counsel, at 202-838-1500.

Background

In an effort to ensure that MSRB rules continue to accurately reflect how the municipal securities market is evolving and to comply with the MSRB's mission to protect investors, state and local governments and other municipal entities, obligated persons and the public interest by promoting a fair and efficient municipal securities market, the MSRB is undertaking a multi-year review of municipal securities primary offering practices and the rules that govern that process. As part of this review, the MSRB engaged in informal discussions with a diverse range of market participants, including dealers, municipal advisors, issuers and regulators. During these discussions, the MSRB sought to better understand evolving and current practices in primary offerings in order to identify whether any guidance or revisions to existing rules to support protections for municipal securities investors and issuers may be warranted. The MSRB greatly values the input from all who participated in those informal discussions and now seeks comment from all interested parties on the questions raised in this concept proposal. In addition, the MSRB seeks comment more generally on MSRB rules pertaining to primary offering practices. Based on its initial discussions with market participants, the MSRB has preliminarily determined to focus on two MSRB rules, which are the primary subject of this concept proposal: Rule G-11, on primary offering practices, and Rule G-32, on disclosures in connection with primary offerings.[2]

CONCEPT PROPOSAL

I. Rule G-11 – Primary Offering Practices

Rule G-11 establishes terms and conditions for sales by dealers of new issues of municipal securities in primary offerings, including provisions on priority of customer orders. The rule was first adopted by the MSRB in 1978, and was designed to

[2] The MSRB separately is considering issues related to Rule G-34, on CUSIP numbers, new issue, and market information requirements. *See, e.g.,* Release No. 34-81595 (Sept. 13, 2017); SR-MSRB-2017-06 (Aug. 30, 2017).

> increase the scope of information available to syndicate managers and members, other municipal securities professionals and the investing public, in connection with the distribution of new issues of municipal securities without impinging upon the right of syndicates to establish their own procedures for the allocation of securities and other matters.[3]

The MSRB noted that in adopting Rule G-11, the Board chose to require the disclosure of practices of syndicates rather than dictate what those practices must be.[4] Because of the evolving nature of the municipal securities market, Rule G-11 has been the subject of a number of amendments over the years. Now, the MSRB seeks comment on whether to: (A) require underwriters to make a bona fide public offering; (B) standardize the process for issuing a free-to-trade wire; (C) require senior syndicate managers to provide more information to issuers; (D) align the payment of group net sales credits with the payment of net designated sales credits; and (E) require retail (or institutional, as applicable) priority orders in negotiated sales to be allocated in full before allocating to lower priority orders, unless the syndicate manager has received permission from the issuer to allocate to lower priority orders.

A. Bona Fide Public Offering

Syndicate members sometimes agree in the Agreement Among Underwriters ("AAU"), Bond Purchase Agreement ("BPA") or other contractual document that they will make a "bona fide public offering" of the bonds allocated to them at the public offering price. The MSRB understands from market participants, however, that it can be difficult to enforce a syndicate member's contractual obligation to make a bona fide public offering, and often there are few, if any, actions taken by issuers or other market participants that result in repercussions to a syndicate member that does not uphold its contractual obligation to make a bona fide public offering.

Separately, the MSRB is aware of regulatory enforcement actions against syndicate members pursuant to Rule G-17 for allegedly failing to make a "bona fide public offering" of municipal securities despite agreeing to do so in a contractual arrangement. In originally developing Rule G-11, the MSRB considered whether to require syndicates to sell securities at a bona fide

[3] MSRB Reports, Vol. 5, No. 6 (Nov. 1985).

[4] *See, e.g.,* MSRB Reports, Vol. 2, No. 5 (Jul. 1982).

offering price during a mandatory bona fide offering period during which the new issue securities would be sold to the public.[5] However, after carefully considering comments received in response to the MSRB's proposal, the Board ultimately decided against such an approach. As market practices have evolved in the approximately four decades since the initial adoption of Rule G-11 and as recent enforcement actions have again raised the concept of bona fide public offerings, the MSRB seeks comment on the concept of explicitly requiring syndicate members to make a bona fide public offering at the initial offering price.

1. Should there be an MSRB rule that requires syndicate members to make a "bona fide public offering" of municipal securities at the public offering price?

2. If the MSRB were to consider such a requirement, what definition of "bona fide public offering" should apply? Should there be a standardized definition or should syndicate members and/or issuers decide among themselves how to define what would be required?

3. If the MSRB had such a requirement, what documentation or other available means would effectively show that an underwriter met the requirement for compliance purposes (*e.g.*, regulatory examinations)?

4. Should syndicate members be required to notify other members and/or the issuer only if they are not going to make a bona fide public offering?

5. Is the concept of "bona fide public offering" better left as a voluntary contractual arrangement (*i.e.*, not mandated by MSRB rule)?

6. In the alternative, should the MSRB provide guidance or consider implementing a rule that supports inclusion of a contractual provision in the AAU requiring a bona fide public offering without itself implementing a requirement for a bona ride public offering?

7. What are the harms, if any, to other syndicate members, the issuer, investors and the general public when a syndicate member fails to make a "bona fide public offering"?

[5] MSRB Exposure Drafts (Apr. 20, 1976, Sept. 8, 1976 and Nov. 17, 1976).

B. Free-to-Trade Wire

In a primary offering of municipal securities, pursuant to the AAU, typically the senior syndicate manager informs other syndicate members when the BPA has been executed, thus indicating the date of sale or time of formal award of the issue. Shortly thereafter, the senior syndicate manager may send a communication to the syndicate in the form of a "free-to-trade wire." This communication removes the various syndicate restrictions set forth in the AAU or otherwise communicated to the syndicate and indicates to syndicate members that they may trade the bonds at prices other than the initial offering price.

Some market participants noted that the free-to-trade wire is not always disseminated to all syndicate members at once, leading to delays in trading for some syndicate members and their clients. These market participants believe there may be a benefit to having a standardized process for issuing the free-to-trade wire to the syndicate, such that all parties receive the information at the same time.

1. Should there be an MSRB rule that requires the senior syndicate manager to issue the free-to-trade wire to all syndicate members at the same time?

2. If the MSRB were to propose a rule for issuing the free-to-trade wire, what should the rule include? Should there be a specific timeframe within which the wire should be sent?

3. If the MSRB were to propose a rule, should it apply in negotiated sales only?

4. What are the pros/cons to such a requirement? What are the reasonable alternatives?

C. Additional Information for the Issuer

Rule G-11(g) requires the senior syndicate manager to provide extensive information to the syndicate regarding the designations and allocations of securities in an offering. However, the senior syndicate manager is not required to provide this level of information to issuers. While issuers sometimes may be involved in reviewing and approving allocations or may be able to obtain information regarding designations and allocations from various sources, including the senior syndicate manager and certain third-party information resources, some market participants have suggested that the senior syndicate manager nonetheless should be required to provide this

information to the issuer.

1. Do all issuers, regardless of the size of the particular offering, have access to detailed information about the underwriting of their securities, such as information about the allocations, designations paid and take downs directed to each member in the syndicate?

2. If not, should Rule G-11 require the senior syndicate manager to provide this information to the issuer?

    a. Should the senior syndicate manager always be required to provide this information, or should the senior syndicate manager be required to provide it only upon request?

    b. Should any proposed requirement specifically allow for issuers to "opt out" of receiving the information?

3. Is there a preferred method for distributing this information to issuers?

4. Is there other information that senior syndicate managers provide to the syndicate, but do not currently provide to issuers, that issuers would find beneficial to receive?

5. What are the reasonable alternatives to, and benefits and burdens associated with, requiring the senior syndicate manager to provide this information to the issuer?

6. Should the senior syndicate manager in a negotiated sale be required to obtain the issuer's approval of designations and/or allocations unless otherwise agreed to between the parties?

D. Alignment of the Payment of Sales Credits for Group Net Orders with the Payment of Sales Credits for Net Designated Orders and Shortened Timeframe

Rule G-11(i) states that the final settlement of a syndicate or similar account shall be made within 30 calendar days following the date the issuer delivers the securities to the syndicate. Group net sales credits (*i.e.*, those sales credits for orders in which all syndicate members benefit according to their

participation in the account)[6] are paid out of the syndicate account when it settles pursuant to Rule G-11(i). As a result, syndicate members must wait 30 calendar days following receipt of the securities by the syndicate before they receive their sales credits on group net orders. Alternatively, Rule G-11(j) states that sales credits due to a syndicate member as designated by a customer in connection with the purchase of securities ("net designated orders") "shall be distributed" within 10 calendar days following the date the issuer delivers the securities to the syndicate. The MSRB seeks comment as to whether the timing of payment of sales credits on group net orders should be aligned with the timing of payment of sales credits on net designated orders, and seeks information on the benefits, burdens and alternatives to such a change. In addition, the MSRB seeks comment as to whether the overall period of time for distribution of sales credits for both group net and net designated orders should be shortened to a period of less than 10 days.

E. Priority of Orders and Allocation of Bonds

Rule G-11(e) requires that in the case of a primary offering, the syndicate must establish priority provisions. Unless otherwise agreed to with the issuer, the priority provisions must give priority to customer orders over orders by members of the syndicate for their own accounts (*i.e.*, stock orders) or for their related accounts. The rule has a provision that addresses the syndicate's ability to allocate municipal securities in a manner that is different from the priority provisions if it is found to be in the best interest of the syndicate. Rule G-11(f) requires the senior syndicate manager to provide syndicate members in writing a statement of, among other things, the issuer's retail order period requirements, if any, and the priority provisions.[7]

The MSRB has issued guidance regarding priority orders stating that,

> an underwriter may violate the duty of fair dealing by making such commitments [regarding the distribution of an issuer's securities] to the issuer and then failing to honor them. This could happen, for example, if an underwriter fails to accept, give priority to, or allocate

[6] *See* MSRB Glossary of Terms.

[7] Rule G-8(a)(viii) requires records to be maintained reflecting, among other things, the retail order period requirements, if applicable.

to retail orders in conformance with the provisions agreed to in an undertaking to provide a retail order period.[8]

However, market participants have indicated that, despite an issuer's instruction, in some primary offerings, syndicate managers partially allocate to retail orders that should have priority, and then proceed to allocate to lower priority orders even though the higher priority orders have not been fully allocated. The MSRB understands that this practice also occurs with regard to institutional priority orders. The MSRB understands that some syndicate managers have taken the position that such a practice is permissible because no rule states explicitly that allocation of retail (or institutional) priority orders must be made, in full, before a syndicate manager may allocate to lower priority orders. The MSRB seeks comment on whether Rule G-11 should be amended to explicitly state the process by which orders must be given priority. As an alternative, the MSRB also seeks comment as to whether interpretive guidance would better serve to clarify this point.

1. Should Rule G-11 be amended to explicitly state that, in negotiated sales, retail priority orders (or institutional priority orders, as applicable) must be allocated up to the amount of priority set by the issuer before allocating to lower priority orders, unless the senior syndicate manager obtains permission from the issuer to allocate otherwise?

2. Is Rule G-11 in its current form clear with respect to the obligations of a senior syndicate manager surrounding the priority of orders? If not, in what provisions or aspects is it unclear?

3. Does the requirement for the syndicate to set priority provisions in a primary offering result in a more transparent and efficient market for municipal securities?

4. Does the discretion syndicate members currently exercise in the allotment of bonds result in a fair and efficient allocation process?

[8] MSRB Interpretation on Priority of Orders for Securities in a Primary Offering under Rule G-17 (Oct. 12, 2010).

II. Rule G-32 – Disclosures in Connection with Primary Offerings

Rule G-32 sets forth the disclosure requirements applicable to underwriters engaged in primary offerings of municipal securities. Among other things, Rule G-32 requires underwriters in primary offerings to submit electronically to EMMA official statements, advance refunding documents and related primary market documents and new issue information, such as that collected on Form G-32. The rule is designed to ensure that a customer that purchases new issue municipal securities is provided with timely access to information relevant to his or her investment decision. Rule G-32 was originally approved in 1978[9] and has been amended periodically since then to help ensure that, as market practices evolved and other regulatory developments occurred, Rule G-32 would remain current and achieve its goal of providing timely access to relevant information about primary offerings.

In connection with the MSRB's current primary offering practices review, and its review of Rule G-32 in particular, the MSRB seeks comment on whether to: (A) require underwriters in a refunding to disclose, within a shorter timeframe, to all market participants at the same time, the CUSIPs refunded and the percentages thereof; (B) require the underwriter or municipal advisor to submit the preliminary official statement ("POS") to EMMA, if one is available; (C) require non-dealer municipal advisors that prepare certain official statements to make the official statement available to the underwriter after the issuer approves it for distribution; (D) auto-populate into Form G-32 certain information that is submitted to DTCC's New Issue Information Dissemination Service (NIIDS) but is not currently required to be provided on Form G-32; and (E) request additional information on Form G-32 that is not currently provided to NIIDS.

A. Disclosure of the CUSIPs Refunded and the Percentages Thereof

Currently, under Rule G-32(b)(ii), if a primary offering advance refunds outstanding municipal securities and an advance refunding document is prepared, the underwriter is required to submit the advance refunding document to EMMA, as well as the information related to the advance refunding document on Form G-32, no later than five business days after the closing date. Accordingly, the market is sometimes unaware of the particular CUSIPs refunded until after the five-day period, and market participants may have unequal access to this information during the five-day period. In order

[9] *See* Release No. 34-15247 (Oct. 19, 1978), 43 FR 50525 (1978).

to increase market transparency, the MSRB seeks comment as to whether underwriters should be required to disclose, within a shorter timeframe and to all market participants at the same time, the CUSIPs refunded and the percentages thereof.

1. Do underwriters always have access to refunding information earlier than five business days from the closing of the refunding? If so, should they be required to disclose, within this shorter timeframe, the CUSIPs refunded and the percentages thereof to ensure that all market participants have access to the information at the same time?

2. Should the information be submitted to EMMA within a certain period of time from the closing of the refunding or the pricing of the refunding?

3. If the timeframe for providing the refunding information cannot be shortened, should Rule G-32 be amended, in any event, to require that all market participants receive the refunding information at the same time?

4. What are the advantages and disadvantages to such a requirement?

5. Are there other less costly or burdensome or more effective alternatives to promote transparency and equal access to this information?

B. Submission of Preliminary Official Statements to EMMA

Currently, Rule G-32 generally does not require submission of the POS to EMMA, even if one is available. In its effort to improve the scope of information about issuers in the primary market, the MSRB made enhancements to EMMA to permit issuers, on a voluntary basis, to submit POSs and other presale information to the MSRB for display on EMMA. In 2012, the MSRB sought comment on a concept proposal that would have, among other things, made the submission of a POS mandatory by an underwriter of a new issue, if the POS was available.[10] After considering various comment letters received, the MSRB determined not to pursue a rulemaking at that time.

[10] MSRB Notice 2012-61 (Dec. 12, 2012).

Accordingly, market participants continue to have disparate access to timely and important information contained in the POS (to the extent one is prepared). To the extent market participants have difficulty accessing, or lack convenient access to the POS, or are unable to access the POS through some other means, they may be at a competitive disadvantage as compared to other market participants who had earlier access to the POS. To address these concerns, the MSRB seeks comment as to whether the underwriter or municipal advisor should be required to submit the POS to EMMA, if one is available.

1. Should the underwriter or municipal advisor be required to submit the POS to EMMA, if one is available? If so, within what time frame should the POS be required to be submitted?

2. Should the underwriter or municipal advisor be required to seek confirmation from the issuer that they may post the POS on EMMA?

3. Would a requirement that the POS be submitted to EMMA assist in ensuring that all market participants have access to the POS at the same time?

4. What are the advantages or disadvantages of such a requirement for dealers, municipal advisors, issuers and market participants?

5. Is there a valid reason to provide a POS to some market participants but not others?

6. Are there alternative methods that the MSRB should consider for providing the information in the POS that would be more effective and efficient for investors and/or less costly or burdensome to underwriters and municipal advisors?

7. Should the requirement to submit a POS to EMMA apply in negotiated and competitive sales? If so, should there be different rules for each type of offering?

8. Should the rule require the underwriter or municipal advisor to post an updated POS if information changes? Should the rule allow an underwriter or municipal advisor to withdraw the POS if the information becomes stale?

C. Whether Non-Dealer Municipal Advisors Should Make the Official Statement Available to the Underwriter After the Issuer Approves It for Distribution

Rule G-32(c) requires a dealer who acts as a financial advisor ("dealer municipal advisor") and prepares an official statement on behalf of an issuer with respect to a primary offering of municipal securities to make the official statement available to the managing underwriter or sole underwriter in a designated electronic format, after the issuer approves its distribution. Currently, this requirement does not extend to municipal advisors that are not also dealers ("non-dealer municipal advisors"). In order to promote consistency in the delivery of the official statement, the MSRB seeks comment as to whether the current requirement in Rule G-32(c) should be extended to non-dealer municipal advisors as well. In addition, the MSRB seeks comment on whether there is any reason not to make this change.

D. Whether the MSRB Should Auto-Populate into Form G-32 Certain Information that is Submitted to NIIDS but is Not Currently Required to be Provided on Form G-32

MSRB Rule G-34(a)(ii)(C) requires an underwriter of a new issue of municipal securities to submit certain information about the new issue to NIIDS. That provision is designed to facilitate timely and accurate trade reporting and confirmation, among other things, by addressing difficulties dealers have in obtaining descriptive information about new issues of municipal securities.[11] While underwriters submit a great deal of information about a new issue to NIIDS, much of this information is not populated into Form G-32 because not all of the fields required to be submitted to NIIDS are required fields on Form G-32. Including some or all of the information provided to NIIDS on Form G-32 has the potential to enhance transparency in the market. The MSRB seeks comment as to whether any of the fields currently submitted to NIIDS, but that are not required to be submitted on Form G-32, should be required fields on Form G-32, and if so, whether the MSRB should auto-populate this information based on the information submitted to NIIDS. The MSRB also seeks comment on what the potential impact, if any, would be on dealers/underwriters if the MSRB were to require additional data points on Form G-32 where such data is already collected and available in NIIDS.

[11] The requirement to provide this information and the process for doing so arise in Rule G-34 and Rule G-32, respectively. While NIIDS provides the system for submitting the information, its use in no way obviates the requirement that information submitted pursuant to Rule G-34 be timely, comprehensive and accurate. *See* MSRB Notice 2007-36 (Nov. 27, 2007).

E. Whether the MSRB Should Request Additional Information on Form G-32 that Currently is Not Provided in NIIDS, and If So, What Data?

Market participants have indicated during informal outreach that including certain additional information on Form G-32 would be valuable and effective in enhancing transparency. Additional information, not currently submitted to NIIDS, but related to a new issue, might benefit the market if required to be provided on Form G-32. The MSRB seeks comment as to whether additional data points, such as those below, should be required on Form G-32:

- Additional Syndicate Manager(s)
- All Premium Call Dates and Prices and Par Call Date
- Corporate Obligor
- Event Triggers that Change Minimum Denomination
- Legal Entity Identifier (LEI) (for each credit enhancer or obligor, if applicable)
- Management Fee
- Municipal Advisor Fee
- Name of Municipal Advisor
- Retail Order Period by CUSIP (rather than by primary offering)
- Selling Group Member(s)
- True Interest Cost
- Yield to Maturity (in addition to Yield to Worst) on Premium Bonds

Questions Specific to the Above Suggested Data Points

1. Should the current Rule G-32 requirement to disclose whether there was a retail order period as part of a primary offering be replaced with a requirement to disclose retail order periods by CUSIP number?

2. Do market participants, such as issuers and obligors, typically have LEIs? If so, should LEI fields be added on Form G-32 and included in Rule G-34 to permit or require underwriters to submit (if available) the LEI of the relevant obligated person, and/or the issuer if they have one?

3. What are the advantages and disadvantages of requiring dealers to disclose any of the above information?

4. Are there any fixed fees in an underwriting (*e.g.*, municipal advisor fee, underwriting fee, etc.) that would be useful if disclosed on Form G-32? To whom would such fees be useful (*e.g.*, other issuers for comparison purposes)? Should this fee information be disclosed to the issuer in connection with an offering earlier in the process, for example, pursuant to a requirement under Rule G-11 (see I.C. above)?

5. Would any of the above information be useful to market participants?

General Questions

1. Is there additional information not listed in this concept release that the MSRB should consider collecting on Form G-32?

2. What is the impact on dealers if this information cannot be retrieved from NIIDS, and therefore must be input directly into Form G-32 (in addition to the information a dealer must input into NIIDS)?

III. Other Questions

1. Has the IRS's issue price rule impacted any primary offering practices in the municipal securities market, and in what ways? If any MSRB rules are affected, what, if any, amendments should be considered?

2. Are there any other primary offering practices that the MSRB should consider in its review?

3. What are the reasonable alternatives to each of the above proposals? For example, are any of the proposals that would require a rule change better addressed through other means, such as interpretive guidance, compliance resources, additional outreach/education, new MSRB resources, or voluntary industry initiatives? Are there less burdensome or more beneficial alternatives?