MSRB Proposed G-20 Comments

The comments below are submitted on behalf of a registered investment adviser (RIA) that is also a municipal advisor (MA) and are provided in response to specific MSRB questions raised in Regulatory Notice 2014-18. The comments relate mostly to how the proposal would affect an RIA that is also an MA (RIA-MA).

1) How prevalent are "gift giving," entertainment practices, the use of non-cash compensation in relation to primary offerings and the other practices addressed in Rule G-20 and the draft amendments ("gift giving and other practices") involving municipal advisors in the municipal securities market? What is the effect of real or perceived gift giving and other practices involving municipal advisors on the municipal securities market? Please provide specific examples of gift giving and other practices not currently addressed in Rule G-20 or the draft amendments involving municipal advisors and that may warrant consideration.

The practices described in Proposed Rule G-20 are substantially limited, if not completely prohibited, by municipal government ethics rules in many jurisdictions in the United States. In the case of an RIA-MA, the practices addressed in Rule G-20 are already completely prohibited: An RIA-MA is acting as both an RIA and an MA when providing MA services, so RIA rules apply. Except for bona fide employees or contractors, SEC regulations strictly prohibit RIAs from transferring anything of any value whatsoever to anyone "for the purpose of obtaining or retaining a [government] client for… an investment adviser." 17 C.F.R. § 275.206(4)-5(a)(2)(i), (f)(10).

However, as to other MAs who are not subject to strict RIA regulation, the gift giving and other practices proposed to be allowed in this rule could have a negative effect on the actual or perceived integrity of the municipal securities market.

2) Do the draft amendments strike the right balance of consistency between the treatment of dealers and municipal advisors, while appropriately accommodating for the differences between these regulated entities? If not, where are differences in treatment warranted that are not reflected in the draft amendments? Conversely, do the draft amendments overemphasize the differences between the regulated entities in a way that is not warranted or desirable?

No comment.

3) Are the exceptions to the $100 limit appropriate? Should some or all of them be drafted more broadly or narrowly? Should any of them be eliminated?

The exceptions generally appear to be tailored to limiting conflict or the appearance of conflict and to allow appropriate social interaction with actual or potential business associates. However, the proposed financial limits are potentially incompatible with existing rules that apply to many

MAs, and are set at an inappropriate level to limit actual or perceived influence on issuer officials or personnel.

As noted above, regulations already completely prohibit RIA-MAs from transferring anything of any value whatsoever to "any person to solicit a government entity" "for the purpose of obtaining or retaining a client for… an investment adviser." Thus, generally, for RIA-MAs, even the $100 limit is irrelevant, because the effective limit on RIA gifts to government officials or personnel is $0. This is because "payment" is defined as "any gift, subscription, loan, advance, or deposit of money or anything of value," and there is no *de minimis* exception to this prohibition. 17 C.F.R. § 275.206(4)-5(f)(7).

The federal government and many states and localities limit gifts to government officials and employees to a value of $20 or less per gift, up to a maximum of $50 per year from the same person or organization. Thus, if the MSRB moves forward with this proposal, we suggest that the MSRB consider mirroring these limits to help level the playing field among all types of MAs and attain broader compatibility with existing federal, state, and local law.

4) Are the various baselines proposed to be used for the purposes of economic analysis appropriate baselines? Are there other relevant baselines that the MSRB should consider?

The proposed baselines may be appropriate for some MAs who engage exclusively in MA activities in jurisdictions with no regulation of gift-giving to issuers and their officials, but for RIA-MAs, additional regulation would impose undue burdens on RIA-MAs whose baseline for gift giving activities is already zero.

5) If the draft amendments were adopted, what would be the likely effects on competition, efficiency and capital formation?

The SEC already regulates RIAs and collects extensive information from RIAs, so the proposed rules may needlessly increase the compliance burden on RIA-MAs. Additionally, because the SEC enforces MSRB rules, the proposed rules would also increase the enforcement burden on the SEC, if RIA-MAs would be required to maintain separate sets of records containing identical information.

The increased regulatory burden on RIA-MAs could cause some experienced and reputable MAs to withdraw from the market, leaving behind MAs who are not subject to strict RIA gift-giving restrictions.

The increased compliance burden would increase costs for those remaining MAs, and thus likely decrease the number of regulated entities and cause those regulated entities to increase fees, which would reduce competition and raise costs for issuers.

6) Is the proposed extension of the provisions regarding non-cash compensation in connection with primary offerings to municipal advisors appropriate?

Yes, the proposed extension is appropriate.

7) Do commenters believe that the draft amendments explicit prohibition of seeking and or obtaining reimbursement for entertainment expenses from the proceeds on an issuance of municipal securities is appropriate? Is the term, "entertainment expenses," which is defined for the purposes of this prohibition, appropriately tailored?

This restriction would be inappropriate as drafted. Although the intent is clearly stated in the preamble, i.e., to limit unnecessary expenses of a regulated entity and to minimize actual or apparent undue influence on issuers, the proposed rule itself is drafted more broadly than necessary to achieve those goals.

For RIA-MA firms, the proposed limitation would be unnecessarily restrictive and potentially detrimental to other business: Assume at firm F, Individual A is an investment adviser who advises commercial clients on private-sector equity securities. Individual M engages in municipal advisor activities, and secures compensation for F from fees earned from advising on municipal offerings. M and A have no clients in common; M and A do not even know each other's names, and may work on opposite sides of the country. Nevertheless, A would be prohibited from being reimbursed by F for the entirely appropriate business expense of taking a prospective commercial client to lunch, even if the prospective client and A have no direct or indirect connection whatsoever with M's municipal advisory activities, because some portion of the reimbursement for these "entertainment expenses" would be attributable to the "proceeds" of an offering. This could not be the kind of activity the MSRB intends to prevent.

To ensure that the MSRB's apparent intent is reflected in any future rule, and to ensure that the prohibition is at least rationally connected to the activity it is apparently attempting to prevent, (i.e., MAs obtaining reimbursement in excess of earned fees for inappropriate staff expenses or unduly influencing municipal officials with lavish meals financed by securities issued at taxpayer expense), we suggest that the MSRB consider rewriting proposed G-20(e) to clarify that the prohibition is not intended to unnecessarily restrict how a regulated entity may appropriately use its fees properly earned from the proceeds of an offering.

8) Are the recordkeeping requirements that apply to dealers in existing Rule G-20 and the analogous draft requirements that would apply to municipal advisors appropriately tailored to obtain information that is relevant for the purposes of Rule G-20? Are there additional costs or benefits to the recordkeeping obligations that the MSRB should consider?

The information is relevant, but for RIA-MAs, the documentation requirements in proposed G-8(h) are unnecessary because RIAs are already required to keep such records under 17 C.F.R. § 275.206(4)-3. Thus, we suggest that the MSRB consider exempting RIA-MAs from the requirements of proposed G-8(h).

9) What would be the effect of draft amended Rule G-20 for dealers that have instituted long-standing compliance programs? What would be the effect of draft amended Rule G-20 for dealer-municipal advisors that have instituted long-standing compliance programs? Do dealers or dealer-municipal advisors anticipate that any of the draft amendments to Rule G-20 would increase or decrease either the occurrence of, or the perception of, gift giving and other practices addressed in Rule G-20 and the draft amendments in order to obtain or retain municipal securities or municipal advisory business in the municipal securities market?

No comment.

10) What alternative methods should the MSRB consider in addressing the potential for improprieties related to gift giving and other practices addressed in current Rule G-20 and the draft amendments to Rule G-20?

As an alternative to proposed G-20, with regard to MA activities, to ensure that RIA-MAs are not unduly disadvantaged by the ability of non-RIA MAs to give gifts, we suggest that the MSRB consider two alternatives:

1) Simply incorporate 17 C.F.R. § 275.206(4)-5 into Rule G-20 and clarify that it also applies to MA activities of any regulated entity: For RIA-MAs, Rule 206(4)-5 already does apply in that manner, so there would be little or no impact on RIA-MAs, and all MAs would be subject to the same rules. Furthermore, a simple incorporation and application of 17 C.F.R. § 275.206(4)-5 would reduce duplicative rulemaking and regulatory compliance activities so that there is a clear set of rules to apply whenever a government entity is involved in any kind of investment advisory activity. This would also increase regulatory certainty for all issuers and entities involved in MA activity.
2) Alternatively, assuming the MSRB incorporates the above-suggested amendments to proposed rules G-20(c), (d), (e), and G-8(h), we suggest that the MSRB consider recommending to the SEC that it adjust Rule 206(4)-5 to be more compatible with proposed rule G-20 as to MA activities of RIA-MAs.