



July 3, 2017

VIA ELECTRONIC DELIVERY

Municipal Securities Rulemaking Board
Attention: Ronald Smith, Corporate Secretary
1300 I Street NW, Suite 1000
Washington, DC 20005

pfm

RE: MSRB 2017-11 Second Request for Comment on Draft Amendments to and Clarifications of MSRB Rule G-34, on Obtaining CUSIP Numbers

1735 Market Street
43rd Floor
Philadelphia, PA 19103
215.567.6100

pfm.com

Dear Mr. Smith:

On behalf of Public Financial Management, Inc., and PFM Financial Advisors LLC (collectively, referred to as "PFM"), PFM would like to thank the Municipal Securities Rulemaking Board (the "MSRB") for the opportunity to comment on the MSRB's revised draft amendments to and clarifications of MSRB Rule G-34 on obtaining CUSIP numbers ("Rule G-34"), pursuant to MSRB 2017-11 Second Request for Comment on Draft Amendments to and Clarifications of MSRB Rule G-34, on Obtaining CUSIP Numbers (the "Second Request for Comment"). As the nation's largest independent municipal advisor and the top-ranked municipal advisor in the nation in terms of both number of transactions and total dollar amount according to Thomson Reuters as of December 2016, we hope that our broad, national perspective on the proposed further revisions to Rule G-34 and their potential effects on the municipal market will provide valuable feedback for the MSRB's careful consideration.

PFM submitted comments to the MSRB's initial draft amendments to and clarifications of MSRB Rule G-34 on obtaining CUSIP numbers (the "Initial Comment Letter"), pursuant to MSRB 2017-05 Request for Comment (the "Initial Request for Comment"). PFM continues to recognize that the MSRB's stated intent in drafting the further amendments to Rule G-34 is to: 1) clarify its existing view with respect to when CUSIP numbers are required to be obtained and who is responsible; 2) alleviate regulatory imbalance between dealer municipal advisors and non-dealer municipal advisors; and 3) create a uniform practice for market participants while reducing the number of municipal securities that fail to have CUSIP numbers assigned.¹ While we appreciate the MSRB's efforts to address the intents of the rule in light of comments received in response to the Initial Request

¹ See generally, MSRB Request for Comment on Draft Amendments to and Clarifications of MSRB Rule G-34, Obtaining CUSIP Numbers, Regulatory Notice 2017-05 (March 1, 2017); See also, MSRB Second Request for Comment on Draft Amendments to and Clarifications of MSRB Rule G-34, Obtaining CUSIP Numbers, Regulatory Notice 2017-11 (June 1, 2017).



for Comment, we do not believe that the proposed further amendments to Rule G-34 in the Second Request for Comment go far enough in providing much of the guidance sought and resolving many of the issues raised in the responses to the Initial Request for Comment. Accordingly, PFM reiterates that we cannot support the revisions in the Second Request for Comment, given the absence of regulatory guidance outlined in items 1-5 below, which we are more fully detailed in PFM's Initial Comment Letter attached hereto, and submits an additional element and commentary expanding on item 2 below, in light of the additional changes proposed by the MSRB in the Second Request for Comment:

- 1) Expansion of the list of event notices pursuant to the Municipal Disclosure Rule 15c2-12² ("Rule 15c2-12") under the Securities and Exchange Act of 1934 (the "Exchange Act") to include private placement transactions, which rule the Securities and Exchange Commission (the "SEC" or "Commission") is currently seeking comment to proposed amendments for such an expansion pursuant to SEC Release No. 34-08130³; Pending the outcome, we believe MSRB should withdraw the proposed changes to Rule G-34 until any changes to Rule 15c2-12 can be contemplated and implemented;
- 2) Further explicit refinement of the definition of a municipal security such that it is clearly differentiated from a non-securitized bank loan or a municipal financial product not requiring a CUSIP to give guidance to all market participants, including municipal entity issuers and obligated persons, beyond the test provided by the U.S. Supreme Court in *Reves v. Ernst & Young, Inc.*⁴; We believe the consequences of the proposed Rule amendments could be in conflict with the marketplace use and may inadvertently lead to mischaracterization or confusion regarding the motivation of the parties or incorrectly appear to indicate plans for further distribution to investors/lenders;
- 3) Establishment of a process for a municipal entity to obtain a CUSIP where neither a municipal advisor nor a broker, dealer or municipal securities dealer acting as an underwriter is involved in a new issue private placement transaction;
- 4) Clarification of the process of obtaining a CUSIP where there are multiple municipal advisors involved in a new issue private placement transaction;
- 5) Consideration of adverse effects on municipal issuers, including dampened interest by private investors and the infliction of overly burdensome administrative costs for municipal entities given the unknown materiality of the additional benefit gained for investors; and

² 17 CFR 240.15c2-12.

³ See Exchange Act SEC Rel. No. 34-80130 (March 15, 2017).

⁴ *Reves v. Ernst & Young, Inc.*, 494 U.S. 56 (1990).



- 6) Explicit regulatory guidance regarding indicia of "reasonable belief" for purposes of relying on the proposed exception proposed in Section (a)(i)(F) of MSRB Rule G-34.

Guidance Regarding the Definition of a "Security" and Indicia of "Reasonable Belief" for Purposes of the Bank Direct Purchase Exception

We appreciate the MSRB's attempt to address commenters' request to exclude direct placements from the requirements to obtain a CUSIP. However, the proposed solution advances another long-standing quandary and introduces additional uncertainty in the industry. In PFM's Initial Comment Letter, PFM proposed that perhaps the MSRB could work with the SEC to provide practical guidance to all market participants, including municipal entity issuers and obligated persons, beyond the list provided in Section 3(a)(10) of the Exchange Act⁵ as tested in *Reves*⁶ such that determination of whether an instrument is a security is clear. With respect to more refinement of the definition of "municipal security," PFM believes that not only would such clarity obviate the need for any of the proposed amendments to Rule G-34 aimed at addressing questions among market participants regarding the application of Rule G-34 to private placements of municipal securities, but it would also provide much needed clarity to the MSRB's newly proposed exception from the proposed CUSIP requirements. In the absence of regulatory clarity with respect to both matters, municipal advisors seeking to rely on the exception would be required to first make a determination that the financial instrument is a municipal security and then form a reasonable belief that the purchasing bank, affiliated banks or consortium of banks formed for the purpose of participating in a direct purchase of a new issue of the instrument(s) is likely to hold it to maturity or limit resale. We again submit that lack of clear guidance regarding the definition of a "security" may lead to market inefficiencies caused by market participants incurring costs and expending time unnecessarily to obtain CUSIPs for all transactions, including those involving instruments not deemed to be securities, out of an abundance of caution of running afoul of regulatory requirements. Alternatively, in order to avail itself of the exception proposed in Section (a)(i)(F) of MSRB Rule G-34, the municipal advisor would be placed in the inexorable position of establishing and implementing policies and procedures reasonably designed to assist the municipal advisor in arriving at a reasonable belief regarding the likelihood of the purchasing bank to hold the instrument(s) to maturity or limit resale of same. To that end, a listing of instruments which clearly either are or are not considered to be a "security" would provide the necessary regulatory clarity to market participants and eliminate unnecessary, market inefficient activities performed for want of harmonized direction. Moreover, guidance regarding the indicia of the required "reasonable belief" would need to include the substance, form, and medium of certification, representation, documentation or other evidence necessary to withstand regulatory scrutiny for the market participant seeking to rely on the exception.

⁵ 15 U.S.C. 78a et seq.

⁶ *Reves v. Ernst & Young, Inc.*, 494 U.S. 56 (1990).



While PFM continues to be supportive of the consistent objectives of the MSRB in seeking to facilitate market transparency and efficiency, we remain fundamentally opposed to the extension of the obligations set forth in Rule G-34 for a non-dealer municipal advisor as proposed in the initial and second draft amendments, thereby creating a direct duty with respect to the discrete interests of investors. Insofar as obtaining CUSIPS facilitates the clearance and settlement of securities, under the proposed amendments to Rule G-34 non-dealer municipal advisors would be inappropriately burdened with the responsibility of engaging in activity that falls outside the purview of their scope of service and epitomizes traditional broker-dealer type activity. Previous occasions have afforded Congress and the SEC multiple opportunities to enact provisions intended to have the municipal advisor also directly serve interests of investors and neither institution has done so to date. By way of refrain, Congress and the SEC have declined to bridge natural and necessary differences between brokers, dealers and underwriters on the one hand and municipal advisors on the other hand leaving intact what the MSRB perceives as "regulatory imbalance" in the draft proposed Rule G-34. If changes are to be made to these core precepts, we respectfully point to the need for Congressional and/or SEC action rather than action by the MSRB in making such a change in the fabric of the municipal advisory regulatory regime.

We continue to believe that the Commission's opportunity to carefully consider and respond (including with rule modifications) to any comments submitted to its proposed amendments to Rule 15c2-12 would provide an essential foundation to any action on the proposed changes to MSRB Rule G-34.

PFM welcomes the opportunity to further discuss our comments with the MSRB, accordingly please feel free to contact us if our feedback would be useful.

Respectfully submitted,

Leo Karwejna
Chief Compliance Officer

Cheryl Maddox
General Counsel

Catherine Humphrey-Bennett
Municipal Advisory Compliance Officer

Attachment



March 31, 2017

VIA ELECTRONIC DELIVERY
Municipal Securities Rulemaking Board
Attention: Ronald Smith, Corporate Secretary
1300 I Street NW, Suite 1000
Washington, DC 20005

pfm

1735 Market Street
43rd Floor
Philadelphia, PA 19103
215.567.6100

pfm.com

RE: MSRB 2017-05 Request for Comment on Draft Amendments to and Clarifications of MSRB Rule G-34, on Obtaining CUSIP Numbers

Dear Mr. Smith:

On behalf of Public Financial Management, Inc., and PFM Financial Advisors LLC (collectively, referred to as "PFM"), PFM would like to thank the Municipal Securities Rulemaking Board (the "MSRB") for the opportunity to comment on the MSRB's draft amendments to and clarifications of MSRB Rule G-34 on obtaining CUSIP numbers ("Rule G-34"). PFM, which has been in existence for over 40 years, is the nation's largest independent municipal advisor and is the top-ranked municipal advisor in the nation in terms of both number of transactions and total dollar amount according to Thomson Reuters as of December 2016. We hope that you agree that our municipal market presence gives us a broad, national perspective on the proposed amendments and clarifications and their potential effects on the municipal market.

PFM recognizes the MSRB's stated intent in drafting the amendments to Rule G-34 to clarify its existing view with respect to when CUSIP numbers are required to be obtained and who is responsible, alleviate regulatory imbalance between dealer municipal advisors and non-dealer municipal advisors, and create a uniform practice for market participants while reducing the number of municipal securities that fail to have CUSIP numbers assigned.¹ We cannot support the MSRB in its endeavors with respect to the proposed amendments to Rule G-34, and instead PFM would like the Board to reconsider the draft amendments for municipal advisors, with focus on the following missing elements:

- 1) Expansion of the list of event notices pursuant to the Municipal Disclosure Rule 15c2-12² ("Rule 15c2-12") under the Securities and

¹ See generally, MSRB Request for Comment on Draft Amendments to and Clarifications of MSRB Rule G-34, Obtaining CUSIP Numbers, Regulatory Notice 2017-05 (March 1, 2017).

² 17 CFR 240.15c2-12.



Exchange Act of 1934 (the "Exchange Act") to include private placement transactions, which rule the Securities and Exchange Commission (the "SEC" or "Commission") is currently seeking comment to proposed amendments for such an expansion pursuant to SEC Release No. 34-08130³; Pending the outcome, we believe MSRB should withdraw the proposed changes to Rule G-34 until any changes to Rule 15c2-12 can be contemplated and implemented;

- 2) Further explicit refinement of the definition of a municipal security such that it is clearly differentiated from a non-securitized bank loan or a municipal financial product not requiring a CUSIP to give guidance to all market participants, including municipal entity issuers and obligated persons, beyond the test provided by the U.S. Supreme Court in *Reves v. Ernst & Young, Inc.*⁴; We believe the consequences of the proposed Rule amendments could be in conflict with the marketplace use and may inadvertently lead to mischaracterization or confusion regarding the motivation of the parties or incorrectly appear to indicate plans for further distribution to investors/lenders;
- 3) Establishment of a process for a municipal entity to obtain a CUSIP where neither a municipal advisor nor a broker, dealer or municipal securities dealer acting as an underwriter is involved in a new issue private placement transaction;
- 4) Clarification of the process of obtaining a CUSIP where there are multiple municipal advisors involved in a new issue private placement transaction; and
- 5) Consideration of adverse effects on municipal issuers, including dampened interest by private investors and the infliction of overly burdensome administrative costs for municipal entities given the unknown materiality of the additional benefit gained for investors.

Harmonizing Rule G-34 with Municipal Disclosure Rule 15c2-12 of the Exchange Act

PFM notes that the Commission published a regulatory release on March 15, 2017, requesting comments to proposed amendments to municipal securities disclosure, with comments expected to be submitted on or before May 15, 2017.⁵ In its release, the Commission remarked that the "proposed amendments would amend the list of events for which notice is required to be provided to the MSRB" and that such "proposed amendments would facilitate investors'

³ See Exchange Act SEC Rel. No. 34-80130 (March 15, 2017).

⁴ *Reves v. Ernst & Young, Inc.*, 494 U.S. 56 (1990).

⁵ *Id.*



and other market participants' access to important information in a timely manner and help enhance transparency in the municipal securities market".⁶ Accordingly, PFM submits that the Commission's proposed amendments to Rule 15c2-12 address the same concerns as the MSRB's stated intent of amendments to Rule G-34. To realize regulatory efficiencies and avoid undue regulatory burden, we believe that the MSRB should postpone any action on Rule G-34 until the Commission has had an opportunity to review any comments the Commission may receive on proposed amendments to Rule 15c2-12 and makes a determination whether or not to adopt the amendments, with or without modification addressing any applicable comments. Providing clarity and guidance to define the attributable financial obligations with the corresponding materiality factors supporting additional disclosure should be a key driver of the ongoing concept of achieving greater transparency for all market participants by making the disclosure a necessary element of investor communications and considerations for existing publicly held debt. As this will be a shift from the current environment of somewhat cloudy materiality standards and voluntary disclosures surrounding this subject matter, PFM believes that only after the Commission has completed its regulatory rulemaking process with respect to Rule 15c2-12 will the MSRB be positioned to determine whether Rule 15c2-12 sufficiently addresses the MSRB's intent of the amendments to Rule G-34 or if further rulemaking is in order. Thereafter, the rules can be appropriately synchronized to the extent further refinement is required.

Guidance Regarding the Definition of a "Security"

With respect to more refinement of the definition of "municipal security," PFM believes the MSRB should work with the SEC to provide practical guidance to all market participants, including municipal entity issuers and obligated persons, beyond the list provided in Section 3(a)(10) of the Exchange Act⁷ as tested in *Reves*⁸ such that determination of whether an instrument is a security is clear. Such clarity would obviate the need for any of the proposed amendments to Rule G-34 aimed at addressing questions in the industry regarding the application of Rule G-34 to private placements of municipal securities. Lack of clear guidance regarding the definition of a "security" may also lead to market inefficiencies caused by market participants incurring costs and expending time unnecessarily to obtain CUSIPs for all transactions, including those involving instruments not deemed to be securities, out of an abundance of caution of running afoul of regulatory requirements. To that end, a listing of instruments which clearly either are or are not considered to be a "security" would provide the necessary regulatory clarity to market participants.

⁶ *Id* at 13928 - 13929.

⁷ 15 U.S.C. 78a et seq.

⁸ *Reves v. Ernst & Young, Inc.*, 494 U.S. 56 (1990).



In our experience, banks may find it useful to obtain a CUSIP or another form of identifier for an instrument in a private transaction for the bank's own tracking and reporting purposes. However, as attainment of a CUSIP is voluntary for instruments that are not "securities," to avoid the unintentional tail wagging the dog, obtaining a CUSIP should not *per se* mischaracterize a nonsecurity as a security subject to all attendant regulatory requirements.

Application of Rule G-34 to Municipal Advisors

PFM agrees that the disclosure of information materially affecting existing bond holders under Rule 15c2-12 is reasonable and appropriate and that increased market transparency is a valuable benefit. However, placing the obligation, administration, and economic burden on municipal advisors does not and will not sufficiently accomplish the stated transparency objectives in order to outweigh the associated costs in terms of digression from a municipal advisor's regulatory mission to the benefit of issuers; nor can it ultimately move the needle to fully satisfy the outlined objective of providing investors with an ability to truly understand any and all related risks. Rather than creating new regulation and compelling municipal advisors to perform certain disclosure distribution functions for documentation and information otherwise not generally available, municipal entities disclosures for pre-existing debt holders and potential investors could be supported by the long-anticipated clarification of "materiality" and application of current continuing disclosure requirements under Rule 15c2-12 as discussed above.

Additionally, application of Rule G-34 to municipal advisors as proposed by the draft amendments will not be the hoped for panacea to resolve the state of imperfect information for investors, since municipal issuers are not required to use municipal advisors in any transaction, including private placement transactions. Thus, in transactions where neither a municipal advisor nor a broker, dealer or municipal securities dealer acting as an underwriter or placement agent is involved in a private placement transaction or direct bank loan, investors in existing issuances would be in the same position as they are in today. Very often a municipal advisor may not be included in these borrower-provider transactions, may only be hired to perform certain administrative functions, or often only learns of a prior transaction when assisting with the issuance of a municipal entity's next public offering of municipal securities. In any such instances, in order to achieve the transparency sought by the MSRB in its draft amendments to Rule G-34, the MSRB will also need to clarify the process of a municipal entity obtaining a CUSIP where neither a municipal advisor nor a broker, dealer or municipal securities dealer acting as an underwriter is involved in a private transaction; PFM is not supportive of further indirect regulation of our municipal entity clients given the corresponding cost/benefit analysis. PFM would implore the MSRB to resist



creation of a regulatory scheme that results in a well-intended, but ill-fated attempt at compromise between the inability to directly require issuers to file disclosures and the objective to protect the interests of the municipal marketplace.

Further, the MSRB should provide guidance regarding the responsible market participant and process of obtaining a CUSIP in instances where the municipal entity borrower may have multiple municipal advisors involved in a new private placement transaction or direct bank loan, including where one of the municipal advisors involved in the transaction is designated as the municipal entity's independent registered municipal advisor with respect to the same aspects of a municipal financial product or an issuance of municipal securities for purposes of Rule 15Ba1-1(d)(3)(vi)⁹ of the Exchange Act or, alternatively, where no municipal advisor involved in the transaction is designated as the municipal entity's IRMA.

The expressed legislative and regulatory purpose with respect to a municipal advisor focuses upon the fiduciary duty owed to municipal entities and obligated persons.¹⁰ The shift underlying the draft amendments to Rule G-34 will inappropriately place municipal advisors in the tenuous position of serving dual interests, that of the municipal issuer and that of investors, which undermines the very core principles of the regulatory regime. Municipal advisors owe a duty of care and loyalty to their clients and cannot be put in a position to choose between the statutory fiduciary duty to the issuer¹¹ and the requirements underlying the proposed draft amendments to Rule G-34 of newfound investor-driven regulatory disclosure requirements for non-publicly sold bond activities. While harmonization of certain MSRB regulation between broker-dealers and municipal advisors is an ongoing objective for the MSRB and market participants alike, one cannot lose sight of important distinctions separating the interests of all involved with the corresponding checks and balances.

Unintended Adverse Economic Consequences and Market Inefficiencies for Issuers

From the issuer's perspective the potential benefits and considerations of private transactions may include some, or any combination of, the following: lower true interest and transaction costs; greater flexibility with respect to the structuring and terms of the financing; and typically, a simpler execution process, because the issuer interacts directly with the providers/lenders, rather

⁹ 17 CFR 240.15Ba1-1(d)(3)(vi)(A); See also, *Registration of Municipal Advisors*, SEC Rel. No. 34-70462 (Sep. 20, 2013), 78 FR 67468, 67472 (Nov. 12, 2013) ("Adopting Release").

¹⁰ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929-2, 124 Stat. 1376, 1871 (2010) (codified at 15 U.S.C. § 78o).

¹¹ See, 15 U.S.C. 780-4(c)(1).



than with multiple bondholders through intermediaries. From the purchaser's perspective, providing financing by means of a direct purchase or bank loan also has advantages, including: direct interaction with the issuer; direct communication with the issuer regarding the transaction structure; and confidence that the transaction will become part of the provider's investment portfolio. These benefits, nevertheless, are diminished and at some point along the spectrum may reflect net costs to the issuer directly or indirectly by dampening interest of potential providers and administrative, economic, and timing costs. Moreover, the current process of applying for a CUSIP requires provision of an offering document, which in a private transaction may not otherwise have been prepared, adding both legal and administrative costs to create a legal document just to comply with the regulatory requirement of obtaining a CUSIP. Assuming, *arguendo*, the CUSIP application process is revised to accommodate this new regulatory requirement, and an offering document is no longer required for application for a CUSIP on certain transactions, obtaining the CUSIP nevertheless adds another step and undue economic burden to the transaction closing process. Any additional burden is more keenly inequitable for municipal issuers that only use privately placed transactions and have no publicly issued debt.

Final Considerations

While we continue to be supportive of the consistent objectives of the MSRB in seeking to facilitate market transparency and efficiency, PFM also remains fundamentally against the extension of the obligations set forth in Rule G-34 to a municipal advisor as proposed in the draft amendments, thereby creating a direct duty with respect to the discrete interests of investors. Previous occasions have afforded Congress and the SEC multiple opportunities to enact provisions intended to have the municipal advisor also directly serve interests of investors and neither institution has done so to date. By way of refrain, Congress and the SEC have declined to bridge natural and necessary differences between brokers, dealers and underwriters on the one hand and municipal advisors on the other hand leaving intact what the MSRB perceives as "regulatory imbalance" in the draft proposed Rule G-34. If changes are to be made to these core precepts, we respectfully point to the need for Congressional and/or SEC action rather than action by the MSRB in making such a change in the fabric of the municipal advisory regulatory regime.



While PFM continues to be supportive of the consistent objectives of the MSRB in seeking to facilitate market transparency and efficiency, we remain fundamentally opposed to the extension of the obligations set forth in Rule G-34 for a non-dealer municipal advisor as proposed in the initial and second draft amendments, thereby creating a direct duty with respect to the discrete interests of investors. Insofar as obtaining CUSIPS facilitates the clearance and settlement of securities, under the proposed amendments to Rule G-34 non-dealer municipal advisors would be inappropriately burdened with the responsibility of engaging in activity that falls outside the purview of their scope of service and epitomizes traditional broker-dealer type activity. Previous occasions have afforded Congress and the SEC multiple opportunities to enact provisions intended to have the municipal advisor also directly serve interests of investors and neither institution has done so to date. By way of refrain, Congress and the SEC have declined to bridge natural and necessary differences between brokers, dealers and underwriters on the one hand and municipal advisors on the other hand leaving intact what the MSRB perceives as "regulatory imbalance" in the draft proposed Rule G-34. If changes are to be made to these core precepts, we respectfully point to the need for Congressional and/or SEC action rather than action by the MSRB in making such a change in the fabric of the municipal advisory regulatory regime.

We continue to believe that the Commission's opportunity to carefully consider and respond (including with rule modifications) to any comments submitted to its proposed amendments to Rule 15c2-12 would provide an essential foundation to any action on the proposed changes to MSRB Rule G-34.

PFM welcomes the opportunity to further discuss our comments with the MSRB, accordingly please feel free to contact us if our feedback would be useful.

Respectfully submitted,

Leo Karwejna
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