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September 30, 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 Amendments to MSRB Rule G-37 to Extend Its Provisions to Municipal Advisors; MSRB Regulatory Notice 2014-15**

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 2014-15 ("Notice") containing draft amendments to MSRB Rule G-37 ("Draft Amendments") on political contributions by municipal securities dealers ("Dealers") and related prohibitions on municipal securities business, extending the Rule to cover municipal advisors and making certain other changes impacting both Dealers and municipal advisors.

## I. Executive Summary

SIFMA commends the MSRB for taking steps with the Draft Amendments to create a level playing field for all market participants in the area of political contributions. SIFMA believes that it is important that all market participants are subject to the same rules governing political activity, and the Draft Amendments significantly advance that interest. However, SIFMA is submitting these comments to further bring consistency among market participants and in consideration of the heightened constitutional standards set forth in the Supreme Court's decision in *McCutcheon v. FEC*, 134 S. Ct. 1434 (2014).

[1] The Securities Industry and Financial Markets Association (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 (GFMA). For more information, visit www.sifma.org.

In *McCutcheon*, the Supreme Court voices strong support for the right to make political contributions in its decision to invalidate the aggregate contribution limits of the Federal Election Campaign Act of 1971, as amended. *See* 134 S. Ct. 1434 (2014). In so doing, the Court makes clear two principles which are relevant to any restriction on political contributions – first, that political contributions may be restricted only to prevent actual *quid pro quo* corruption or the appearance thereof and, second, that the need for such restrictions must not be based on speculation. *Id*. at 1441, 1456. We applaud the MSRB's effort, as stated on page 6 of the Notice, to require a link between a contribution to an official and a consequent prohibition on business under Rule G-37 (the "Rule"). The existence of such a link is essential for the Rule to be tailored in a manner that is constitutionally appropriate under *McCutcheon*. It is in furtherance of this effort to ensure that Rule G-37 is closely drawn to its stated objective and to level the playing field among market participants that SIFMA offers the following specific comments:

- The time period between SEC approval of the Draft Amendments and their effective date, proposed to be two weeks, should be lengthened to at least 6 months as has been the case in other, similar "pay-to-play" rules.

- The definition of "municipal advisor representative" should be revised to include only those associated persons primarily engaged in municipal advisory activities, in conformity with the definition of "municipal finance representative" for Dealers.

- The *de minimis* exception for political contributions to candidates for whom an individual is entitled to vote under Rule G-37 ($250) should be revised to be consistent with the analogous *de minimis* exceptions under SEC Rule 206(4)-5 for investment advisers and CFTC Rule 23.451 for swap-dealers ($350). Additionally, the "look-back" provision of the Rule should be revised to include an exception for any contributions made by an individual who was covered by the SEC or CFTC pay-to-play rules at the time of the contribution and contributed within the *de minimis* amounts under those rules.

- The cross-ban provision for Dealer municipal advisors should be eliminated in that it is overly broad and does not serve the purpose of attempting to eliminate contributions that are linked to the relevant business.

- The Draft Amendments impose a strict-liability ban on a Dealer or municipal advisor as a result of a political contribution made by its third-party municipal advisor solicitors. Creating such strict liability for a third party's activities is antithetical to the well-established precept that they are not controlled by their clients, and, as a practical matter, it is impossible for

Dealers and municipal advisors to police them. Thus, the Draft Amendments should be revised to eliminate the inclusion of third parties in this ban.

- The Draft Amendments modify the two-year ban to extend the end-date to two years after the date on which the Dealer or municipal advisor is able to transition out of the business with all affected government entities, a transition period that may be required by a municipal advisor's fiduciary duties. This extension, however, is not limited to the government entity subject to the transition, but rather applies to municipal advisor and Dealer business with any government entity affected by the contribution. This should be modified to extend the ban only for business with the entity with which the Dealer or municipal advisor is engaged at the time of the contribution, and not all entities of which the contribution's recipient may be an official.

## II. Comments on Content of the Draft Amendments

### A. Effective Date

The Draft Amendments' expansion of Rule G-37's contribution restrictions are proposed to take effect only two weeks following final approval by the SEC. Two weeks is an insufficient period of time to implement the policy changes and training programs required to comply with the Draft Amendments, even for Dealers that have years of experience with existing Rule G-37's requirements, let alone for municipal advisors that have never before been subject to any similar regulatory regime.

Indeed, in recognition of such difficulty in implementing procedures, other pay-to-play rules have provided significantly longer periods of time for regulated entities to comply with their provisions. For instance, when the SEC approved the final text of SEC Rule 206(4)-5 on June 30, 2010, it provided that the rule would not be effective until 60 days following publication in the Federal Register and the compliance date was set for 6 months after that. The CFTC similarly provided a minimum of 6 months between the effective date of Rule 23.451 and its compliance date. If the Draft Amendments were simply an extension of existing Rule G-37 to municipal advisors, establishing a compliance period shorter than 6 months may be more justifiable. However, the Draft Amendments introduce a number of new requirements to the existing rule for Dealers, making compliance no less complicated than with an entirely new rule. Additionally, by extending the Rule's provisions to municipal advisors, the Draft Amendments potentially cover a range of employees in various different business units of large firms, further increasing the difficulties of adopting appropriate compliance procedures. In light of these

complexities, it is appropriate to provide at least as much time before the Draft Amendments become effective as was provided upon the final adoption of SEC Rule 206(4)-5 and CFTC Rule 23.451.

Accordingly, the Draft Amendments should be revised so that its compliance date is no sooner than 6 months following final SEC approval.

**B. Municipal Advisor Representatives**

The definition of "municipal advisor representative" is included within the definition of municipal advisor professional and, therefore, such individuals are among those whose contributions trigger an automatic prohibition on engaging in municipal advisory activities and, in the case of a Dealer municipal advisor, municipal securities business. The term is defined to mean "any associated person engaged in municipal advisory activities on the firm's behalf, other than a person whose functions are solely clerical or ministerial." The fact that the definition captures any non-clerical associated persons who engage in even a *de minimis* amount of municipal advisory activities is both overly broad and not aligned with the analogous term in the municipal securities prong of the Rule, municipal finance representative.

As noted above, the Supreme Court held in *McCutcheon* that regulating political contributions is permissible only to combat actual or apparent *quid pro quo* corruption, meaning an attempt to obtain a particular official's decision in exchange for money, or the appearance of such a scheme. *Id*. at 1441. Although it is arguable that contributions by an individual who is primarily engaged in covered activity could give rise to an appearance of *quid pro quo* corruption, inferring such corruption where an individual's primary responsibilities and activities are unrelated to such business is not tenable. Under *McCutcheon*, it is insufficient to speculate that contributions by such individuals need to be restricted; specific incidents of this category of individuals engaging in illicit conduct would need to exist and be asserted as a justification. *See id*. at 1456. The risk of contributions by individuals not primarily engaged in covered activity creating an appearance of *quid pro quo* corruption is greatly diminished and is unsupported by specific allegations such that it does not warrant an intrusion into the First Amendment rights of such individuals.

The need for a sufficient nexus between the responsibilities of an associated person and regulated business is recognized by the MSRB in its drafting of existing Rule G-37, as the definition of a municipal finance representative includes only those associated persons primarily engaged in municipal securities business. There is no meaningful distinction between the goals of the two prongs of the Rule as amended by the Draft Amendments that would warrant the broader definition of municipal advisor representative, especially given the imperative that the MSRB

has placed on tailoring the Rule to circumstances where there is a link between a contribution and a ban on business.

Finally, in SEC Rule 206(4)-5 and CFTC Rule 23.451, employees who engage in covered investment advisory or swap-dealer activity are not covered under such rules regardless of how much they engage in such activity. Rather, other than senior officers and supervisors, those rules only cover employees who solicit the covered business in that they are more likely to make contributions that are linked to obtaining the business.

Accordingly, the definition of municipal advisor representative in the Draft Amendments should be revised to include only those associated persons primarily engaged in municipal advisory activities.

### C. Harmonize *De Minimis* Exceptions

MSRB Rule G-37 both currently and as amended by the Draft Amendments includes an exception for certain *de minimis* contributions made to officials of municipal entities. In order for this exception to apply, the contribution must not exceed $250 per election and must be made by a municipal finance professional or, under the Draft Amendments, a municipal advisor professional who is entitled to vote for the candidate. As such, the MSRB under Rule G-37 has historically recognized the importance of protecting the right of individuals to make political contributions to candidates for whom they are entitled to vote. While SIFMA recognizes the MSRB's reluctance to provide a *de minimis* exception for a contribution from a covered person to a candidate for whom they may not vote, we request that the *de minimis* exception when an individual is entitled to vote for a candidate be conformed to the $350 amount under SEC Rule 206(4)-5 and CFTC Rule 23.451.

Indeed, there does not appear to be any evidence supporting $250, $350 or any other specific dollar figure as the level at which a contribution exerts a corrupting influence, making the definition of a *de minimis* contribution somewhat arbitrary. However, to the extent a *de minimis* amount is exempted, it should be uniform across these rules. It is difficult to justify that $350 is a sufficient amount to corrupt an official with respect to municipal securities business, but not investment advisory services. Therefore, in order to ease the compliance burden on the many Dealer and municipal advisor firms also subject to the SEC and CFTC rules, SIFMA suggests that the Draft Amendments bring the *de minimis* exception of MSRB Rule G-37 into conformity with the exceptions in those rules for contributions to candidates for whom an individual may vote. The lack of uniformity amongst these three rules makes it difficult for firms to develop clear and comprehensive compliance systems and standards, and to provide employees

clear and consistent guidelines for permissible political activity which, consequently, imposes significant administrative burden and expense.[2] In bringing this *de minimis* exception into conformity with the other federal pay-to-play rules, covered individuals and the compliance personnel assisting them will need only concern themselves with a single limit for contributions to candidates for whom they may vote, while recognizing the MSRB's desire to limit the *de minimis* exception only to those individuals who are entitled to vote for a candidate. Harmonization of rules, as a general principal, reduces compliance costs and increases regulatory certainty.

Along similar lines, the Draft Amendments should also revise the Rule's "look-back" provision[3] to include an exception for a contribution made by an individual prior to becoming covered by Rule G-37; provided that, such individual was covered by either SEC Rule 206(4)-5 or CFTC Rule 23.451 at the time of the contribution and such contribution was within the *de minimis* exceptions under those rules, including the exception for contributions to candidates for whom one may not vote. Making such a change, along with the increase in the *de minimis* exception discussed above, would conform the limits with which an individual subject to the SEC and/or CFTC rules, but not yet covered by Rule G-37, would need to comply. Again, this would ease the compliance burden for firms subject to multiple rules in that they would not be required to apply different standards for employees subject to the SEC and/or CFTC rule who may at some point be covered by Rule G-37. At the same time, such an exception would in no way jeopardize the integrity of the municipal securities market given that contributions over $150/$350 under such circumstances would still trigger the ban provisions and individuals currently covered by the Rule would continue to be subject to an absolute prohibition on all contributions to candidates for whom they are not entitled to vote.

Accordingly, the Draft Amendments should be revised to (1) raise the current *de minimis* exception for contributions to officials for whom a municipal finance professional or municipal advisor professional is entitled to vote to $350 and (2) include an exception in the "look-back" context for a contribution made by

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[2] It should be noted that most, if not all, states maintain labor laws that prohibit companies from unreasonably restricting the outside political or personal activities of their employees, which essentially requires that companies subject to multiple pay-to-play rules permit employees to make contributions up to the maximum amount allowed by the applicable rule. Therefore, imposing an internal policy prohibiting contributions in excess of the lowest *de minimis* exception across the board, which may be easier to administer, is not a tenable option.

[3] Rule G-37, both currently and as amended by the Draft Amendments, may prohibit covered business as the result of a contribution made by an individual prior to his or her becoming a municipal finance professional or, under the Draft Amendments, a municipal advisor professional. This provision of the rule is commonly referred to as the "look-back."

an individual prior to becoming a municipal finance professional or municipal advisor professional; provided that, such individual was covered by either SEC Rule 206(4)-5 or CFTC Rule 23.451 at the time of the contribution and the contribution was within the *de minimis* exceptions under such rules.

### D. Cross-Bans

The cross-ban provision of the Draft Amendments would prohibit a Dealer municipal advisor from engaging in municipal securities business as a result of a contribution by a municipal advisor professional to an official with dealer selection influence and, similarly, would apply in the converse situation where a municipal finance professional triggers a ban on municipal advisory activities (the "Cross-Ban"). As a result, a ban on business would be triggered by a contribution by an individual with an even more tenuous connection to the prohibited business than in the situation discussed above in section II. B. Here, an individual with no relationship whatsoever to municipal securities business would trigger a ban on her Dealer municipal advisor firm doing such business. Thus, it is unclear how Cross-Bans comport with the MSRB's stated goal of requiring a link between a contribution and covered business. Additionally, under the standard advanced in the *McCutcheon* decision, the risk of actual or apparent *quid pro quo* corruption stemming from a contribution to an official with selection influence wholly unrelated to the contributor's duties is too remote and speculative to justify imposing Cross-Bans. Indeed, the Cross-Ban provision assumes that a Dealer municipal advisor is using employees in the other divisions (such as the municipal securities division using municipal advisor professionals) to circumvent the Rule.

Accordingly, the Draft Amendments should be revised to eliminate the Cross-Ban provision.

### E. Municipal Advisor Third-Party Solicitors

Under the Draft Amendments, a municipal advisor third-party solicitor engaged by a Dealer or municipal advisor to solicit municipal securities business, municipal advisory business, or investment advisory services on its behalf would trigger a ban for its client as a result of a contribution by it, its municipal advisor professionals, or any of their controlled PACs to an official of a municipal entity it was engaged to solicit. The expansion of the Rule to cover these persons is overly broad in certain cases and unfairly subjects market participants to a strict-liability prohibition on business for the actions of persons they cannot control.

Under the plain language of the Draft Amendments, the ban would apply to all of the client's municipal securities or municipal advisory business with an affected government entity regardless of which type of business it was engaged to

solicit. For example, a contribution by a municipal advisor third-party solicitor to an official with dealer selection influence would trigger a ban on municipal securities business even if it was engaged to solicit only municipal advisory business from that official's municipal entity. This lack of linkage is further exacerbated by the fact that a Dealer is barred from using third parties to solicit municipal securities business under MSRB Rule G-38. Furthermore, it is difficult to envision a situation in which a third-party would attempt to exert illicit control over an official decision regarding business it was not hired to obtain and, as the Supreme Court held in *McCutcheon*, mere speculation as to the possibility of corruption schemes are insufficient to form the basis for a restriction on contributions. *Id*. As such, there is no link sufficient to create a risk of *quid pro quo* corruption or the appearance thereof where a municipal advisor third-party solicitor makes contributions to officials with influence over business they are not attempting to obtain for a client.

Even where there could be a more direct link creating a risk of the appearance of *quid pro quo* corruption, subjecting market participants to an automatic prohibition on municipal securities business and/or municipal advisory activities as a result of a contribution made by an entity or individual not under its control or subject to its policies and procedures is an overly broad and unfair mechanism to prevent an appearance of *quid pro quo* corruption. There is no means by which a Dealer or municipal advisor can effectively prevent prohibited contributions by its third-party solicitors. While representations and warranties in solicitor contracts and training of their personnel may mitigate some risk, ultimately the Draft Amendments put Dealers' and municipal advisors' business in automatic jeopardy as if the third parties are agents of or supervised by the Dealer or municipal advisor. In addition to the impractical nature of imposing a strict-liability ban on business for actions of third parties, in doing so the Draft Amendments turn back a well-established precept that market participants do not control third parties. While clearly municipal advisor third-party solicitors may prevent themselves from engaging in certain business by their own actions, imposing such consequences on their clients would rewrite the current structure and understanding of such vendor-client relationships. It should be noted that the SEC, in drafting Rule 206(4)-5, initially imposed strict liability on an investment adviser for the contributions of its third-party solicitors, but eventually eliminated such a standard. In the current version of the SEC rule's placement agent provisions, advisers are not liable for such contributions, but must only ensure that third parties soliciting investment advisory business on their behalf are subject to a pay-to-play rule.

Accordingly, the Draft Amendments should be revised to exclude municipal advisor third-party solicitors, their municipal advisor professionals, and their controlled PACs from the group of persons that may trigger a ban on business for Dealers and municipal advisors. Alternatively, the Draft Amendments should be

clarified to impose a ban resulting from a contribution by municipal advisor third-party solicitors, their municipal advisor professionals, and their controlled PACs only when such contribution is made to an official with selection influence over the type of business the solicitor was engaged to solicit.

### F. Modification of the Two-Year Ban

Under existing Rule G-37, a prohibited contribution triggers a ban on engaging in municipal securities business with any municipal entity of which the recipient is an "official of an issuer" beginning from the date of the contribution and ending two years after such date. The Draft Amendments extend the end-date of this period to two years after all municipal securities business or municipal advisory business, as applicable, with such municipal entity ceases. This extension permits a Dealer or municipal advisor to engage in an orderly transition period out of the prohibited business, while still being subject to the full two-year ban. However, in cases where the recipient of a prohibited contribution is a covered official of multiple governmental entities, the Draft Amendments would prohibit a firm from engaging in covered business with each of them for that extended period of time even if the transition period was required for only one of them. Accordingly, the firm could be unfairly prohibited from doing business with certain entities for a period of time in excess of two years.

While we understand the need to extend the ban when it comes to necessary transition services for a particular government entity, there is no justification to extend the ban to government entities for which transition services are not necessary. Indeed, by limiting the extended ban to the particular government entity, the net effect for non-affected government entities would be a two-year ban, the period intended under the rule. Thus, the modification of the two-year ban should be tailored to apply only to any entity with which a firm engages in the covered business beyond the date of the contribution to permit an orderly transition, allowing the prohibition on business with all other entities impacted by the contribution to expire two years after the date of the contribution.

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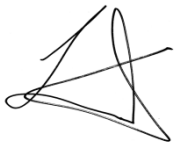
Please do not hesitate to contact me at (212) 313-1130, or our counsel, Ki P. Hong or Charles M. Ricciardelli of Skadden, Arps, Slate, Meagher & Flom LLP at (202) 371-7017 with any questions.

Sincerely yours,



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