



**National Association of Independent
Public Finance Advisors**

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April 13, 2012

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Suite 600
Alexandria, VA 22314

Re: MSRB Notice 2012-13

The National Association of Independent Public Finance Advisors (“NAIPFA”) appreciates the opportunity to provide comments on Municipal Securities Rulemaking Board (“MSRB”) Notice 2012-13 (the “Notice”) and, in particular, the proposed amendments to MSRB Rule G-11 (“G-11” or the “Rule”). NAIPFA’s comments are provided in the spirit that the rule being established will ensure that issuers can rely on receiving unbiased advice and that the issuer remains in control of their debt issuance process.

NAIPFA believes that the MSRB’s proposed addition of section (k) to Rule G-11 (“Section K”) will be beneficial to issuers. However, NAIPFA is concerned that the proposed amendments to G-11(a) will not be beneficial to issuers and, in fact, may result in issuers having to make higher interest payments. NAIPFA, however, would welcome an amendment that puts in place a uniform definition of the term “retail”. In addition, given the current language contained within G-11(f), NAIPFA questions the rationale behind the proposed amendments and believes that the MSRB’s concerns will not be alleviated through either the imposition of more regulations or arbitrary alteration of the current rule. Instead, the MSRB’s concerns would be better addressed through more rigorous enforcement of the current rule.

I. Proposed Addition of G-11(k)

NAIPFA fully supports the addition of Section K. It is NAIPFA’s understanding that this proposed change will likely result in increased market transparency and will allow issuers to better assess the effectiveness of their underwriter both in terms of the underwriter’s ability to sell the issuer’s securities as well as the underwriter’s adherence to the issuer’s desires.

In addition, NAIPFA believes that the proposed addition of Section K may help curtail the detrimental practice known as “flipping” through the additional disclosure obligations outlined in section G-11(k)(iii). In this regard, NAIPFA would like to reiterate its prior comments and state that it is supportive of virtually any rule curtailing the practice of “flipping”, as the use of this practice is generally an indication that the issuer has received less than fair market value for their securities.



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II. Proposed Amendments to G-11(a) & (f)

NAIPFA understands that the inclusion of a definition of the term “retail order period” is necessary to facilitate the other proposed changes to G-11. However, NAIPFA has serious concerns regarding the requirement under G-11(a)(vii) that obligates an issuer to define the term “retail”, and NAIPFA is unclear as to how this proposed amendment will achieve the MSRB’s stated goals. Further, NAIPFA is also concerned that proposed Rule G-11(a)(vii) could ultimately be harmful to issuers. In addition, NAIPFA believes that current rule G-11(f) is sufficient to achieve the MSRB’s stated goals if proper enforcement efforts are put forth.

A) Issuers will be unable or unwilling to define the term “retail”

NAIPFA believes that issuers and, in particular, small infrequent and less sophisticated issuers may not have the knowledge or ability to define the term “retail” for the purpose of defining the “retail order period”, and those who do wish to develop a definition may not have the expertise to do so effectively. This lack of knowledge, ability or desire on the part of issuers may cause them to turn to whoever is assisting them with the issuance process, be it their municipal advisor or their underwriter. In such a scenario, the role of the municipal advisor is clear; the municipal advisor will be obligated to provide the issuer with advice that is in the issuer’s best interest with regard to the retail order period. However, what is less clear is the role of the underwriter in such a scenario. For example, if the issuer is unable to develop a definition of “retail” or develops a definition of “retail” that is not appropriate, is the underwriter under any obligation to advise the issuer with regard to these matters? Regardless, if the underwriter does advise the issuer on these matters, does the underwriter have any duties to the issuer regarding the advice they provide to the issuer with respect to the issuer’s definition of “retail”? In other words, does an underwriter have any obligations to the issuer to disclose that the advice that it is providing with regard to the definition of “retail” may not be consistent with the issuer’s best interest?

NAIPFA believes that such a scenario places the underwriter and the issuer in an untenable situation. On the one hand, the underwriter must engage in fair dealing and cannot mislead the issuer by providing the issuer with advice that is overtly harmful to the issuer’s interests while simultaneously balancing the interests of its investors. On the other hand, the issuer will be relying upon the advice that it receives from its underwriter and will invariably believe that the advice being provided is in their best interest, since it is unlikely that an issuer would willingly seek advice from an entity when it knows that the advice provided is likely to be not in their best interest.

Under the foregoing scenario NAIPFA is concerned that if an issuer is not provided any affirmative underwriter disclosures regarding the advice it receives relating to the definition of the term “retail”, underwriters could easily cross the line into becoming fiduciaries to the issuer as a result of the issuer’s undue reliance on this advice. Alternatively, in the event that



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underwriters do not obtain fiduciary duties, the issuer will likely be harmed by the advice they receive from the underwriter because the advice they receive from the underwriter cannot be in their best interest due to the underwriter's duty to balance the interests of their investors. For example, if it is in the issuer's best interest to conduct a three day retail order period because this will generate the lowest interest rates for the issuer, the issuer could be harmed by an underwriter whose clientele is comprised primarily of institutional investors and who recommends a one day retail order period because the interests of the underwriter's institutional investor clients will not be properly balanced if a three day order period is utilized.

In such a scenario, NAIPFA believes that it is imperative for the issuer to be apprised of these facts prior to accepting the advice of their underwriter. Such disclosures would allow the issuer to make a thoughtful determination as to (a) whether their underwriter is going to be able to effectively sell their securities, and (b) whether the issuer should adopt its *own* definition of retail in light of these disclosures.

Among the concerns put forth by the MSRB as the rationale for these proposed amendments was that market participants have expressed concern that broker-dealers have been using the "retail order periods to achieve yields that may be below market." NAIPFA is concerned that the lack of affirmative disclosure requirements contained within the proposed amendments will not alleviate this concern and may in fact exacerbate the problem; underwriters will now be relied upon even more than in the past by issuers, as issuers will now be forced to perform a task that they will either be unable or unwilling to accomplish without the direct assistance of another individual, which in many cases will be their underwriter. Issuer's will place an undue amount of trust in their underwriter as a result of this rule, underwriters will not be able to provide advice that is in the issuer's best interest, and the rates/yields that will be achieved will likely be higher than market as a result.

B) The Current Rule is Sufficient But For Lack of Enforcement

The MSRB has premised its proposed amendments, at least in part, upon concerns raised by market participants. These concerns range from a "disregard by brokers, dealers, and municipal securities dealers of terms and conditions required by issuers for retail order periods" to the failure by syndicate managers to "disseminate timely notice of issuer terms and conditions regarding retail order periods to all dealers", to broker-dealers use the retail order period to "achieve yields that may be below market." In response to these concerns, the MSRB has (a) increased underwriter disclosure obligations with regard to sales data, which NAIPFA supports, and (b) put forth a definition of the term "retail order period" that requires issuers to define the term "retail". By and large, however, the amendments to the rule will not alleviate the MSRB concerns.



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NAIPFA believes that neither increasing trade data disclosures nor forcing issuers to define the term “retail” will cause broker-dealers to not disregard an issuer’s terms and conditions, nor will such measures cause some broker-dealers to conduct more effective retail order periods.

Conversely, NAIPFA believes that more scrutiny and enforcement actions under the current rule would curtail these practices. Currently, Rule G-11(f) reads as follows:

Communications Relating to Issuer Syndicate Requirements, Priority Provisions and Order Period. Prior to the first offer of any securities by a syndicate, the senior syndicate manager shall furnish in writing to the other members of the syndicate (i) a written statement of all terms and conditions required by the issuer, (ii) the priority provisions, (iii) the procedure, if any, by which such priority provisions may be changed, (iv) if the senior syndicate manager or managers are to be permitted on a case-by-case basis to allocate securities in a manner other than in accordance with the priority provisions, the fact that they are to be permitted to do so, and (v) if there is to be an order period, whether orders may be confirmed prior to the end of the order period. Any change in the priority provisions shall be promptly furnished in writing by the senior syndicate manager to the other members of the syndicate. Syndicate members shall promptly furnish in writing the information described in this section to others, upon request. If the senior syndicate manager, rather than the issuer, prepares the written statement of all terms and conditions required by the issuer, such statement shall be provided to the issuer.

The proposed changes to G-11(f) will be inconsequential to this provision’s effectiveness. The proposed changes will not accomplish the MSRB’s stated rationale for amending the current rule. NAIPFA believes that if the MSRB’s stated purpose is to be achieved, the only way to accomplish this objective is through increased enforcement of the current rule. Yet, the Notice fails in this regard.

C) Proposed Rule G-11(a)(vii) Shifts the Burden to the Issuer

As noted above, the MSRB’s stated purpose is to, in part, ensure that broker-dealers are not taking advantage of the issuer by way of the retail order period and to cause broker-dealers to comply with an issuer’s stated desires. As noted above, however, the current rule would accomplish this stated purpose if proper enforcement were to take place. Conversely, the proposed amendments to the Rule will not address the MSRB’s stated purpose and will instead merely act as a mechanism for shifting the responsibility of the retail order period’s effectiveness onto the issuer.

Under the current rule, if a retail order period were to occur, the issuer has two options, do nothing or provide directives to the underwriter. If the issuer chooses to do nothing, the underwriter will conduct the retail order period however it sees fit. In the event that the retail order period is ineffective or does not achieve the desired rates for the issuer, the issuer can hold the underwriter accountable for its failure. The current approach gives issuers the choice of



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whether to take responsibility for the retail order period. If the issuer does not have specific desires relating to the retail order period, the issuer can sit back and do nothing, whereas an issuer who seeks to control of the retail order period has the ability to do so. Thus, an issuer who provides directives to the underwriter is less likely to be able to hold an underwriter accountable in the event a retail order period does not go as planned.

Conversely, under proposed Rule G-11, issuers will be forced to define the term “retail” and thus will be forced to take responsibility for the outcome of the retail order period. Both large frequent issuers, and small unsophisticated and infrequent issuers will be saddled with obligations relating to the retail order period that they may not fully appreciate and, as discussed above, may cause decisions to be made by the issuer with regard to the retail order period that may not be in their best interest. NAIPFA is concerned that such an approach is contrary to the MSRB’s mandate of protecting the interests of municipal issuers and could in fact be harmful to their interests. NAIPFA cannot see how requiring unsophisticated infrequent issuers who do not generally understand the municipal marketplace to define the term “retail” will be beneficial to their interests. The most likely outcome of the proposed amendments is not going to be the achievement of the MSRB’s stated objectives, but will instead be an increased reliance by municipal issuers on underwriters who will likely be unable to provide advice that is in the issuer’s best interest.

What is more, NAIPFA believes that the G-11(a)(vii) mandate may actually cause issuers to pay higher interest rates. For example, if an issuer defines the term “retail” as being all individuals located within the limits of the municipality, it is extremely unlikely that an underwriter would be able to achieve that result. Thereafter, the underwriter would have to inform the issuer of the unsuccessful retail order period. But, rather than stating that the retail order period was ineffective as a result of the issuer’s definition of “retail”, the underwriter will likely state that the rates/yields utilized were insufficient to generate enough interest in the issuer’s securities. The underwriter would likely then inform the issuer that it will have to increase the issuer’s rates/yields in order to get the issue sold, potentially at levels above what would be considered fair market value, although not necessarily unreasonable in light of the circumstances.

Currently, under the proposed amendments underwriters will be under no obligation to inform the issuer that their definition is inconsistent with industry norms or that it may negatively impact the rates that they ultimately receive for their securities. NAIPFA is concerned that this may result in the artificial inflation of the issuer’s interest rates as a result of a failed retail order period conducted in accordance with the issuer’s instructions, a result that is not in the issuer’s best interest.



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D) The MSRB Should Adopt a Uniform Definition of Retail

The definition of “retail” is widely understood among non-issuer market participants. The MSRB itself understands that the term “retail” generally means something other than “institutional” and generally includes “individual investors and small organizations”.¹ Based upon this general understanding of the term “retail”, NAIPFA can find no rational basis for requiring issuers to develop their own definition.

Instead, NAIPFA believes that proposed Rule G-11 should simply be amended to include the generally accepted definition of the term “retail” for purposes of defining the “retail order period” along with the inclusion of a provision that allows issuers to change the definition, voluntarily, if they so desire. NAIPFA believes that a uniform definition of retail, amendable by the issuer, coupled with the current dictates of G-11(f) as well as increased enforcement efforts, will achieve the MSRB’s stated goal of curtailing broker-dealer disregard for issuer mandated terms and conditions. Further, this approach will prevent a shifting of the burden of the retail order period’s effectiveness onto an issuer unless the issuer desires to carry that burden.

Conclusion

NAIPFA hopes these comments provide insight into our concerns with regard to MSRB Notice 2012-13. We believe a large number of issuers are infrequent and/or small issuers. NAIPFA remains very concerned that these issuers will not be adequately protected in light of the apparent lack of enforcement of the current rule and the apparent shifting of burdens the proposed rule will achieve. NAIPFA is also concerned that the proposed rule will result in issuers continuing to place an undue amount of trust in underwriters as a result of the advice that is being provided to them, which will likely be perceived by the issuer as having been provided with their best interest in mind. Conversely, the suggested amendments detailed in these comments would provide the needed additional protection to municipal entities, and would accomplish the MSRB’s stated goals.

Sincerely,

Colette J. Irwin-Knott, CIPFA
President, National Association of Independent Public Finance Advisors

¹ See “Retail Customer” and “Retail Sale”, Glossary of Municipal Securities Terms, Second Edition (January 2004), http://msrb.org/msrb1/glossary/glossary_db.asp?sel=r (last visited April 4, 2012).



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cc: The Honorable Mary L. Schapiro, Chairman
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Troy A. Paredes, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
Liban Jama, Counsel to Commissioner Aguilar
Lynnette Kelly, Executive Director, Municipal Securities Rulemaking Board