OMB APPROVAL	
OMB Number:	3235-0045
Expires:	August 31, 2011
Estimated average burden hours per response	38

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * 142

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2011 - * 15
Amendment No. (req. for Amendments *)

Proposed Rule Change by Municipal Securities Rulemaking Board

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * ☒ Amendment * ☐ Withdrawal ☐

Section 19(b)(2) * ☒ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

☐ 19b-4(f)(1) ☐ 19b-4(f)(2) ☐ 19b-4(f)(3) ☐ 19b-4(f)(4) ☐ 19b-4(f)(5) ☐ 19b-4(f)(6)

Exhibit 2 Sent As Paper Document ☐

Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the proposed rule change (limit 250 characters, required when Initial is checked *).

Proposed interpretive notice concerning the application of MSRB Rule G-17 to municipal advisors

Contact Information

Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name * Peg Last Name * Henry

Title * General Counsel, Market Regulation

E-mail * phenry@msrb.org

Telephone * (703) 797-6600 Fax (703) 797-6700

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

Municipal Securities Rulemaking Board

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date 08/24/2011

By Ronald W. Smith
(Name *)

Corporate Secretary
(Title *)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Ronald Smith, rsmith@msrb.org

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information (required)

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change (required)

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

Add Remove View

Exhibit Sent As Paper Document ☐

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

Add Remove View

Exhibit Sent As Paper Document ☐

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of Proposed Rule Change

(a) The Municipal Securities Rulemaking Board (the "MSRB" or "Board") is hereby filing with the Securities and Exchange Commission (the "SEC" or "Commission") a proposed rule change consisting of a proposed interpretive notice (the "Notice") concerning the application of MSRB Rule G-17 to municipal advisors. The MSRB requests that the proposed rule change be made effective on the date that rules defining the term "municipal advisor" under the Securities Exchange Act of 1934 (the "Exchange Act") are first made effective by the Commission or such later date as the proposed rule change is approved by the Commission.

The text of the proposed rule change is set forth below:

INTERPRETIVE NOTICE CONCERNING THE APPLICATION OF MSRB RULE G-17 TO MUNICIPAL ADVISORS ADVISING OBLIGATED PERSONS OR SOLICITING MUNICIPAL ENTITIES ON BEHALF OF OTHERS

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")[1] amended Section 15B of the Securities Exchange Act of 1934 (the "Exchange Act") to provide for the regulation of municipal advisors[2] by the Municipal Securities Rulemaking Board ("MSRB") and to direct the MSRB expressly to protect municipal entities and obligated persons. Among other things, the MSRB was directed to adopt rules that are

> designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest . . . .[3]

Accordingly, the MSRB amended its Rule G-17 to provide: "In the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice."[4] This notice provides guidance on a municipal advisor's duties under Rule G-17 when providing municipal advisory services to an obligated person[5] and a municipal advisor's duties to a municipal entity when undertaking a solicitation of a municipal entity on behalf of another person.[6] The examples discussed in this notice are illustrative only, and are not meant to encompass all obligations of municipal advisors under Rule G-17.

Rule G-17 precludes a municipal advisor from engaging in any deceptive, dishonest, or unfair practice with any person, including a municipal entity or an obligated

person. The rule contains an anti-fraud prohibition. Thus, a municipal advisor must not misrepresent or omit the facts, risks, or other material information about municipal advisory activities undertaken with a municipal entity or obligated person. However, Rule G-17 does not merely prohibit deceptive conduct on the part of the municipal advisor. It also establishes a general duty of a municipal advisor to deal fairly with all persons (including, but not limited to, municipal entities and obligated persons), even in the absence of fraud. Even so, unlike a municipal advisor's duty to its municipal entity client, neither the Dodd-Frank Act, nor Rule G-17 requires a municipal advisor to exercise a fiduciary duty when advising an obligated person, unless that obligated person is itself a municipal entity.[7]

DUTY TO OBLIGATED PERSONS

FAIR DEALING

Suitability and Risk Disclosure. A municipal advisor's duties to its obligated person client under Rule G-17 will vary depending upon whether the municipal advisor has recommended a municipal securities transaction or municipal financial product to its client, or whether it has been asked to review such a transaction or product recommended by another person. If a municipal advisor has recommended such a transaction or product to its client, the advisor must have reasonable grounds for believing that the transaction or product is suitable for the client, based on the client's financial circumstances, objectives, tax status,[8] and any other material information known by the municipal advisor about the client and the transaction or product, after reasonable inquiry.

If a municipal advisor has recommended a transaction or product to its client, the advisor must advise the client of the material risks and characteristics of the structure or product. Such disclosure must be sufficient to allow the obligated person to assess the magnitude of its potential exposure as a result of the transaction or product. The municipal advisor must also advise the client of any incentives for the municipal advisor to recommend the transaction or product and any other associated conflicts of interest in the manner described herein under "Fair Dealing/Disclosure of Conflicts."[9] For example, a municipal advisor that recommends that an obligated person enter into a variable rate demand obligation financing must inform the obligated person of the risk of interest rate fluctuations and the material terms of any associated credit or liquidity facilities (*e.g.*, the risk that the obligated person might not be able to replace the facility upon its expiration and might be required to repay the facility provider over a short period of time). Similarly, a municipal advisor that recommends that an obligated person enter into a municipal derivative contract must disclose the material risks (including market, credit, operational, and liquidity risks) and characteristics of the derivative.

If a municipal advisor has been engaged by its obligated person client to review a municipal securities transaction or municipal financial product recommended by another party (*e.g.*, an underwriter), Rule G-17 requires the municipal advisor to evaluate and advise the client of the material risks and characteristics of the transaction or product and

to further advise the client as to whether the advisor has reasonable grounds for believing that the transaction or product recommended by another party is suitable for the client, based on the client's financial circumstances, objectives, tax status, and any other material information known by the municipal advisor about the client and the transaction or product. The municipal advisor is not required to have considered then reasonably feasible alternatives unless otherwise requested to do so by the client. Furthermore, the municipal advisor need not advise its client as to the suitability of a transaction or product recommended by another party if it has expressly disclaimed that obligation in its engagement letter or other writing with the client.

Due Care. In all cases, the municipal advisor's Rule G-17 duty to deal fairly requires it to exercise due care in the provision of advice to its obligated person client, which requires that the municipal advisor possess the necessary capacity, resources, and knowledge to render informed advice. A municipal advisor must not undertake a swap advisory engagement or security-based swap advisory engagement unless it has sufficient knowledge to evaluate the transaction and its risks, as well as the pricing and the appropriateness of the transaction.[10] The municipal advisor must also have a reasonable basis for any representations it makes in any certificate it signs that will be relied upon by other parties to the transaction. A municipal advisor's obligation to act with due care does not make the municipal advisor a guarantor of a successful financing or a guarantor that there are no facts material to its client's decision-making process other than the ones known by the municipal advisor and disclosed to the client.

Disclosure of Conflicts. The municipal advisor's Rule G-17 duty to deal fairly with an obligated person client requires the municipal advisor to disclose material conflicts of interest, such as those that may color its judgment and impair its ability to render unbiased advice to its client. Such conflicts of interest include those existing at the time the engagement is entered into, and those discovered or arising during the course of the engagement. All disclosures of conflicts, including those discovered or arising during the course of the engagement, must be made in writing to an official of the obligated person that the municipal advisor reasonably believes has the authority to bind the obligated person by contract with the municipal advisor. Such disclosures must be made in a manner sufficiently detailed to inform the obligated person of the nature and implications of the conflict. The following are examples of the types of conflicts that must be disclosed by the municipal advisor, but this list is not intended to be exhaustive:

(i) payments by municipal advisors made for the purpose of obtaining or retaining municipal securities business;

(ii) payments from third parties to the municipal advisor in relation to the municipal advisory engagement;

(iii) payments from third parties to enlist the municipal advisor's recommendation of their services to the obligated person;

(iv) whether the municipal advisor or an affiliate of the municipal advisor is acting as a principal in matters concerning the municipal advisory engagement;

(v) the form of compensation for the municipal advisory engagement; and

(vi) other engagements or relationships that might impair the municipal advisor's ability to provide unbiased advice to its obligated person client.

Failure to disclose conflicts of interest has resulted in various SEC enforcement actions and administrative proceedings for, among other things, violations of Rule G-17 by dealer financial advisors.[11] If a conflict is so significant that it is described in this notice as an unfair, deceptive, or dishonest practice, such conflict would preclude a municipal advisor from undertaking an engagement with an obligated person client and disclosure of such conflict would not be effective in permitting such engagement to be undertaken.

Informed Consent. In addition to its duty to disclose various conflicts, Rule G-17 also requires the municipal advisor to obtain informed consent from its obligated person client to each of the conflicts disclosed. The municipal advisor must receive written consent to its conflicts by an official of the obligated person that the municipal advisor reasonably believes has the authority to bind the obligated person by contract with the municipal advisor before the municipal advisory engagement begins or, in the case of conflicts discovered or arising after the municipal advisory engagement has begun, before the municipal advisor may continue to provide such services. For purposes of Rule G-17, an obligated person client will be deemed to have consented to conflicts that are clearly described in its engagement letter or other written contract with the municipal advisor, if the obligated person client expressly acknowledges the existence of such conflicts. If the official of the obligated person client agrees to proceed with the municipal advisory engagement after receipt of the conflicts disclosure but will not provide written acknowledgement of such conflicts, the municipal advisor may proceed with the engagement after documenting with specificity why it was unable to obtain such written acknowledgement.

Disclosure of conflicts, coupled with written consent, will not satisfy the requirements of Rule G-17 in instances in which the municipal advisor has reason to believe that such consent is not informed. In such cases, a municipal advisor must make additional efforts reasonably designed to inform the officials of the obligated person client of the nature and implications of the municipal advisor's conflicts. Additionally, disclosures to an official of the obligated person who is a party to the conflict of interest (such as recipients of payments from municipal advisors) will not satisfy the requirements of Rule G-17.

Forms of Compensation. The manner in which municipal advisors are compensated varies according to the nature of the engagement and the requirements of the obligated person client, among other factors. Pursuant to Rule G-17, a municipal

advisor must provide written disclosure to its obligated person client of what the amount (in dollars and to the extent it can be quantified) of its direct compensation and indirect compensation (*e.g.*, amounts paid to affiliates) from the engagement will be, or is projected to be, as well as the scope of services to be provided for that compensation. Additionally, except as provided below, the municipal advisor must provide written disclosure to its client of the conflicts of interest associated with various forms of compensation, including the form of compensation applicable to its engagement. One way in which a municipal advisor may satisfy its obligation to provide written disclosure of the conflicts with various forms of compensation is to provide its client with the document entitled "Disclosure of Conflicts of Interest With Various Forms of Compensation," attached as Appendix A to this notice (the "Compensation Disclosure Document"). The disclosures described in this paragraph must be provided as described above under "DUTY TO OBLIGATED PERSONS/FAIR DEALING/Disclosure of Conflicts." Provision by the municipal advisor to its client of the Compensation Disclosure Document will not satisfy the municipal advisor's obligation to disclose conflicts of interest not addressed in the Compensation Disclosure Document, such as payments from third parties. Notwithstanding the foregoing, if the obligated person client has required that a particular form of compensation be used, the compensation conflicts disclosure provided by the municipal advisor need only address that particular form of compensation.

DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES

Misrepresentations. Rule G-17 requires that all representations made by municipal advisors to their obligated person clients, whether written or oral, must be truthful and accurate, and municipal advisors must not omit material facts. For example, a municipal advisor's response to an obligated person's request for proposals or qualifications must fairly and accurately describe the municipal advisor's capacity, resources, and knowledge to perform the proposed municipal advisory engagement as of the time the proposal is submitted and must not contain any representations or other material information about such capacity, resources, or knowledge that the municipal advisor knows or should know to be inaccurate or misleading. Matters not within the personal knowledge of those preparing the response (*e.g.*, pending litigation) must be confirmed by those with knowledge of the subject matter. A municipal advisor may not represent that it has the requisite knowledge or expertise with respect to a particular type of transaction or product if the personnel that it intends to work on the engagement do not have the requisite knowledge or expertise.

Excessive Compensation. The MSRB recognizes that what is considered reasonable compensation for a municipal advisor will vary according to the municipal advisor's expertise, the complexity of the financing, whether the fee is contingent upon the closing of the transaction, and the length of time spent on the engagement, among other factors. However, in certain cases and depending upon the specific facts and circumstances of the engagement, a municipal advisor's compensation may be so disproportionate to the nature of the municipal advisory services performed as to indicate that the municipal advisor is engaging in an unfair practice in violation of Rule G-17.[12]

Payments from third parties are included in determining whether compensation is excessive. Furthermore, the MSRB notes that municipal advisors subject to hourly billing arrangements must not submit bills that do not accurately reflect the nature of the services performed and the personnel performing them.

Kickbacks and Other Payments. Kickback arrangements, or certain fee-splitting arrangements, with underwriters or the providers of investments or services to obligated persons also represent unfair, dishonest, and deceptive practices that are prohibited by Rule G-17,[13] as do payments by municipal advisors made for the purpose of obtaining or retaining municipal advisory business other than reasonable fees paid to a municipal advisor described in Section 15B(e)(9) of the Exchange Act.[14]

SOLICITATION OF A MUNICIPAL ENTITY

While the Dodd-Frank Act imposes a fiduciary obligation on municipal advisors acting on behalf of their municipal entity clients, municipal advisors are not required to exercise a fiduciary duty when soliciting municipal entities on behalf of unrelated third parties (in such capacity, a "solicitor"). Solicitors are, however, subject to Rule G-17, and are required to deal fairly with the municipal entities they solicit and not engage in conduct that is deceptive, dishonest, or unfair.

FAIR DEALING

Disclosure of Material Facts about Solicitation. Under its Rule G-17 duty to deal fairly, a solicitor must provide written disclosure of all material facts about the solicitation to the municipal entity being solicited, including:

(i) the name of the solicitor's client;

(ii) the type of business being solicited;

(iii) the amount of the solicitor's compensation;

(iv) the source of all compensation received by the solicitor;

(v) payments (including in-kind) made by the solicitor to facilitate the solicitation regardless of characterization; and

(vi) any relationships of the solicitor with any employees or board members of the municipal entity or any other persons affiliated with the municipal entity or its officials who may have influence over the selection of the solicitor's client.

Material Information about Products or Services. In addition to the disclosure obligations described above, if the solicitor has been engaged by its client to present information to the municipal entity about a product or service being offered by the client,

the solicitor is required to disclose all material risks and characteristics of the product or service. The solicitor must also advise the municipal entity of any incentives received by the solicitor (other than compensation from its client) to recommend the product or service, as well as any other associated conflicts of interest regarding the product or service, and must not make material misstatements or omissions when discussing the product or service.

DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES

Kickbacks and Other Payments. Kickbacks, or fee-splitting arrangements with others, made or entered into by solicitors for the purpose of facilitating the solicitation represent unfair, dishonest, and deceptive practices that violate Rule G-17. Persons and firms arranging, making and receiving such payments have been the subject of various enforcement actions by both the SEC and various state authorities.[15]

Lavish Gifts and Gratuities. Lavish gifts and gratuities made to officials of the municipal entity or affiliated parties may improperly influence the decision of the municipal entity to engage the solicitor's client. Generally, a gift will be considered lavish if its value exceeds the limits imposed by MSRB Rule G-20 (on gifts). Government officials controlling the award of public pension fund business have been found to violate federal and state securities laws by the acceptance of such gifts,[16] as have those making the gifts.[17]

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1 Pub. Law. No. 111-203, 124 Stat. 1376 (2010).

2 The term "municipal advisor" is defined in Section 15B(e)(4) of the Exchange Act and the rules and regulations promulgated thereunder.

3 Section 15B(b)(2)(C) of the Exchange Act.

4 Exchange Act Release No. 63599; File No. SR-MSRB-2010-16 (December 22, 2010).

5 The term "obligated person" is defined in Section 15B(e)(10) of the Exchange Act to mean

> any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities.

6 Section 15B(e)(9) of the Exchange Act provides that,

the term "solicitation of a municipal entity or obligated person" means a direct or indirect communication with a municipal entity or obligated person made by a person, for direct or indirect compensation, on behalf of a broker, dealer, municipal securities dealer, municipal advisor, or investment adviser (as defined in section 202 of the Investment Advisers Act of 1940) that does not control, is not controlled by, or is not under common control with the person undertaking such solicitation for the purpose of obtaining or retaining an engagement by a municipal entity or obligated person of a broker, dealer, municipal securities dealer, or municipal advisor for or in connection with municipal financial products, the issuance of municipal securities, or of an investment adviser to provide investment advisory services to or on behalf of a municipal entity.

[7] *See* Section 15B(c)(1) of the Exchange Act. State laws may, however, impose a fiduciary duty on a municipal advisor when providing advice to an obligated person client. For purposes of this notice, the client of the municipal advisor will be presumed not to be a municipal entity. Although a municipal advisor advising an obligated person does not have a fiduciary duty to the municipal entity that is the conduit issuer for the obligated person (but is not the client of the advisor), it still has a fair dealing duty to the municipal entity.

[8] For example, an obligated person that is exempt from tax under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended, is subject to private inurement limitations that may affect how a transaction may be structured. A municipal advisor's obligation to consider an obligated person client's tax status in making a suitability determination does not carry with it an obligation to provide tax advice to the client.

[9] For example, a conflict of interest may exist when the municipal advisor receives compensation from a swap provider for recommending the swap provider to the obligated person.

[10] Section 4s(h)(5) of the Commodity Exchange Act requires that a swap dealer with a special entity client (including states, local governments, and public pension funds) must have a reasonable basis to believe that the special entity has an independent representative that satisfies these criteria, among others. Section 15F(h)(5) of the Exchange Act imposes the same requirements with respect to security-based swaps.

[11] *See, e.g.*, *In the Matter of Lazard Freres and Merrill Lynch*, SEC Release No. 34-36419 (Oct. 26, 1995) (settlement in connection with alleged violation of Rule G-17 due to failure of underwriter and financial advisor to disclose payments made by underwriter to financial advisor); *In re Wheat, First Securities, Inc.*, SEC Initial Dec. Release No. 155 (Dec. 17, 1999) (administrative law judge found

violation of Rule G-17 by financial advisor for making false disclosure to municipal entity that it had not employed a lobbyist to secure its advisory contract with the county and that it had not entered into an arrangement with a third party to make payments contingent upon its securing the advisory contract); *In re Pryor, McClendon, Counts & Co., Inc. et al.*, Exchange Act Release No. 48095 (Jun. 26, 2003) (settlement in connection with alleged violation of Rule G-17 for financial advisor's failure to disclose payment to government official made to secure advisory assignment).

[12] *See, e.g.*, the following cases for examples of excessive compensation arrangements: *In re O'Brien Partners, Inc.*, Exchange Act Release No. 7594 (Oct. 27, 1998) (settlement in connection with investment adviser allegedly received "referral fees" from a finder that assisted in the reinvestment of municipal bond proceeds in guaranteed investment contracts, repurchase agreements and forwards; referral fees allegedly totaled $450,000 and represented 50-60% of finder commission); *In the Matter of Mark S. Ferber*, Exchange Act Release No. 38102 (Dec. 31, 1996) (settlement in connection with financial advisor allegedly received payments from broker-dealer totaling almost $6 million over two years in exchange for recommendations that his clients select that broker-dealer as underwriter or provider of other financial services, including interest rate swaps); *In the Matter of Arthurs Lestrange & Co., Inc. and Michael Bova*, SEC Release Nos. 33-7775, 34-42148 (Nov. 17, 1999) (settlement in connection with financial advisor allegedly engaged in fee splitting arrangement under which financial advisor contributed its financial advisory fee of $210,000 to pool of advisory and brokerage service compensation, received $1.5 million from the investment broker, and paid $500,000 to a finder); *In the Matter of William R. Hough & Co.*, SEC Release Nos. 33-7826, 34-42632 (Apr. 6, 2000) (settlement in connection with financial advisor allegedly received $35,000 for its financial advisory services and $400,000 from the investment provider; financial advisor allegedly received $300,000 from a forward supply contract provider for "developing a forward supply assignment program"); *In the Matter of John S. Reger and Business & Financial Advisors, Inc.*, SEC Release No. 33-7973 (Apr. 23, 2001) (settlement in connection with financial advisor allegedly received $129,000 kickback from escrow securities provider, representing 40% of escrow provider's profit).

[13] *Id.* Rule G-17 does not preclude a municipal advisor from receiving payment for its municipal advisory services from a third party, as long as the municipal advisor discloses, and the obligated person client provides its informed written consent to, such payment arrangement and the amount of such payment. As with the disclosure of other conflicts of interest, such disclosure must be made before the municipal advisory engagement is entered into, or at the time the conflict arises, if later.

[14] *See* the cases at note 12, *supra*. Municipal advisors that are described in Section 15B(e)(9) of the Exchange Act because they solicit business from municipal

entities on behalf of other municipal advisors are subject to all MSRB rules for municipal advisors.

15 *See, e.g., SEC v. Steven L. Rattner*, SEC Lit. Release No. 21748 (November 18, 2010) (SEC alleged that defendant violated Section 17(a)(2) of the Securities Act of 1933 by securing investments in his private equity firm from a state retirement fund after he arranged for a firm affiliate to distribute a movie produced by the retirement fund's chief investment officer and his brothers; defendant then allegedly caused his firm to retain an advisor and fundraiser for a former state comptroller as a "placement agent" and pay him more than $1 million in sham fees even though the defendant was already dealing directly with the state deputy comptroller and did not need an introduction to the retirement fund); *SEC v. Henry Morris, et al.*, SEC Lit. Release Nos. 20963, 21001, 21018 and 21036 (filed March 19, 2009, April 15, 2009, April 30, 2009 and May 12, 2009, respectively) (SEC alleged that defendants and others required investment managers seeking to do business with the state retirement fund to make payments to unrelated finders and placement agents who then made payments or other benefits as directed by state officials); *see also* Allocution to Violation of New York State's Martin Act by Henry Morris, http://www.ag.ny.gov/media_center/2010/nov/Exhibit_A_ocr.pdf.

16 Allocution to Violation of New York State's Martin Act by Alan G. Hevesi, http://www.ag.ny.gov/media_center/2010/oct/pdfs/Hevesi_Allocution.pdf (state comptroller who controlled investment decisions of state retirement fund accepted paid vacation for himself and his family paid for by official of private equity fund soliciting business from the retirement fund).

17 Announcement of Plea Agreement of Elliott Broidy with New York State Attorney General, http://www.ag.ny.gov/media_center/2009/dec/dec3b_09.html (plea to violation of New York State Martin Act by defendant for his involvement in a pay to play kickback scheme at the state comptroller office in connection with the state retirement fund's investment in a fund operated by defendant's firm; defendant paid at least $75,000 for first class airfare, luxury hotel suites, a car and driver, a helicopter tour, and security detail on vacation trips for high ranking official of the state retirement fund and concealed those payments through charities and false invoices).

* * * * * *

APPENDIX A

DISCLOSURE OF CONFLICTS OF INTEREST WITH VARIOUS FORMS OF COMPENSATION

The Municipal Securities Rulemaking Board requires us, as your municipal advisor, to provide written disclosure to you about the actual or potential conflicts of interest

presented by various forms of compensation. We must provide this disclosure unless you have required that a particular form of compensation be used. You should select a form of compensation that best meets your needs and the agreed upon scope of services.

Forms of compensation; potential conflicts. The forms of compensation for municipal advisors vary according to the nature of the engagement and requirements of the client, among other factors. Various forms of compensation present actual or potential conflicts of interest because they may create an incentive for an advisor to recommend one course of action over another if it is more beneficial to the advisor to do so. This document discusses various forms of compensation and the timing of payments to the advisor.

Fixed fee. Under a fixed fee form of compensation, the municipal advisor is paid a fixed amount established at the outset of the transaction. The amount is usually based upon an analysis by the client and the advisor of, among other things, the expected duration and complexity of the transaction and the agreed-upon scope of work that the advisor will perform. This form of compensation presents a potential conflict of interest because, if the transaction requires more work than originally contemplated, the advisor may suffer a loss. Thus, the advisor may recommend less time-consuming alternatives, or fail to do a thorough analysis of alternatives. There may be additional conflicts of interest if the municipal advisor's fee is contingent upon the successful completion of a financing, as described below.

Hourly fee. Under an hourly fee form of compensation, the municipal advisor is paid an amount equal to the number of hours worked by the advisor times an agreed-upon hourly billing rate. This form of compensation presents a potential conflict of interest if the client and the advisor do not agree on a reasonable maximum amount at the outset of the engagement, because the advisor does not have a financial incentive to recommend alternatives that would result in fewer hours worked. In some cases, an hourly fee may be applied against a retainer (*e.g.,* a retainer payable monthly), in which case it is payable whether or not a financing closes. Alternatively, it may be contingent upon the successful completion of a financing, in which case there may be additional conflicts of interest, as described below.

Fee contingent upon the completion of a financing or other transaction. Under a contingent fee form of compensation, payment of an advisor's fee is dependent upon the successful completion of a financing or other transaction. Although this form of compensation may be customary for the client, it presents a conflict because the advisor may have an incentive to recommend unnecessary financings or financings that are disadvantageous to the client. For example, when facts or circumstances arise that could cause the financing or other transaction to be delayed or fail to close, an advisor may have an incentive to discourage a full consideration of such facts and circumstances, or to discourage consideration of alternatives that may result in the cancellation of the financing or other transaction.

Fee paid under a retainer agreement. Under a retainer agreement, fees are paid to a municipal advisor periodically (*e.g.*, monthly) and are not contingent upon the

completion of a financing or other transaction. Fees paid under a retainer agreement may be calculated on a fixed fee basis (*e.g.*, a fixed fee per month regardless of the number of hours worked) or an hourly basis (*e.g.*, a minimum monthly payment, with additional amounts payable if a certain number of hours worked is exceeded). A retainer agreement does not present the conflicts associated with a contingent fee arrangement (described above).

Fee based upon principal or notional amount and term of transaction. Under this form of compensation, the municipal advisor's fee is based upon a percentage of the principal amount of an issue of securities (*e.g.*, bonds) or, in the case of a derivative, the present value of or notional amount and term of the derivative. This form of compensation presents a conflict of interest because the advisor may have an incentive to advise the client to increase the size of the securities issue or modify the derivative for the purpose of increasing the advisor's compensation.

[If applicable, describe other form of compensation for the engagement and associated conflicts with a comparable level of specificity].

Acknowledgement

The undersigned hereby acknowledges that he/she has received this disclosure and that he/she has been given the opportunity to raise questions and discuss the foregoing matters with the advisor.

_____ [name of client]
By: _____
Name: _____
Title: _____
Date: _____

* * * * * *

2. Procedures of the Self-Regulatory Organization

The proposed interpretive notice was adopted by the MSRB at its May 19-20, 2011 and July 27-29, 2011 meetings. Questions concerning this filing may be directed to Peg Henry, General Counsel, Market Regulation, or Karen Du Brul, Associate General Counsel, at 703-797-6600.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")[1], the MSRB was expressly directed by Congress to

[1] Pub. L. No. 111-203, 124 Stat. 1376 (2010).

protect municipal entities and obligated persons. Accordingly, the MSRB is proposing to provide interpretive guidance that addresses how Rule G-17 applies to municipal advisors when advising obligated person clients or when soliciting municipal entities on behalf of others.

A more-detailed description of the provisions of the Notice follows:

Duty to Obligated Persons; Fair Dealing. The Notice would provide that the Rule G-17 duty of fair dealing requires that the municipal advisor determine if a recommended municipal securities transaction or municipal financial product is suitable for its obligated person client, and that it provide disclosure of the material risks and characteristics of the transaction or product, as well as any incentives the municipal advisor has received for recommending the transaction or product and any other associated conflicts of interest. Further, under the Notice, the Rule G-17 duty of fair dealing would require that the municipal advisor exercise due care when providing advice to the obligated person client, and not undertake an engagement if the municipal advisor does not have the necessary skills and resources to perform its duties in respect of the engagement.

The Notice also would provide that the municipal advisor must disclose all material conflicts of interest such as those that may color its judgment and impair its ability to render unbiased advice to its obligated person client, including those existing at the time the engagement is entered into, and those discovered or arising during the course of the engagement. The municipal advisor would be required to make these disclosures in writing and, in general, to obtain the informed consent thereto by an official of the obligated person having the authority to bind the obligated person by contract with the municipal advisor. Conflicts that constituted an unfair, deceptive, or dishonest practice would preclude a municipal advisor from undertaking an engagement with an obligated person client and disclosure of such conflict would not be effective in permitting such engagement to be undertaken.

The Notice would provide that a municipal advisor is required to provide written disclosure of the amount of its direct compensation and indirect compensation (e.g., amounts paid to affiliates) from the engagement, and the scope of services to be provided. The municipal advisor would also be required to provide written disclosure of the conflicts of interest associated with various forms of compensation, including the form of compensation applicable to its engagement, unless the obligated person client has required a particular form of compensation, in which case such disclosure would only need to address that particular form of compensation.

Deceptive, Dishonest or Unfair Practices. The Notice would provide that all representations made by municipal advisors to their obligated person clients, whether written or oral, must be truthful and accurate, and municipal advisors must not omit material facts, and that matters not within the personal knowledge of those preparing the response (e.g., pending litigation) must be confirmed by those with knowledge of the subject matter. A municipal advisor would not be permitted to represent that it has the

requisite knowledge or expertise with respect to a particular type of transaction or product if the personnel that it intends to work on the engagement do not have the requisite knowledge or expertise.

The Notice would provide that in certain cases and depending upon the specific facts and circumstances of the engagement, a municipal advisor's compensation, including payments from third parties, may be so disproportionate to the nature of the municipal advisory services to be an unfair practice in violation of Rule G-17.

The Notice would also provide that kickback arrangements, and certain fee-splitting arrangements, with underwriters or the providers of investments or services to obligated persons are unfair, dishonest, and deceptive practices that are prohibited by Rule G-17, as are payments by municipal advisors made for the purpose of obtaining or retaining municipal advisory business, other than reasonable fees paid to a municipal advisor regulated by the MSRB.

Solicitation of a Municipal Entity; Fair Dealing. The Notice would provide that, while municipal advisors are not required to exercise a fiduciary duty when soliciting municipal entities on behalf of third parties (in such capacity, a "solicitor"), they are required to deal fairly with the municipal entities they solicit and not engage in conduct that is deceptive, dishonest, or unfair.

The Notice would provide that a solicitor must provide written disclosure of all material facts about the solicitation to the municipal entity being solicited, including, among other things, the amount and source of all compensation received by the solicitor, any payments (including in-kind) made by the solicitor to facilitate the solicitation regardless of characterization; and any relationships of the solicitor with any employees, board members, or affiliated persons of the municipal entity or its officials who may have influence over the selection of the solicitor's client.

The Notice would provide that the solicitor, if engaged by its client to present information to the municipal entity about a product or service being offered by the client, is required to disclose all material risks and characteristics of the product or service, as well as any incentives received by the solicitor (other than compensation from its client) to recommend the product or service, and any other conflicts of interest regarding the product or service.

Deceptive, Dishonest or Unfair Practices. The Notice would provide that kickbacks and fee-splitting arrangements with others, made or entered into by solicitors for the purpose of facilitating the solicitation are unfair, dishonest, and deceptive practices that violate Rule G-17. The Notice would also provide that lavish gifts and gratuities (that exceed limits set forth in MSRB Rule G-20) made to officials of the municipal entity or affiliated parties may improperly influence the decision of the municipal entity to engage the solicitor's client, and may therefore be a violation of Rule G-17.

(b) The MSRB believes that the proposed interpretive notice is consistent with Section 15B(b)(2) of the Exchange Act, which provides that:

> The Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

Section 15B(b)(2)(C) of the Exchange Act, provides that the rules of the MSRB shall:

> be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

The proposed rule change is consistent with Section 15B(b)(2) of the Exchange Act because it will protect obligated persons and municipal entities from fraudulent and manipulative acts and practices and promote just and equitable principles of trade, as well as emphasizing the duty of fair dealing owed by municipal advisors to their obligated person clients and to municipal entities when soliciting such entities on behalf of third parties. Rule G-17 has two components, one an anti-fraud prohibition, and the other a fair dealing requirement (which promotes just and equitable principles of trade). The Notice would address both components of the rule. The sections of the Notice entitled "DUTY TO OBLIGATED PERSONS/DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES" and "SOLICITATION OF A MUNICIPAL ENTITY/DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES" primarily would provide guidance as to conduct required to comply with the anti-fraud component of the rule and, in some cases, conduct that would violate the anti-fraud component of the rule, depending on the facts and circumstances. The sections of the Notice entitled "DUTY TO OBLIGATED PERSONS/FAIR DEALING" and "SOLICITATION OF A MUNICIPAL ENTITY/FAIR DEAING" primarily would provide guidance as to conduct required to comply with the fair dealing component of the rule.

Section 15B(b)(2)(L)(iv) of the Exchange Act requires that rules adopted by the Board:

not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

The proposed rule change is necessary for the protection of obligated persons and municipal entities and the robust protection of investors against fraud. Many municipal advisors play a key role in the structuring of offerings of municipal securities by obligated persons through municipal entities and the preparation of offering documents used to market those securities to investors. In some cases, they advise on the appropriateness of derivatives entered into by obligated persons, the effectiveness of which may have a substantial impact on the finances of their clients. In other cases, they solicit business from public pension funds, which, if not conducted according to the highest standards, may have a substantial effect on the finances of the state and local governments that control those funds. Municipal entities, obligated persons, and investors, therefore, have a substantial interest in municipal advisors conducting their municipal advisory activities fairly and not engaging in fraudulent conduct.

Accordingly, the MSRB does not believe that the proposed rule change would impose an unreasonable burden on small municipal advisors. However, the MSRB recognizes that there are costs of compliance. That is the reason the MSRB has included Appendix A to the Notice. By using Appendix A to provide disclosure concerning compensation conflicts, small municipal advisors will satisfy the compensation disclosure requirement of the Notice without having to retain legal counsel to assist them in the preparation of such disclosure.

4. Self-Regulatory Organization's Statement on Burden on Competition

The MSRB does not believe that the proposed rule change would impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act, since it would apply equally to all municipal advisors advising obligated persons or soliciting third-party business from municipal entities.

5. Self-Regulatory Organization's Statement on Comments Received on the Proposed Rule Change by Members, Participants, or Others.

On February 14, 2011, the MSRB requested comment on a draft of the Notice (the "draft Notice"). The MSRB received comment letters from: the American Federation of State, County and Municipal Employees ("AFSCME"); B-Payne Group Financial Advisors ("B-Payne Group"); Catholic Finance Corporation ("Catholic Finance"); Municipal Regulatory Consulting LLC ("MRC"); the National Association of Independent Public Finance Advisors ("NAIPFA"); Not for Profit Capital Strategies ("Capital Strategies"); Public Financial Management ("PFM"); and the Securities Industry and Financial Markets Association ("SIFMA").

SCOPE OF NOTICE

- **Comment: Delay Provisions Until SEC Rule on Municipal Advisors Finalized.** SIFMA requested that the MSRB withdraw or delay some or all of the provisions of the draft Notice until the SEC has defined "municipal advisor," after which time they asked that the MSRB afford commenters an additional opportunity to comment on the Notice.

- **MSRB Response:** Because Rule G-17 became applicable to municipal advisors on December 23, 2010, the MSRB feels it is important to provide guidance on how the rule applies to municipal advisors. The MSRB has requested that the proposed rule change be made effective on the date that rules defining the term "municipal advisor" under the Exchange Act are first made effective by the SEC, or such later date that the SEC approves the proposed rule change. At that time, the MSRB may propose additional guidance, if necessary.

- **Comment: Duty When Advising Obligated Persons.** Capital Strategies requested that the MSRB clarify a municipal advisor's duty when a financing alternative for a municipal advisor's obligated person client is not in the best interests of a municipal entity.

- **MSRB Response:** The MSRB determined to address these comments by revising the Notice so that it would provide (in endnote 7): "Although a municipal advisor advising an obligated person does not have a fiduciary duty to the municipal entity that is the conduit issuer for the obligated person (but is not the client of the advisor), it still has a fair dealing duty to the municipal entity." Thus, when a municipal advisor is advising an obligated person, its primary obligation of fair dealing is to its client. The municipal advisor would not be required to act in the best interests of the municipal entity acting as a conduit issuer, although the advisor would be prohibited from acting in a deceptive, dishonest or unfair manner.

- **Comment: Interpretation of Fair Dealing Too Broad.** SIFMA said that the draft Notice interpreted a municipal advisor's fair dealing obligations far beyond the common understanding of "fair dealing" and beyond prior interpretations of fair dealing as applied to brokers, dealers, and municipal securities dealers ("dealers"). SIFMA said that the draft Notice imposed many "fiduciary-like" obligations on municipal advisors when advising entities other than municipal entities. SIFMA further commented that concepts of a duty of care and a duty to disclose conflicts and obtain consent have never before been interpreted to be part of a duty to deal fairly under Rule G-17, and that imposing these duties under Rule G-17 may be inconsistent with existing obligations of currently regulated persons.

- **MSRB Response:** The MSRB has determined not to make any changes to the Notice based on these comments. The MSRB notes that prior interpretations of the concept of "fair dealing" with respect to dealers applied to counterparty, not

advisory, relationships, and that a comparison between such prior interpretations and duties applicable to an advisor would therefore be inappropriate. Further, the MSRB considered carefully the violations of fair dealing and fiduciary duty in numerous state and federal cases, as well as SEC proceedings, and determined that fair dealing obligations and fiduciary obligations in an advisory relationship were closely aligned and not as disparate as SIFMA might suggest.

DUTY TO OBLIGATED PERSONS

Appropriateness; Due Care.

- **Comment: Revise "Appropriateness" Standard.** SIFMA questioned whether the draft Notice created a new standard of conduct by requiring a municipal advisor to advise an obligated person client as to the appropriateness of a municipal financial product or transaction or whether "appropriateness" was intended by the MSRB to mean the same thing as "suitability." SIFMA and MRC said that the MSRB should define the duty to be consistent with other suitability standards currently applicable to dealers.

- **MSRB Response:** The MSRB determined to address this comment by revising the Notice so that it would substitute the term "suitability" for the term "appropriateness" and to provide that the municipal advisor must have reasonable grounds for believing that a recommended municipal securities transaction or municipal financial product is suitable for the client, based on certain information about the client and the product or transaction known by the municipal advisor.

- **Comment: Address Competing Standards.** SIFMA said that the MSRB should not impose an appropriateness standard on regulated entities that were already subject to a competing standard. SIFMA said that the Rule G-17 obligation to advise obligated person clients of material risks should be deemed satisfied if the municipal advisor complied with similar requirements under another applicable regulatory regime. Further, SIFMA said that this duty should be limited to specified transactions and not extended to ordinary course transactions such as bank deposits and the issuance of fixed or floating rate debt.

- **MSRB Response:** The MSRB disagrees in part with these comments and accordingly has determined not to make the changes to the Notice suggested by these comments, except as noted above. As noted above, the MSRB revised the Notice so that it would substitute the word "suitability" for the term "appropriateness" to align what SIFMA suggested might be potentially conflicting regulatory regimes. Further, the municipal advisor would not be deemed to have automatically satisfied the requirements of Rule G-17 by satisfying the requirements of another regulatory regime. The MSRB believes that adoption of SIFMA's comments with respect to ordinary course transactions would negate a significant purpose of the Notice.

- **Comment: Risk Disclosure; Duplication and Scope.** Catholic Finance suggested that where an underwriter had proposed a specific transaction and had adequately disclosed the risks, the municipal advisor need not also disclose the risks. Catholic Finance also requested clarification about whether the disclosure of risks and material incentives had to be in writing, as well as whether the same disclosures needed to be repeated to experienced clients in similar, successive transactions.

- **MSRB Response:** The MSRB has determined not to make the changes suggested by these comments. While a municipal advisor would not be required to disclose the same risks that an underwriter has disclosed, the municipal advisor would be required to determine the adequacy of such disclosure and advise its client as to whether the municipal advisor had reasonable grounds for believing the transaction or product recommended by the underwriter is suitable for such client. Such evaluation and advice are separate from whatever disclosure the underwriter presents. Further, while the disclosure of material risks would not be required to be in writing, the municipal advisor would be required to disclose any incentives and any other conflicts of interest in writing. Finally, with respect to disclosing the same risks to experienced clients in similar, successive transactions, the municipal advisor would be expected to consider whether disclosure would be advisable in light of new facts or circumstances concerning the client or the market, or the client's choice of new or different personnel directed to complete the transaction.

- **Comment: Determine Status of Client.** Capital Strategies requested that the MSRB clarify a municipal advisor's obligation if the status of its client could not be determined until after substantial advisory activity had taken place, citing an instance of a client initially considering a tax-exempt borrowing (and therefore being considered obligated person) but finally deciding to obtain a bank loan.

- **MSRB Response:** This comment is more appropriately addressed to the SEC, which has the authority to define the term "obligated person" as used in the Exchange Act.

- **Comment: Limit Obligations to Terms of Contract.** SIFMA and NAIPFA argued that a municipal advisor should be required to do only what the obligated person client contracted for, and SIFMA said that an advisor need not expressly disclaim an obligation absent an explicit agreement between the parties. SIFMA also said that Rule G-17 should not imply additional obligations when reviewing a product or transaction recommended to its client by another, specifically the obligation to review for appropriateness and to disclose material risks, outside of what has been specifically contracted for between the parties.

- **MSRB Response:** The MSRB has determined not to make any changes to the Notice as a result of this comment. The MSRB expects that municipal advisors that wish to limit their engagements with obligated persons would do so in

writings (whether as part of engagement letters or separately) that limit the scope of their engagements to particularly enumerated services or which state that any services not specified in the writing would not be provided by the advisor. This should impose no measurable additional cost on the advisor or the obligated person.

- **Comment: Clarify Due Diligence Obligations.** NAIPFA suggested that various duties, such as a duty to investigate or to make reasonable inquiry, appear to be variations on due diligence requirements and requested that they be worded in the same manner in the draft Notice and a proposed interpretive notice under proposed Rule G-36 (on fiduciary duty of municipal advisors). NAIPFA asked that these be revised and clarified. SIFMA suggested that any duty to analyze appropriateness be limited to facts that the municipal advisor was required to obtain under MSRB rules, or otherwise had in its possession, and that no further due diligence be required.

- **MSRB Response:** The MSRB has determined not to make any changes to the Notice based on these comments. The Notice would not impose a "due diligence" obligation upon municipal advisors. However, to the extent that a municipal advisor makes a recommendation, the fulfillment of such advisor's suitability obligation as described above would necessitate that the advisor gather and review the information on which such suitability determination is based. The wording of the Notice differs from that of the Rule G-36 proposed notice because of the different duties owed by municipal advisors to their clients under the two notices.

Disclosure of Conflicts.

- **Comment: Incorporate Requirements of Advisory Contracts in Rule G-23.** MRC suggested that the requirements to disclose conflicts and to obtain informed consent would be more appropriately addressed in MSRB Rule G-23, and that the requirements should be removed from the draft Notice.

- **MSRB Response:** The MSRB disagrees with these comments and has determined not to make any changes to the Notice based on these comments. Rule G-23 only concerns financial advisory activities of dealers with respect to issues of municipal securities. The Notice would be the appropriate place to address these disclosures by all municipal advisors with obligated person clients.

  Comment: Disclose Linking Fees and Engagements. Catholic Finance suggested that disclosure concerning forms of compensation include disclosures by dealer firms offering to link engagements and fees as a municipal advisor with a separate engagement as underwriter on a separate transaction.

  MSRB Response. The MSRB has determined not to make any changes to the Notice based on these comments. The Notice would provide that other, associated

conflicts of interest would be required to be disclosed and described, if applicable. This provision of the Notice would thus address many additional types of conflicts.

Forms of Compensation.

- **Comment: Disclosure of Conflicts Confusing and Unnecessary.** Several commenters suggested that the MSRB delete Appendix A to the draft Notice (Disclosure of Conflicts with Various Forms of Compensation) and the requirement of the Notice that municipal advisors disclose the conflicts with various forms of compensation (B-Payne Group, MRC; NAIPFA; PFM). Commenters argued that the disclosure would be confusing and that the type of fee arrangement (specifically contingent fees) did not affect professional performance. MRC suggested that any disclosure requirements were more appropriately addressed in Rule G-23. NAIPFA suggested that disclosure of conflicts in forms of compensation be limited to the conflicts applicable to the form of compensation methodology at the time the compensation methodology was proposed. NAIPFA also suggested that "pitches" or other discussions of ideas with municipal entities prior to engagement should not require delivery of the disclosure. AGFS supported the proposal to require municipal advisors to clarify the advantages and disadvantages of various forms of compensation.

- **MSRB Response:** The MSRB has determined to revise the Notice so that it would address these comments. Because municipal advisors owe a duty of fair dealing with respect to their obligated person clients, the MSRB considers it essential that they disclose all material conflicts to their clients. The Notice has been revised so that it would provide that, if the obligated person client has required that a particular form of compensation be used, the disclosure provided by the municipal advisor would need only address that form of compensation. The revised Notice would also require that conflicts disclosures, including those regarding compensation, need only be delivered before the municipal advisor has been engaged to provide municipal advisory services, unless the conflicts are discovered or arise later.

  The MSRB has determined not to eliminate Appendix A from the Notice. Appendix A was included in the Notice for the benefit of small municipal advisors to help them avoid the need to hire an attorney to prepare compensation conflicts disclosure associated with common forms of compensation. Use of Appendix A would not be mandatory and municipal advisors would be free to draft their own disclosure addressing these conflicts.

- **Comment: Disclose Fees of All Participants.** B-Payne Group said that fees of all participants (including bond attorneys) should be disclosed.

- **MSRB Response:** In the view of the MSRB, it is appropriate to interpret Rule G-17 differently for arm's-length counterparty relationships on the one hand (such

as underwriters appropriately maintain with issuers) and advisory relationships on the other. The MSRB notes that it does not have jurisdiction over bond lawyers, unless they are functioning as municipal advisors, and, therefore, in most cases, may not require them to disclose compensation conflicts.

- **Comment: Due Diligence to Determine Authority of Municipal Official.** NAIPFA suggested that, in determining the authority of an official of an obligated person client to enter into a contract, to receive various disclosures, and to deliver informed consent, a municipal advisor should be permitted to rely on the apparent authority of such official to acknowledge the conflicts disclosure, assuming the advisor has no reason to believe that such person lacks the requisite authority.

- **MSRB Response:** The MSRB has determined to revise the Notice so that it would provide that a municipal advisor is required to deliver written disclosures of conflicts to, and receive informed consent from, those officials of the obligated person whom the municipal advisor reasonably believes have the authority to bind the obligated person client by contract with the municipal advisor.

- **Comment: Consent Presumed With Receipt of Written Agreement.** NAIPFA suggested that a municipal advisor be permitted to presume consent if it receives an executed contract (or similar document), or verbal agreement that a written engagement letter (or similar document) has been accepted, or written or verbal acknowledgement that the advisor has been selected following a request for proposal ("RFP") process in which the form of compensation was appropriately disclosed and applicable disclosure provided.

- **MSRB Response:** The MSRB notes that the following provisions of the Notice would address this comment. The Notice would provide: "For purposes of Rule G-17, an obligated person client will be deemed to have consented to conflicts that are clearly described in its engagement letter or other written contract with the municipal advisor, if the obligated person client expressly acknowledges the existence of such conflicts. If the official of the obligated person client agrees to proceed with the municipal advisory engagement after receipt of the conflicts disclosure but will not provide written acknowledgement of such conflicts, the municipal advisor may proceed with the engagement after documenting with specificity why it was unable to obtain such written acknowledgement." Accordingly, the MSRB has determined not to make any changes to the Notice to address this comment.

Misrepresentations.

- **Comment: Disclose Only General Conflicts of Interest.** SIFMA said that it would be difficult for an advisor to accurately determine its capacity, resources, and knowledge when discussing a potential engagement with an obligated person client or on a forward-looking basis, and suggested that it be able to satisfy its obligation by providing generalized disclosures about its qualifications.

- **MSRB Response:** The Notice would specify, in the context of a response to an RFP, that the response must accurately describe the municipal advisor's knowledge and capabilities, and prohibits a municipal advisor from making false or misleading statements about its knowledge and capabilities, or omitting material facts about its knowledge and capabilities. The municipal advisor would be expected to base its response on its understanding about the scope of the engagement at that time. If the scope of the engagement changes, the municipal advisor would be prohibited from making false or misleading statements about its continued ability to perform the engagement. Accordingly, the MSRB has determined not to make any changes to the notice based on this comment.

Excessive Compensation.

- **Comment: Definition of Excessive Compensation.** NAIPFA and B-Payne Group requested further clarification on the definition of "excessive compensation." NAIPFA suggested certain criteria, including, among other things: (i) the time and labor required, the novelty and difficulty of the issue involved, and the skill requisite to perform the municipal advisory services properly; (ii) the fee customarily charged in the locality for similar municipal advisory services; (iii) the amount involved and the results obtained; (iv) the nature and length of the professional relationship with the client; (v) the experience, reputation, and ability of the municipal advisor or municipal advisors performing the services; and (vi) whether the fee is fixed or contingent. B-Payne Group objected to any evaluation of whether its fees were excessive, arguing that no regulator was in a position to evaluate the reasonableness of the municipal advisor's fee.

- **MSRB Response:** The MSRB has determined to revise the Notice so that it would address these comments. The Notice would describe excessive compensation as compensation that is so disproportionate to the nature of the municipal advisory services performed as to indicate that the municipal advisor is engaging in an unfair practice in violation of Rule G-17. The MSRB would revise the Notice so that it would provide that "The MSRB recognizes that what is considered reasonable compensation for a municipal advisor will vary according to the municipal advisor's expertise, the complexity of the financing, whether the fee is contingent upon the closing of the transaction, and the length of time spent on the engagement, among other factors." As this language recognizes, many factors can appropriately affect the amount of the fee, and the specific factors listed in the Notice would not be exclusive. Thus, it may be that the various other factors noted by commenters could have an impact on the compensation paid to a municipal advisor. In all cases, the municipal advisor should be able to support the legitimacy of its fees.

SOLICITATION OF A MUNCIPAL ENTITY

Disclosure of Material Facts; Gifts.

- **Comment: Extent of Disclosure May Be of Questionable Value.** SIFMA suggested that the requirement to disclose all relationships with influential employees, board members, or affiliates of the municipal entity may be extensive and of questionable value. Further, SIFMA noted that a solicitor may not be in the best position to disclose all material risks and characteristics, and that such effort will be duplicative of the provider's (its client's) obligation once it has been retained an a municipal advisor.

- **MSRB Response:** The MSRB disagrees with this comment, especially given the relationship-driven business that enforcement actions have revealed. See, e.g., endnote 15 to the Notice. Accordingly, the MSRB has determined not to make any changes to the Notice to address these comments.

- **Comment: Address Gifts in Rule G-20.** SIFMA suggested that the MSRB should address the issue of gifts in MSRB Rule G-20, as it has done for similar prohibitions on dealers.

- **MSRB Response:** The MSRB notes that the provisions in the Notice regarding Rule G-20 would only be reminders of existing MSRB guidance under Rule G-17, which is equally applicable to municipal advisors. Accordingly, the MSRB has determined not to make any changes to the Notice to address this comment.

- **Comment: Limit Duties of Affiliated Solicitors.** SIFMA said that the duties attendant on solicitors should not apply to solicitors affiliated with municipal advisors, and such solicitors should not be considered to be engaged in municipal advisory activities when soliciting on behalf of their municipal advisor affiliates.

- **MSRB Response:** The MSRB notes that affiliated solicitors are not included in the definition of "municipal advisor" under Section 15B(e)(4) of the Exchange Act and that Rule G-17 and the Notice would not apply to such solicitors. The Notice has been revised to refer to solicitations on behalf of "unrelated" third parties.

- **Comment: Clarify Referrals and Solicitations.** Catholic Finance requested clarification on whether referrals to it from prior clients constituted solicitation, and whether services performed as part of its exempt purpose and for its constituents at reduced or no compensation, or loans made to its constituents at subsidized rates, would constitute gifts under Rule G-17.

- **MSRB Response:** The MSRB has determined not to make any changes to the Notice based on this comment. The MSRB notes that the definition of "solicitation of a municipal entity or obligated person" found in Section 15B(e)(9)

of the Exchange Act does not apply to solicitations for which compensation is neither directly nor indirectly received. Under amendments to MSRB Rule G-20 proposed by the MSRB, the rule would only restrict gifts made to natural persons.

OTHER COMMENTS.

- **Comment: Manner of Regulation and Cost of Compliance.** B-Payne Group expressed the view that the MSRB should regulate municipal advisors by getting "experienced personnel on the ground in regional markets and charge them with staying on top of situations," rather than regulating municipal advisors as the MSRB regulates dealers. It argued for exemptions from MSRB rules for small municipal advisors and said the cost of compliance for such advisors would outweigh the regulatory benefit. Other parts of the comment letter addressed matters that were outside the scope of the request for comment on draft Rule G-17 (e.g., professional qualifications testing, training for local finance officials) and are not summarized here.

- **MSRB Response:** For regulation of municipal advisors to be fair, all municipal advisors must know what rules apply to them. Rule G-17 requires municipal advisors to conduct their municipal advisory activities in a fair manner, and the proposed rule change would provide guidance to municipal advisors on what that duty of fair dealing means so they can tailor their conduct accordingly. Without such guidance, "experienced personnel on the ground" would likely enforce the Exchange Act in an inconsistent manner, which the MSRB doubts that B-Payne Group would consider fair.

  The MSRB recognizes that there are costs of compliance with its rules. That is the reason the MSRB has included Appendix A to the Notice. By using Appendix A to provide disclosure concerning compensation conflicts, small municipal advisors will satisfy the compensation disclosure requirement of the Notice without having to retain legal counsel to assist them in the preparation of such disclosure.

- **Comment: Implementation Period.** SIFMA suggested that because Rule G-17 would subject municipal advisors to rules they are not currently subject to, the MSRB should consider providing for an implementation period of no less than one year.

- **MSRB Response.** The MSRB recognizes that some municipal advisors may be subject to rules that are not currently applicable. However, the appropriate implementation period will depend upon the provisions of the SEC's rule relating to municipal advisors.

6. Extension of Time Period of Commission Action

The MSRB declines to consent to an extension of the time period specified in Section 19(b)(2) of the Exchange Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2).

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibits

1. Federal Register Notice

2. Notice Requesting Comment and Comment Letters

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(RELEASE NO. 34- ; File No. SR-MSRB-2011-15)

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of Proposed Interpretive Notice Concerning the Application of Rule G-17 to Municipal Advisors

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("the Exchange Act")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on August 24, 2011, the Municipal Securities Rulemaking Board ("Board" or "MSRB") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the MSRB. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The MSRB is filing with the SEC a proposed rule change consisting of a proposed interpretive notice (the "Notice") concerning the application of MSRB Rule G-17 to municipal advisors. The MSRB requests that the proposed rule change be made effective on the date that rules defining the term "municipal advisor" under the Exchange Act are first made effective by the Commission or such later date as the proposed rule change is approved by the Commission.

The text of the proposed rule change is available on the MSRB's website at www.msrb.org/Rules-and-Interpretations/SEC-Filings/2011-Filings.aspx, at the MSRB's principal office, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

In its filing with the Commission, the MSRB included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")[3], the MSRB was expressly directed by Congress to protect municipal entities and obligated persons. Accordingly, the MSRB is proposing to provide interpretive guidance that addresses how Rule G-17 applies to municipal advisors when advising obligated person clients or when soliciting municipal entities on behalf of others.

A more-detailed description of the provisions of the Notice follows:

Duty to Obligated Persons; Fair Dealing. The Notice would provide that the Rule G-17 duty of fair dealing requires that the municipal advisor determine if a recommended municipal securities transaction or municipal financial product is suitable for its obligated person client, and that it provide disclosure of the material risks and characteristics of the transaction or product, as well as any incentives the municipal advisor has received for recommending the transaction or product and any other associated conflicts of interest. Further, under the Notice, the Rule G-17 duty of fair dealing would require that the municipal advisor exercise due care when providing advice to the obligated person client, and not undertake an engagement if the municipal advisor

[3] Pub. L. No. 111-203, 124 Stat. 1376 (2010).

does not have the necessary skills and resources to perform its duties in respect of the engagement.

The Notice also would provide that the municipal advisor must disclose all material conflicts of interest such as those that may color its judgment and impair its ability to render unbiased advice to its obligated person client, including those existing at the time the engagement is entered into, and those discovered or arising during the course of the engagement. The municipal advisor would be required to make these disclosures in writing and, in general, to obtain the informed consent thereto by an official of the obligated person having the authority to bind the obligated person by contract with the municipal advisor. Conflicts that constituted an unfair, deceptive, or dishonest practice would preclude a municipal advisor from undertaking an engagement with an obligated person client and disclosure of such conflict would not be effective in permitting such engagement to be undertaken.

The Notice would provide that a municipal advisor is required to provide written disclosure of the amount of its direct compensation and indirect compensation (e.g., amounts paid to affiliates) from the engagement, and the scope of services to be provided. The municipal advisor would also be required to provide written disclosure of the conflicts of interest associated with various forms of compensation, including the form of compensation applicable to its engagement, unless the obligated person client has required a particular form of compensation, in which case such disclosure would only need to address that particular form of compensation.

Deceptive, Dishonest or Unfair Practices. The Notice would provide that all representations made by municipal advisors to their obligated person clients, whether written or oral, must be truthful and accurate, and municipal advisors must not omit material facts, and that matters not within the personal knowledge of those preparing the response (e.g., pending

litigation) must be confirmed by those with knowledge of the subject matter. A municipal advisor would not be permitted to represent that it has the requisite knowledge or expertise with respect to a particular type of transaction or product if the personnel that it intends to work on the engagement do not have the requisite knowledge or expertise.

The Notice would provide that in certain cases and depending upon the specific facts and circumstances of the engagement, a municipal advisor's compensation, including payments from third parties, may be so disproportionate to the nature of the municipal advisory services to be an unfair practice in violation of Rule G-17.

The Notice would also provide that kickback arrangements, and certain fee-splitting arrangements, with underwriters or the providers of investments or services to obligated persons are unfair, dishonest, and deceptive practices that are prohibited by Rule G-17, as are payments by municipal advisors made for the purpose of obtaining or retaining municipal advisory business, other than reasonable fees paid to a municipal advisor regulated by the MSRB.

Solicitation of a Municipal Entity; Fair Dealing. The Notice would provide that, while municipal advisors are not required to exercise a fiduciary duty when soliciting municipal entities on behalf of third parties (in such capacity, a "solicitor"), they are required to deal fairly with the municipal entities they solicit and not engage in conduct that is deceptive, dishonest, or unfair.

The Notice would provide that a solicitor must provide written disclosure of all material facts about the solicitation to the municipal entity being solicited, including, among other things, the amount and source of all compensation received by the solicitor, any payments (including in-kind) made by the solicitor to facilitate the solicitation regardless of characterization; and any relationships of the solicitor with any employees, board members, or affiliated persons of the

municipal entity or its officials who may have influence over the selection of the solicitor's client.

The Notice would provide that the solicitor, if engaged by its client to present information to the municipal entity about a product or service being offered by the client, is required to disclose all material risks and characteristics of the product or service, as well as any incentives received by the solicitor (other than compensation from its client) to recommend the product or service, and any other conflicts of interest regarding the product or service.

Deceptive, Dishonest or Unfair Practices. The Notice would provide that kickbacks and fee-splitting arrangements with others, made or entered into by solicitors for the purpose of facilitating the solicitation are unfair, dishonest, and deceptive practices that violate Rule G-17. The Notice would also provide that lavish gifts and gratuities (that exceed limits set forth in MSRB Rule G-20) made to officials of the municipal entity or affiliated parties may improperly influence the decision of the municipal entity to engage the solicitor's client, and may therefore be a violation of Rule G-17.

2. Statutory Basis

The MSRB believes that the proposed interpretive notice is consistent with Section 15B(b)(2) of the Exchange Act, which provides that:

> The Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

Section 15B(b)(2)(C) of the Exchange Act, provides that the rules of the MSRB shall:

> be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

The proposed rule change is consistent with Section 15B(b)(2) of the Exchange Act because it will protect obligated persons and municipal entities from fraudulent and manipulative acts and practices and promote just and equitable principles of trade, as well as emphasizing the duty of fair dealing owed by municipal advisors to their obligated person clients and to municipal entities when soliciting such entities on behalf of third parties. Rule G-17 has two components, one an anti-fraud prohibition, and the other a fair dealing requirement (which promotes just and equitable principles of trade). The Notice would address both components of the rule. The sections of the Notice entitled "DUTY TO OBLIGATED PERSONS/DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES" and "SOLICITATION OF A MUNICIPAL ENTITY/DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES" primarily would provide guidance as to conduct required to comply with the anti-fraud component of the rule and, in some cases, conduct that would violate the anti-fraud component of the rule, depending on the facts and circumstances. The sections of the Notice entitled "DUTY TO OBLIGATED PERSONS/FAIR DEALING" and "SOLICITATION OF A MUNICIPAL ENTITY/FAIR DEAING" primarily would provide guidance as to conduct required to comply with the fair dealing component of the rule.

Section 15B(b)(2)(L)(iv) of the Exchange Act requires that rules adopted by the Board:

> not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

The proposed rule change is necessary for the protection of obligated persons and municipal entities and the robust protection of investors against fraud. Many municipal advisors play a key role in the structuring of offerings of municipal securities by obligated persons through municipal entities and the preparation of offering documents used to market those securities to investors. In some cases, they advise on the appropriateness of derivatives entered into by obligated persons, the effectiveness of which may have a substantial impact on the finances of their clients. In other cases, they solicit business from public pension funds, which, if not conducted according to the highest standards, may have a substantial effect on the finances of the state and local governments that control those funds. Municipal entities, obligated persons, and investors, therefore, have a substantial interest in municipal advisors conducting their municipal advisory activities fairly and not engaging in fraudulent conduct.

Accordingly, the MSRB does not believe that the proposed rule change would impose an unreasonable burden on small municipal advisors. However, the MSRB recognizes that there are costs of compliance. That is the reason the MSRB has included Appendix A to the Notice. By using Appendix A to provide disclosure concerning compensation conflicts, small municipal advisors will satisfy the compensation disclosure requirement of the Notice without having to retain legal counsel to assist them in the preparation of such disclosure.

B. Self-Regulatory Organization's Statement on Burden on Competition

The MSRB does not believe that the proposed rule change would impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act,

since it would apply equally to all municipal advisors advising obligated persons or soliciting third-party business from municipal entities.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

On February 14, 2011, the MSRB requested comment on a draft of the Notice (the "draft Notice"). The MSRB received comment letters from: the American Federation of State, County and Municipal Employees ("AFSCME"); B-Payne Group Financial Advisors ("B-Payne Group"); Catholic Finance Corporation ("Catholic Finance"); Municipal Regulatory Consulting LLC ("MRC"); the National Association of Independent Public Finance Advisors ("NAIPFA"); Not for Profit Capital Strategies ("Capital Strategies"); Public Financial Management ("PFM"); and the Securities Industry and Financial Markets Association ("SIFMA").

SCOPE OF NOTICE

- Comment: Delay Provisions Until SEC Rule on Municipal Advisors Finalized. SIFMA requested that the MSRB withdraw or delay some or all of the provisions of the draft Notice until the SEC has defined "municipal advisor," after which time they asked that the MSRB afford commenters an additional opportunity to comment on the Notice.
- MSRB Response: Because Rule G-17 became applicable to municipal advisors on December 23, 2010, the MSRB feels it is important to provide guidance on how the rule applies to municipal advisors. The MSRB has requested that the proposed rule change be made effective on the date that rules defining the term "municipal advisor" under the Exchange Act are first made effective by the SEC, or such later date that the SEC approves the proposed rule change. At that time, the MSRB may propose additional guidance, if necessary.

- Comment: Duty When Advising Obligated Persons. Capital Strategies requested that the MSRB clarify a municipal advisor's duty when a financing alternative for a municipal advisor's obligated person client is not in the best interests of a municipal entity.
- MSRB Response: The MSRB determined to address these comments by revising the Notice so that it would provide (in endnote 7): "Although a municipal advisor advising an obligated person does not have a fiduciary duty to the municipal entity that is the conduit issuer for the obligated person (but is not the client of the advisor), it still has a fair dealing duty to the municipal entity." Thus, when a municipal advisor is advising an obligated person, its primary obligation of fair dealing is to its client. The municipal advisor would not be required to act in the best interests of the municipal entity acting as a conduit issuer, although the advisor would be prohibited from acting in a deceptive, dishonest or unfair manner.
- Comment: Interpretation of Fair Dealing Too Broad. SIFMA said that the draft Notice interpreted a municipal advisor's fair dealing obligations far beyond the common understanding of "fair dealing" and beyond prior interpretations of fair dealing as applied to brokers, dealers, and municipal securities dealers ("dealers"). SIFMA said that the draft Notice imposed many "fiduciary-like" obligations on municipal advisors when advising entities other than municipal entities. SIFMA further commented that concepts of a duty of care and a duty to disclose conflicts and obtain consent have never before been interpreted to be part of a duty to deal fairly under Rule G-17, and that imposing these duties under Rule G-17 may be inconsistent with existing obligations of currently regulated persons.

- MSRB Response: The MSRB has determined not to make any changes to the Notice based on these comments. The MSRB notes that prior interpretations of the concept of "fair dealing" with respect to dealers applied to counterparty, not advisory, relationships, and that a comparison between such prior interpretations and duties applicable to an advisor would therefore be inappropriate. Further, the MSRB considered carefully the violations of fair dealing and fiduciary duty in numerous state and federal cases, as well as SEC proceedings, and determined that fair dealing obligations and fiduciary obligations in an advisory relationship were closely aligned and not as disparate as SIFMA might suggest.

DUTY TO OBLIGATED PERSONS

Appropriateness; Due Care.

- Comment: Revise "Appropriateness" Standard. SIFMA questioned whether the draft Notice created a new standard of conduct by requiring a municipal advisor to advise an obligated person client as to the appropriateness of a municipal financial product or transaction or whether "appropriateness" was intended by the MSRB to mean the same thing as "suitability." SIFMA and MRC said that the MSRB should define the duty to be consistent with other suitability standards currently applicable to dealers.
- MSRB Response: The MSRB determined to address this comment by revising the Notice so that it would substitute the term "suitability" for the term "appropriateness" and to provide that the municipal advisor must have reasonable grounds for believing that a recommended municipal securities transaction or municipal financial product is suitable for the client, based on certain information about the client and the product or transaction known by the municipal advisor.

- Comment: Address Competing Standards. SIFMA said that the MSRB should not impose an appropriateness standard on regulated entities that were already subject to a competing standard. SIFMA said that the Rule G-17 obligation to advise obligated person clients of material risks should be deemed satisfied if the municipal advisor complied with similar requirements under another applicable regulatory regime. Further, SIFMA said that this duty should be limited to specified transactions and not extended to ordinary course transactions such as bank deposits and the issuance of fixed or floating rate debt.
- MSRB Response: The MSRB disagrees in part with these comments and accordingly has determined not to make the changes to the Notice suggested by these comments, except as noted above. As noted above, the MSRB revised the Notice so that it would substitute the word "suitability" for the term "appropriateness" to align what SIFMA suggested might be potentially conflicting regulatory regimes. Further, the municipal advisor would not be deemed to have automatically satisfied the requirements of Rule G-17 by satisfying the requirements of another regulatory regime. The MSRB believes that adoption of SIFMA's comments with respect to ordinary course transactions would negate a significant purpose of the Notice.
- Comment: Risk Disclosure; Duplication and Scope. Catholic Finance suggested that where an underwriter had proposed a specific transaction and had adequately disclosed the risks, the municipal advisor need not also disclose the risks. Catholic Finance also requested clarification about whether the disclosure of risks and material incentives had to be in writing, as well as whether the same disclosures needed to be repeated to experienced clients in similar, successive transactions.

- MSRB Response: The MSRB has determined not to make the changes suggested by these comments. While a municipal advisor would not be required to disclose the same risks that an underwriter has disclosed, the municipal advisor would be required to determine the adequacy of such disclosure and advise its client as to whether the municipal advisor had reasonable grounds for believing the transaction or product recommended by the underwriter is suitable for such client. Such evaluation and advice are separate from whatever disclosure the underwriter presents. Further, while the disclosure of material risks would not be required to be in writing, the municipal advisor would be required to disclose any incentives and any other conflicts of interest in writing. Finally, with respect to disclosing the same risks to experienced clients in similar, successive transactions, the municipal advisor would be expected to consider whether disclosure would be advisable in light of new facts or circumstances concerning the client or the market, or the client's choice of new or different personnel directed to complete the transaction.
- Comment: Determine Status of Client. Capital Strategies requested that the MSRB clarify a municipal advisor's obligation if the status of its client could not be determined until after substantial advisory activity had taken place, citing an instance of a client initially considering a tax-exempt borrowing (and therefore being considered obligated person) but finally deciding to obtain a bank loan.
- MSRB Response: This comment is more appropriately addressed to the SEC, which has the authority to define the term "obligated person" as used in the Exchange Act.
- Comment: Limit Obligations to Terms of Contract. SIFMA and NAIPFA argued that a municipal advisor should be required to do only what the obligated person client contracted for, and SIFMA said that an advisor need not expressly disclaim an obligation

absent an explicit agreement between the parties. SIFMA also said that Rule G-17 should not imply additional obligations when reviewing a product or transaction recommended to its client by another, specifically the obligation to review for appropriateness and to disclose material risks, outside of what has been specifically contracted for between the parties.

- MSRB Response: The MSRB has determined not to make any changes to the Notice as a result of this comment. The MSRB expects that municipal advisors that wish to limit their engagements with obligated persons would do so in writings (whether as part of engagement letters or separately) that limit the scope of their engagements to particularly enumerated services or which state that any services not specified in the writing would not be provided by the advisor. This should impose no measurable additional cost on the advisor or the obligated person.
- Comment: Clarify Due Diligence Obligations. NAIPFA suggested that various duties, such as a duty to investigate or to make reasonable inquiry, appear to be variations on due diligence requirements and requested that they be worded in the same manner in the draft Notice and a proposed interpretive notice under proposed Rule G-36 (on fiduciary duty of municipal advisors). NAIPFA asked that these be revised and clarified. SIFMA suggested that any duty to analyze appropriateness be limited to facts that the municipal advisor was required to obtain under MSRB rules, or otherwise had in its possession, and that no further due diligence be required.
- MSRB Response: The MSRB has determined not to make any changes to the Notice based on these comments. The Notice would not impose a “due diligence” obligation upon municipal advisors. However, to the extent that a municipal advisor makes a

recommendation, the fulfillment of such advisor's suitability obligation as described above would necessitate that the advisor gather and review the information on which such suitability determination is based. The wording of the Notice differs from that of the Rule G-36 proposed notice because of the different duties owed by municipal advisors to their clients under the two notices.

Disclosure of Conflicts.

- Comment: Incorporate Requirements of Advisory Contracts in Rule G-23. MRC suggested that the requirements to disclose conflicts and to obtain informed consent would be more appropriately addressed in MSRB Rule G-23, and that the requirements should be removed from the draft Notice.
- MSRB Response: The MSRB disagrees with these comments and has determined not to make any changes to the Notice based on these comments. Rule G-23 only concerns financial advisory activities of dealers with respect to issues of municipal securities. The Notice would be the appropriate place to address these disclosures by all municipal advisors with obligated person clients.
- Comment: Disclose Linking Fees and Engagements. Catholic Finance suggested that disclosure concerning forms of compensation include disclosures by dealer firms offering to link engagements and fees as a municipal advisor with a separate engagement as underwriter on a separate transaction.
- MSRB Response. The MSRB has determined not to make any changes to the Notice based on these comments. The Notice would provide that other, associated conflicts of interest would be required to be disclosed and described, if applicable. This provision of the Notice would thus address many additional types of conflicts.

Forms of Compensation.

- Comment: Disclosure of Conflicts Confusing and Unnecessary. Several commenters suggested that the MSRB delete Appendix A to the draft Notice (Disclosure of Conflicts with Various Forms of Compensation) and the requirement of the Notice that municipal advisors disclose the conflicts with various forms of compensation (B-Payne Group, MRC; NAIPFA; PFM). Commenters argued that the disclosure would be confusing and that the type of fee arrangement (specifically contingent fees) did not affect professional performance. MRC suggested that any disclosure requirements were more appropriately addressed in Rule G-23. NAIPFA suggested that disclosure of conflicts in forms of compensation be limited to the conflicts applicable to the form of compensation methodology at the time the compensation methodology was proposed. NAIPFA also suggested that "pitches" or other discussions of ideas with municipal entities prior to engagement should not require delivery of the disclosure. AGFS supported the proposal to require municipal advisors to clarify the advantages and disadvantages of various forms of compensation.
- MSRB Response: The MSRB has determined to revise the Notice so that it would address these comments. Because municipal advisors owe a duty of fair dealing with respect to their obligated person clients, the MSRB considers it essential that they disclose all material conflicts to their clients. The Notice has been revised so that it would provide that, if the obligated person client has required that a particular form of compensation be used, the disclosure provided by the municipal advisor would need only address that form of compensation. The revised Notice would also require that conflicts disclosures, including those regarding compensation, need only be delivered before the

municipal advisor has been engaged to provide municipal advisory services, unless the conflicts are discovered or arise later.

The MSRB has determined not to eliminate Appendix A from the Notice. Appendix A was included in the Notice for the benefit of small municipal advisors to help them avoid the need to hire an attorney to prepare compensation conflicts disclosure associated with common forms of compensation. Use of Appendix A would not be mandatory and municipal advisors would be free to draft their own disclosure addressing these conflicts.

- Comment: Disclose Fees of All Participants. B-Payne Group said that fees of all participants (including bond attorneys) should be disclosed.
- MSRB Response: In the view of the MSRB, it is appropriate to interpret Rule G-17 differently for arm's-length counterparty relationships on the one hand (such as underwriters appropriately maintain with issuers) and advisory relationships on the other. The MSRB notes that it does not have jurisdiction over bond lawyers, unless they are functioning as municipal advisors, and, therefore, in most cases, may not require them to disclose compensation conflicts.
- Comment: Due Diligence to Determine Authority of Municipal Official. NAIPFA suggested that, in determining the authority of an official of an obligated person client to enter into a contract, to receive various disclosures, and to deliver informed consent, a municipal advisor should be permitted to rely on the apparent authority of such official to acknowledge the conflicts disclosure, assuming the advisor has no reason to believe that such person lacks the requisite authority.
- MSRB Response: The MSRB has determined to revise the Notice so that it would provide that a municipal advisor is required to deliver written disclosures of conflicts to,

and receive informed consent from, those officials of the obligated person whom the municipal advisor reasonably believes have the authority to bind the obligated person client by contract with the municipal advisor.

- Comment: Consent Presumed With Receipt of Written Agreement. NAIPFA suggested that a municipal advisor be permitted to presume consent if it receives an executed contract (or similar document), or verbal agreement that a written engagement letter (or similar document) has been accepted, or written or verbal acknowledgement that the advisor has been selected following a request for proposal ("RFP") process in which the form of compensation was appropriately disclosed and applicable disclosure provided.
- MSRB Response: The MSRB notes that the following provisions of the Notice would address this comment. The Notice would provide: "For purposes of Rule G-17, an obligated person client will be deemed to have consented to conflicts that are clearly described in its engagement letter or other written contract with the municipal advisor, if the obligated person client expressly acknowledges the existence of such conflicts. If the official of the obligated person client agrees to proceed with the municipal advisory engagement after receipt of the conflicts disclosure but will not provide written acknowledgement of such conflicts, the municipal advisor may proceed with the engagement after documenting with specificity why it was unable to obtain such written acknowledgement." Accordingly, the MSRB has determined not to make any changes to the Notice to address this comment.

Misrepresentations.

- Comment: Disclose Only General Conflicts of Interest. SIFMA said that it would be difficult for an advisor to accurately determine its capacity, resources, and knowledge

when discussing a potential engagement with an obligated person client or on a forward-looking basis, and suggested that it be able to satisfy its obligation by providing generalized disclosures about its qualifications.

- MSRB Response: The Notice would specify, in the context of a response to an RFP, that the response must accurately describe the municipal advisor's knowledge and capabilities, and prohibits a municipal advisor from making false or misleading statements about its knowledge and capabilities, or omitting material facts about its knowledge and capabilities. The municipal advisor would be expected to base its response on its understanding about the scope of the engagement at that time. If the scope of the engagement changes, the municipal advisor would be prohibited from making false or misleading statements about its continued ability to perform the engagement. Accordingly, the MSRB has determined not to make any changes to the notice based on this comment.

Excessive Compensation.

- Comment: Definition of Excessive Compensation. NAIPFA and B-Payne Group requested further clarification on the definition of "excessive compensation." NAIPFA suggested certain criteria, including, among other things: (i) the time and labor required, the novelty and difficulty of the issue involved, and the skill requisite to perform the municipal advisory services properly; (ii) the fee customarily charged in the locality for similar municipal advisory services; (iii) the amount involved and the results obtained; (iv) the nature and length of the professional relationship with the client; (v) the experience, reputation, and ability of the municipal advisor or municipal advisors performing the services; and (vi) whether the fee is fixed or contingent. B-Payne Group

objected to any evaluation of whether its fees were excessive, arguing that no regulator was in a position to evaluate the reasonableness of the municipal advisor's fee.

- MSRB Response: The MSRB has determined to revise the Notice so that it would address these comments. The Notice would describe excessive compensation as compensation that is so disproportionate to the nature of the municipal advisory services performed as to indicate that the municipal advisor is engaging in an unfair practice in violation of Rule G-17. The MSRB would revise the Notice so that it would provide that "The MSRB recognizes that what is considered reasonable compensation for a municipal advisor will vary according to the municipal advisor's expertise, the complexity of the financing, whether the fee is contingent upon the closing of the transaction, and the length of time spent on the engagement, among other factors." As this language recognizes, many factors can appropriately affect the amount of the fee, and the specific factors listed in the Notice would not be exclusive. Thus, it may be that the various other factors noted by commenters could have an impact on the compensation paid to a municipal advisor. In all cases, the municipal advisor should be able to support the legitimacy of its fees.

SOLICITATION OF A MUNCIPAL ENTITY

Disclosure of Material Facts; Gifts.

- Comment: Extent of Disclosure May Be of Questionable Value. SIFMA suggested that the requirement to disclose all relationships with influential employees, board members, or affiliates of the municipal entity may be extensive and of questionable value. Further, SIFMA noted that a solicitor may not be in the best position to disclose all material risks

and characteristics, and that such effort will be duplicative of the provider's (its client's) obligation once it has been retained an a municipal advisor.

- MSRB Response: The MSRB disagrees with this comment, especially given the relationship-driven business that enforcement actions have revealed. See, e.g., endnote 15 to the Notice. Accordingly, the MSRB has determined not to make any changes to the Notice to address these comments.
- Comment: Address Gifts in Rule G-20. SIFMA suggested that the MSRB should address the issue of gifts in MSRB Rule G-20, as it has done for similar prohibitions on dealers.
- MSRB Response: The MSRB notes that the provisions in the Notice regarding Rule G-20 would only be reminders of existing MSRB guidance under Rule G-17, which is equally applicable to municipal advisors. Accordingly, the MSRB has determined not to make any changes to the Notice to address this comment.
- Comment: Limit Duties of Affiliated Solicitors. SIFMA said that the duties attendant on solicitors should not apply to solicitors affiliated with municipal advisors, and such solicitors should not be considered to be engaged in municipal advisory activities when soliciting on behalf of their municipal advisor affiliates.
- MSRB Response: The MSRB notes that affiliated solicitors are not included in the definition of "municipal advisor" under Section 15B(e)(4) of the Exchange Act and that Rule G-17 and the Notice would not apply to such solicitors. The Notice has been revised to refer to solicitations on behalf of "unrelated" third parties.
- Comment: Clarify Referrals and Solicitations. Catholic Finance requested clarification on whether referrals to it from prior clients constituted solicitation, and whether services performed as part of its exempt purpose and for its constituents at reduced or no

compensation, or loans made to its constituents at subsidized rates, would constitute gifts under Rule G-17.

- MSRB Response**:** The MSRB has determined not to make any changes to the Notice based on this comment**.** The MSRB note**s** that the definition of "solicitation of a municipal entity or obligated person" found in Section 15B(e)(9) of the Exchange Act does not apply to solicitations for which compensation is neither directly nor indirectly received. Under amendments to MSRB Rule G-20 proposed by the MSRB, the rule would only restrict gifts made to natural persons.

OTHER COMMENTS.

- Comment: Manner of Regulation and Cost of Compliance. B-Payne Group expressed the view that the MSRB should regulate municipal advisors by getting "experienced personnel on the ground in regional markets and charge them with staying on top of situations," rather than regulating municipal advisors as the MSRB regulates dealers. It argued for exemptions from MSRB rules for small municipal advisors and said the cost of compliance for such advisors would outweigh the regulatory benefit. Other parts of the comment letter addressed matters that were outside the scope of the request for comment on draft Rule G-17 (e.g., professional qualifications testing, training for local finance officials) and are not summarized here.
- MSRB Response: For regulation of municipal advisors to be fair, all municipal advisors must know what rules apply to them. Rule G-17 requires municipal advisors to conduct their municipal advisory activities in a fair manner, and the proposed rule change would provide guidance to municipal advisors on what that duty of fair dealing means so they can tailor their conduct accordingly. Without such guidance, "experienced personnel on

the ground" would likely enforce the Exchange Act in an inconsistent manner, which the MSRB doubts that B-Payne Group would consider fair.

The MSRB recognizes that there are costs of compliance with its rules. That is the reason the MSRB has included Appendix A to the Notice. By using Appendix A to provide disclosure concerning compensation conflicts, small municipal advisors will satisfy the compensation disclosure requirement of the Notice without having to retain legal counsel to assist them in the preparation of such disclosure.

- Comment: Implementation Period. SIFMA suggested that because Rule G-17 would subject municipal advisors to rules they are not currently subject to, the MSRB should consider providing for an implementation period of no less than one year.
- MSRB Response. The MSRB recognizes that some municipal advisors may be subject to rules that are not currently applicable. However, the appropriate implementation period will depend upon the provisions of the SEC's rule relating to municipal advisors.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning

the foregoing, including whether the proposed rule change is consistent with the Exchange Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-MSRB-2011-15 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-MSRB-2011-15. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. Copies of such filing also will be available for inspection and copying at the MSRB's offices. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-MSRB-2011-15 and

should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[4]

Elizabeth M. Murphy
Secretary

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4 17 CFR 200.30-3(a)(12).

MSRB
Municipal Securities
Rulemaking Board

MSRB NOTICE 2011-13 (FEBRUARY 14, 2011)

REQUEST FOR COMMENT ON DRAFT INTERPRETIVE NOTICE CONCERNING THE APPLICATION OF MSRB RULE G-17 TO MUNICIPAL ADVISORS

The Municipal Securities Rulemaking Board ("MSRB") is requesting comment on a draft interpretive notice concerning the application of MSRB Rule G-17 to municipal advisors providing advice to obligated persons or soliciting business from municipal entities on behalf of others.

Comments should be submitted no later than April 11, 2011. Comments should be sent via e-mail to CommentLetters@msrb.org. Please indicate the notice number in the subject line of the e-mail. To submit comments via regular mail, please send them to Ronald W. Smith, Corporate Secretary, MSRB, 1900 Duke Street, Alexandria, VA 22314. Written comments will be available for public inspection on the MSRB's web site.[1] The MSRB will hold an informational webinar on the draft interpretive notice on Rule G-17 described in this request for comment on March 1 at 3:00 p.m. The webinar will also address MSRB Notice 2011-14 (February 14, 2011) on draft Rule G-36 (on fiduciary duty of municipal advisors) and associated draft interpretive guidance. **Register** for the webinar.

Questions about this notice should be directed to Peg Henry, Deputy General Counsel, or Karen Du Brul, Associate General Counsel, at 703-797-6600.

BACKGROUND

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. Law No. 111-203) ("Dodd-Frank Act") amended Section 15B of the Securities Exchange Act of 1934 ("Exchange Act") to provide for the regulation of municipal advisors[2] and to direct the MSRB to protect municipal entities and obligated persons.[3]

The MSRB amended Rule G-17, effective December 22, 2010, to make the rule applicable to municipal advisors.[4]Amended Rule G-17 provides:

> In the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.

REQUEST FOR COMMENT

The MSRB requests comment on the draft interpretive notice set forth below concerning the application of Rule G-17 to municipal advisors that advise obligated persons clients and municipal advisors soliciting business from municipal entities on behalf of others.[5]

A municipal advisor is required by Rule G-17 to deal fairly with its obligated person clients. This includes a duty to evaluate the appropriateness of a proposed municipal securities transaction or municipal

financial product or transaction for its client, unless the client has agreed to a more limited engagement. The municipal advisor must also disclose all material conflicts of interest, such as those that may impair its ability to render unbiased advice and obtain its client's informed consent to such conflicts of interest. The municipal advisor also must not undertake an engagement unless it has necessary capacity, resources, and knowledge to render informed advice.

Rule G-17 also prohibits a municipal advisor from engaging in deceptive, dishonest, or unfair practices when advising an obligated person. Thus, a municipal advisor may not misrepresent its qualifications and must not accept excessive compensation, including kickbacks and certain other third-party payments.

Rule G-17 also applies to municipal advisors when soliciting business from municipal entities (such as public pension funds) on behalf of third parties. The municipal advisor as solicitor owes a duty of fair dealing to the municipal entity, including a duty to disclose material facts about the solicitation (such as amount and sources of compensation, and relationships with employees or board members of the municipal entity). In addition, if the municipal advisor has been engaged by its client to present information about a product or service offered by the third party, the municipal advisor as solicitor must disclose all material risks and characteristics of the product or service. The municipal advisor as solicitor is also prohibited from engaging in deceptive, dishonest, and unfair practices, such as accepting kickbacks and other undisclosed payments, and giving lavish gifts and gratuities to officials of the municipal entity.

Commenters should note that the interpretive notice is based upon the statutory definition of municipal advisor set forth in the Dodd-Frank Act without regard to any interpretation of that term proposed by the Securities and Exchange Commission ("SEC") in its proposed permanent registration rule for municipal advisors (Securities Exchange Act Release No. 34-63576 (December 20, 2010). If the SEC's permanent registration rule is adopted in its current form, the MSRB may request comment on revisions to the draft interpretive notice.

TEXT OF DRAFT INTERPRETIVE NOTICE

INTERPRETIVE GUIDANCE CONCERNING THE APPLICATION OF MSRB RULE G-17 TO MUNICIPAL ADVISORS ADVISING OBLIGATED PERSONS OR SOLICITING MUNICIPAL ENTITIES ON BEHALF OF OTHERS

The Dodd-Frank Act[1] amended Section 15B of the Securities Exchange Act of 1934 (the "Exchange Act") to provide for the regulation of municipal advisors[2] by the Municipal Securities Rulemaking Board ("MSRB") and to direct the MSRB expressly[3] to protect municipal entities and obligated persons. Among other things, the MSRB was directed to adopt rules that are designed to "prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest . . . . "[4]

Accordingly, the MSRB amended its Rule G-17 to provide: "In the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice."[5] This notice provides guidance on a municipal advisor's duties under Rule G-17 when providing advice to an obligated person[6] and a municipal advisor's

duties to a municipal entity when undertaking a solicitation of a municipal entity on behalf of another person.[7] The examples discussed in this notice are illustrative only, and are not meant to encompass all obligations of municipal advisors under Rule G-17.

Rule G-17 precludes a municipal advisor from engaging in any deceptive, dishonest, or unfair practice with any person, including a municipal entity or an obligated person. The rule contains an anti-fraud prohibition similar to the standard set forth in Rule 10b-5 adopted by the Securities and Exchange Commission ("SEC") under the Exchange Act. Thus, a municipal advisor must not misrepresent the facts, risks, or other material information about municipal advisory activities undertaken with a municipal entity or obligated person. However, Rule G-17 does not merely prohibit deceptive conduct on the part of the municipal advisor. It also establishes a general duty of a municipal advisor to deal fairly with all persons (including but not limited to municipal entities and obligated persons), even in the absence of fraud. Even so, unlike a municipal advisor's duty to its municipal entity client,[8] the Dodd-Frank Act does not require a municipal advisor to exercise a fiduciary duty when advising an obligated person, unless that obligated person is itself a municipal entity.[9]

DUTY TO OBLIGATED PERSONS

FAIR DEALING

Appropriateness. A municipal advisor's duties to its obligated person client under Rule G-17 will vary depending upon whether the municipal advisor has recommended a municipal securities transaction or municipal financial product to its client, or whether it has been asked to review such a transaction or product recommended by another person. If a municipal advisor has recommended such a transaction or product to its client, the advisor must have concluded, in its professional judgment, that the transaction or product is appropriate for the client, given its financial circumstances, objectives, and market conditions, and must advise the client of material risks and characteristics of the structure or product. The municipal advisor must also advise the client of any incentives for the municipal advisor to recommend the transaction or product and any other associated conflicts of interest.[10]

For example, a municipal advisor that recommends that an obligated person enter into a variable rate demand obligation financing should inform the obligated person of the risk of interest rate fluctuations and the material terms of any associated credit or liquidity facilities (*e.g.*, the risk that the obligated person might not be able to replace the facility upon its expiration and might be required to repay the facility provider over a short period of time). Similarly, a municipal advisor that recommends that an obligated person enter into a municipal derivative contract must disclose the material risks (including market, credit, operational, and liquidity risks) and characteristics of the derivative.

If a municipal advisor has been engaged by its obligated person client to review a municipal securities transaction or municipal financial product recommended by another party (*e.g.*, an underwriter), Rule G-17 requires the municipal advisor to evaluate and advise the client of the material risks and characteristics of the transaction or product and its appropriateness for the client, based on the client's financial circumstances, objectives, and market conditions. The municipal advisor is not required to have considered then reasonably feasible alternatives unless otherwise requested to do so by the client. Furthermore, the municipal advisor need not advise its client as to the appropriateness of the transaction or product if it has expressly disclaimed that obligation in its engagement letter or other writing with the client.

Due Care. In all cases, the municipal advisor's Rule G-17 duty to deal fairly requires it to exercise due care in the provision of advice to its obligated person client, which requires that the municipal advisor possess the necessary capacity, resources, and knowledge to render informed advice. A municipal advisor should not undertake a swap advisory engagement unless it has sufficient knowledge to evaluate the transaction and its risks, as well as the pricing and the appropriateness of the transaction.[11] The municipal advisor must also have a reasonable basis for any representations it makes in any certificate it signs that will be relied upon by other parties to the transaction. A municipal advisor's obligation to act with due care does not make the municipal advisor a guarantor of a successful financing or a guarantor that there are no facts material to its client's decision-making process other than the ones known by the municipal advisor and disclosed to the client.

Disclosure of Conflicts. The municipal advisor's Rule G-17 duty to deal fairly with an obligated person client requires the municipal advisor to disclose material conflicts of interest, such as those that may color its judgment and impair its ability to render unbiased advice to its client. All disclosures of conflicts must be made in writing to officials of the obligated person with the authority to bind the obligated person by contract with the municipal advisor. Such disclosures must be made in a manner sufficiently detailed to inform the obligated person of the nature and implications of the conflict. The following are examples of the types of conflicts that must be disclosed by the municipal advisor, but this list is not intended to be exhaustive:

(i) payments by municipal advisors made for the purpose of obtaining or retaining municipal advisory business;

(ii) payments from third parties to the municipal advisor in relation to the municipal advisory engagement;

(iii) payments from third parties to enlist the municipal advisor's recommendation of their services to the obligated person;

(iv) whether the municipal advisor or an affiliate of the municipal advisor is acting as a principal in matters concerning the municipal advisory engagement; and

(v) other engagements or relationships that might impair the municipal advisor's ability to provide unbiased advice to its obligated person client.

Failure to disclose conflicts of interest has resulted in various SEC enforcement actions and administrative proceedings for, among other things, violations of Rule G-17 by dealer financial advisors.[12]

Informed Consent. In addition to its duty to disclose various conflicts, Rule G-17 also requires the municipal advisor to obtain informed consent from its obligated person client to each of the conflicts disclosed. The municipal advisor must receive written consent to its conflicts by officials of the obligated person with the authority to bind the obligated person by contract with the municipal advisor before the municipal advisor may provide municipal advisory services to the obligated person or, in the case of conflicts arising after the municipal advisory relationship has commenced, before the municipal advisor may continue to provide such services. For purposes of Rule G-17, an obligated person will be deemed to have consented to conflicts that are clearly described in its engagement letter or other written contract with the municipal advisor, if the obligated person expressly acknowledges the existence of such conflicts. If the officials of the obligated person agree to proceed with the municipal advisory engagement after receipt of the

conflicts disclosure but will not provide written acknowledgement of such conflicts, the municipal advisor may proceed with the engagement after documenting with specificity why it was unable to obtain their written acknowledgement.

Disclosure of conflicts, coupled with written consent, will not satisfy the requirements of Rule G-17 in instances in which the municipal advisor has reason to believe that such consent is not informed. In such cases, a municipal advisor should make additional efforts reasonably designed to inform the officials of the obligated person of the nature and implications of the municipal advisor's conflicts. Additionally, disclosures to officials of the obligated person who are themselves parties to the conflict of interest (such as recipients of payments from municipal advisors) will not suffice to satisfy the requirements of Rule G-17.

Forms of Compensation. The manner in which municipal advisors are compensated varies according to the nature of the engagement and the requirements of the obligated person client, among other factors. Pursuant to Rule G-17, a municipal advisor must provide written disclosure to its obligated person client of what the amount (in dollars and to the extent it can be quantified) of its direct compensation and indirect compensation (*e.g.*, amounts paid to affiliates) from the engagement will be, or is projected to be, as well as the scope of services to be provided for that compensation. Additionally, the municipal advisor must provide written disclosure to its client of the conflicts of interest with various forms of compensation, including the form of compensation applicable to its engagement, even if the client has required that a particular form of compensation be used. One way in which a municipal advisor may satisfy its obligation to provide written disclosure of the conflicts with various forms of compensation is to provide its client with the document entitled "Disclosure of Conflicts of Interest With Various Forms of Compensation," attached as Appendix A to this notice (the "Compensation Disclosure Document"). The disclosures described in this paragraph must be provided as described above under "Duty to Obligated Persons/Fair Dealing/Disclosure of Conflicts." Provision by the municipal advisor to its client of the Compensation Disclosure Document will not satisfy the municipal advisor's obligation to disclose conflicts of interest not addressed in the Compensation Disclosure Document, such as payments from third parties.

DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES

Misrepresentations. Rule G-17 requires that all representations made by municipal advisors to their obligated person clients, whether written or oral, must be truthful and accurate, and municipal advisors must not omit material facts. For example, a municipal advisor's response to an obligated person's request for proposals or qualifications must fairly and accurately describe the municipal advisor's capacity, resources, and knowledge to perform the proposed municipal advisory engagement as of the time the proposal is submitted and must not contain any representations or other material information about such capacity, resources, or knowledge that the municipal advisor knows or should know to be inaccurate or misleading. Matters not within the personal knowledge of those preparing the response (*e.g.*, pending litigation) must be confirmed by those with knowledge of the subject matter. A municipal advisor may not represent that it has the requisite knowledge or expertise with respect to a particular type of transaction or product if the personnel that it intends to work on the engagement do not have the requisite knowledge or expertise.

Excessive Compensation. While the MSRB recognizes that what is considered reasonable compensation for a municipal advisor will vary according to the municipal advisor's expertise and the nature of the financing, in certain cases and depending upon the specific facts and

circumstances of the engagement, a municipal advisor's compensation may be so disproportionate to the nature of the municipal advisory services performed as to indicate that the municipal advisor is engaging in an unfair practice in violation of Rule G-17.[13] Payments from third parties are included in determining whether compensation is excessive. Furthermore, the MSRB notes that municipal advisors subject to hourly billing arrangements must not submit bills that do not accurately reflect the nature of the services performed and the personnel performing them.

Kickbacks and other payments. Kickback arrangements, or certain fee-splitting arrangements, with underwriters or the providers of investments or services to obligated persons also represent unfair, dishonest, and deceptive practices that are prohibited by Rule G-17,[14] as do payments by municipal advisors made for the purpose of obtaining or retaining municipal advisory business other than reasonable fees paid to a municipal advisor described in Section 15B(e)(9) of the Exchange Act.[15]

SOLICITATION OF A MUNICIPAL ENTITY

While the Dodd-Frank Act imposes a fiduciary obligation on municipal advisors acting on behalf of their municipal entity clients, municipal advisors are not required to exercise a fiduciary duty when soliciting municipal entities on behalf of third parties (in such capacity, a "solicitor"). Solicitors are, however, subject to Rule G-17, and are required to deal fairly with the municipal entities they solicit and not engage in conduct that is deceptive, dishonest, or unfair.

FAIR DEALING

Disclosure of Material Facts about Solicitation. Under its Rule G-17 duty to deal fairly, a solicitor must disclose all material facts about the solicitation to the municipal entity, including:

(i) the name of the solicitor's client;

(ii) the type of business being solicited;

(iii) the amount of the solicitor's compensation;

(iv) the source of all compensation received by the solicitor;

(v) payments (including in-kind) made by the solicitor to facilitate the solicitation regardless of characterization; and

(vi) any relationships of the solicitor with any employees or board members of the municipal entity or any other persons affiliated with the municipal entity or its officials who may have influence over the selection of the solicitor's client.

Material Information about Products or Services. In addition to the disclosure obligations described above, if the solicitor has been engaged by its client to present information to the municipal entity about a product or service being offered by the client, the solicitor is required to disclose all material risks and characteristics of the product or service. The solicitor must also advise the municipal entity of any incentives received by the solicitor (other than compensation from its client) to recommend the product or service, as well as any other conflicts of interest regarding the product or service, and must not make material misstatements or omissions when discussing the product or service.

DECEPTIVE, DISHONEST, OR UNFAIR PRACTICES

Kickbacks and Other Payments. Kickbacks, or fee-splitting arrangements with others, made or entered into by solicitors for the purpose of facilitating the solicitation represent unfair, dishonest, and deceptive practices that violate Rule G-17. Persons and firms arranging, making and receiving such payments have been the subject of various enforcement actions by both the SEC and various state authorities.[16]

Lavish Gifts and Gratuities. Lavish gifts and gratuities made to officials of the municipal entity or affiliated parties may improperly influence the decision of the municipal entity to engage the solicitor's client. Generally, a gift will be considered lavish if its value exceeds the limits imposed by MSRB Rule G-20 (on gifts and gratuities). Government officials controlling the award of public pension fund business have been found to violate federal and state securities laws by the acceptance of such gifts,[17] as have those making the gifts.[18]

APPENDIX A

DISCLOSURE OF CONFLICTS OF INTEREST WITH VARIOUS FORMS OF COMPENSATION

The Municipal Securities Rulemaking Board (MSRB) requires us, as your municipal advisor, to provide written disclosure to you about the actual or potential conflicts of interest presented by various forms of compensation. We must provide this disclosure even if you have already chosen a particular form of compensation. The municipal advisor's client should select a form of compensation that best meets its needs and the agreed upon scope of services.

Forms of Compensation; Potential Conflicts. The forms of compensation for municipal advisors vary according to the nature of the engagement and requirements of the client, among other factors. Various forms of compensation present actual or potential conflicts of interest because they may create an incentive for an advisor to recommend one course of action over another if it is more beneficial to the advisor to do so. This document discusses various forms of compensation and the timing of payments to the advisor.

Fixed fee. Under a fixed fee form of compensation, the municipal advisor is paid a fixed amount established at the outset of the transaction. The amount is usually based upon an analysis by the client and the advisor of, among other things, the expected duration and complexity of the transaction and the agreed-upon scope of work that the advisor will perform. This form of compensation presents a potential conflict of interest because, if the transaction requires more work than originally contemplated, the advisor may suffer a loss. Thus, the advisor may recommend less time-consuming alternatives, or fail to do a thorough analysis of alternatives. There may be additional conflicts of interest if the municipal advisor's fee is contingent upon the successful completion of a financing, as described below.

Hourly fee. Under an hourly fee form of compensation, the municipal advisor is paid an amount equal to the number of hours worked by the advisor times an agreed-upon hourly billing rate. This form of compensation presents a potential conflict of interest if the client and the advisor do not agree on a reasonable maximum amount at the outset of the engagement, because the advisor does not have a financial incentive to recommend alternatives that would result in fewer hours worked. In some cases, an hourly fee may be applied against a retainer (*e.g.*, a retainer payable monthly), in which case it is payable whether or not a financing closes. Alternatively, it

may be contingent upon the successful completion of a financing, in which case there may be additional conflicts of interest, as described below.

Fee contingent upon the completion of a financing or other transaction. Under a contingent fee form of compensation, payment of an advisor's fee is dependent upon the successful completion of a financing or other transaction. Although this form of compensation may be customary for the client, it presents a conflict because the advisor may have an incentive to recommend unnecessary financings or financings that are disadvantageous to the client. For example, when facts or circumstances arise that could cause the financing or other transaction to be delayed or fail to close, an advisor may have an incentive to discourage a full consideration of such facts and circumstances, or to discourage consideration of alternatives that may result in the cancellation of the financing or other transaction.

Fee paid under a retainer agreement . Under a retainer agreement, fees are paid to a municipal advisor periodically (*e.g.*, monthly) and are not contingent upon the completion of a financing or other transaction. Fees paid under a retainer agreement may be calculated on a fixed fee basis (*e.g.*, a fixed fee per month regardless of the number of hours worked) or an hourly basis (*e.g.*, a minimum monthly payment, with additional amounts payable if a certain number of hours worked is exceeded). A retainer agreement does not present the conflicts associated with a contingent fee arrangement (described above).

Fee based upon principal or notional amount and term of transaction. Under this form of compensation, the municipal advisor's fee is based upon a percentage of the principal amount of an issue of securities (*e.g.*, bonds) or, in the case of a derivative, the present value of or notional amount and term of the derivative. This form of compensation presents a conflict of interest because the advisor may have an incentive to advise the client to increase the size of the securities issue or modify the derivative for the purpose of increasing the advisor's compensation.

[If applicable, describe other form of compensation for the engagement and associated conflicts with a comparable level of specificity].

Acknowledgement

The undersigned hereby acknowledges that he/she has received this disclosure and that he/she has been given the opportunity to raise questions and discuss the foregoing matters with the advisor.

_____ [name of client]

By: _____

Name: _____

Title:_____

Date:_____

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[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. Law. No. 111-203, 124 Stat. 1376 (2010).

[2] Section 15B(e)(4)(A) of the Exchange Act defines the term "municipal advisor" to mean: "a person (who is not a municipal entity or an employee of a municipal entity) that (i) provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues; or (ii) undertakes a solicitation of a municipal entity."

[3] The MSRB has previously observed that Rule G-17 requires dealers to deal fairly with issuers in connection with the underwriting of their municipal securities. *See* Reminder Notice on Fair Practice Duties to Issuers of Municipal Securities, MSRB Notice 2009-54 (September 29, 2009); Rule G-17 Interpretive Letter – Purchase of new issue from issuer, MSRB interpretation of December 1, 1997, reprinted in MSRB Rule Book. *See also* Interpretive Guidance Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities, MSRB Notice 2011-12 (February 14, 2011).

[4] Section 15B(b)(2)(C) of the Exchange Act.

[5] Exchange Act Release No. 63599; File No. SR-MSRB-2010-16 (December 22, 2010).

[6] The term "obligated person" is defined in Section 15B(e)(10) of the Exchange Act to mean "any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities."

[7] Section 15B(e)(9) of the Exchange Act provides that,

> the term "solicitation of a municipal entity or obligated person" means a direct or indirect communication with a municipal entity or obligated person made by a person, for direct or indirect compensation, on behalf of a broker, dealer, municipal securities dealer, municipal advisor, or investment adviser (as defined in section 202 of the Investment Advisers Act of 1940) that does not control, is not controlled by, or is not under common control with the person undertaking such solicitation for the purpose of obtaining or retaining an engagement by a municipal entity or obligated person of a broker, dealer, municipal securities dealer, or municipal advisor for or in connection with municipal financial products, the issuance of municipal securities, or of an investment adviser to provide investment advisory services to or on behalf of a municipal entity.

[8] Although a municipal advisor advising an obligated person does not have a fiduciary duty to the municipal entity that is the conduit issuer for the obligated person, it still has a fair dealing duty to the municipal entity. Thus, in advising an obligated person about the structure of a financing, the advisor should not recommend a structure that is unfair to the municipal entity issuer.

[9] *See* Section 15B(c)(1) of the Exchange Act; *see also* MSRB Rule G-36 (on fiduciary duty of a municipal advisor), which governs a municipal advisor's duty to its municipal entity clients and Fiduciary Duty of a Municipal Advisor, MSRB Notice 2011-14 (February 14, 2011) (the "Fiduciary Duty Notice"). State laws may, however, impose a fiduciary duty on a municipal advisor when providing advice to an obligated person client. For purposes of this notice, the client of the municipal advisor will be presumed not to be a municipal entity.

[10] For example, a conflict of interest may exist when the municipal advisor receives compensation from a swap provider for recommending the swap provider to the obligated person.

[11] Section 4s(h)(5) of the Dodd-Frank Act requires that a swap dealer with a special entity client (including states, local governments, and public pension funds) must have a reasonable basis to believe that the special entity has an independent representative that satisfies these criteria, among others.

[12] *See, e.g., In the Matter of Lazard Freres and Merrill Lynch*, SEC Rel. No. 34-36419 (Oct. 26, 1995) (settlement in connection with alleged violation of Rule G-17 due to failure of underwriter and financial advisor to disclose payments made by underwriter to financial advisor); *In re Wheat, First Securities, Inc.*, SEC Initial Dec. Rel. No. 155 (Dec. 17, 1999) (administrative law judge found violation of Rule G-17 by financial advisor for making false disclosure to municipal entity that it had not employed a lobbyist to secure its advisory contract with the county and that it had not entered into an arrangement with a third party to make payments contingent upon its securing the advisory contract); *In re Pryor, McClendon, Counts & Co., Inc. et al.*, Exchange Act Release No. 48095 (Jun. 26, 2003) (settlement in connection with alleged violation of Rule G-17 for financial advisor's failure to disclose payment to government official made to secure advisory assignment).

[13] *See, e.g.*, the following cases for examples of excessive compensation arrangements: *In re O'Brien Partners, Inc.,* Exchange Act Release No. 7594 (Oct. 27, 1998) (settlement in connection with investment adviser allegedly received "referral fees" from a finder that assisted in the reinvestment of municipal bond proceeds in guaranteed investment contracts, repurchase agreements and forwards; referral fees allegedly totaled $450,000 and represented 50-60% of finder commission); *In the Matter of Mark S. Ferber*, Exchange Act Release No. 38102 (Dec. 31, 1996) (settlement in connection with financial advisor allegedly received payments from broker-dealer totaling almost $6 million over two years in exchange for recommendations that his clients select that broker-dealer as underwriter or provider of other financial services, including interest rate swaps); *In the Matter of Arthurs Lestrange & Co., Inc. and Michael Bova*, SEC Release Nos. 33-7775, 34-42148 (Nov. 17, 1999) (settlement in connection with financial advisor allegedly engaged in fee splitting arrangement under which financial advisor contributed its financial advisory fee of $210,000 to pool of advisory and brokerage service compensation, received $1.5 million from the investment broker, and paid $500,000 to a finder); *In the Matter of William R. Hough & Co.*, SEC Release Nos. 33-7826, 34-42632 (Apr. 6, 2000) (settlement in connection with financial advisor allegedly received $35,000 for its financial advisory services and $400,000 from the investment provider; financial advisor allegedly received $300,000 from a forward supply contract provider for "developing a forward supply assignment program"); *In the Matter of John S. Reger and Business & Financial Advisors, Inc.,* SEC Rel. No. 33-7973 (Apr. 23, 2001) (settlement in connection with financial advisor allegedly received $129,000 kickback from escrow securities provider, representing 40% of escrow provider's profit).

[14] *Id.* Rule G-17 does not preclude a municipal advisor from receiving payment for its municipal advisory services from a third party, as long as the municipal advisor discloses, and the obligated person client provides its informed written consent to, such payment arrangement and the amount of such payment. As with the disclosure of other conflicts of interest, such disclosure should be made before the municipal advisory engagement is entered into, or at the time the conflict arises, if later.

[15] *See* the cases at note 13, *supra.* Municipal advisors that are described in Section 15B(e)(9) of the Exchange Act because they solicit business from municipal entities on behalf of other municipal advisors are subject to all MSRB rules for municipal advisors.

[16] *See, e.g.*, *SEC v. Steven L. Rattner*, SEC Lit. Rel. No. 21748 (November 18, 2010) (SEC alleged that defendant violated Section 17(a)(2) of the Securities Act of 1933 by securing investments in his firm private equity firm from a state retirement fund after he arranged for a firm affiliate to distribute a movie produced by the retirement fund's chief investment officer and his brothers; defendant then allegedly caused his firm to retain an advisor and fundraiser for a former state comptroller as a "placement agent" and pay him more than $1 million in sham fees even though the defendant was already dealing directly with the state deputy comptroller and did not need an introduction to the retirement fund); *SEC v. Henry Morris, et al*., SEC Lit. Rel. Nos. 20963, 21001, 21018 and 21036 (filed March 19,2009, April 15, 2009, April 30, 2009 and May 12, 2009, respectively) (SEC alleged that defendants and others required investment managers seeking to do business with the state retirement fund to make payments to unrelated finders and placement agents who then made payments or other benefits as directed by state officials); *see also* Allocution to Violation of New York State's Martin Act by Henry Morris, http://www.ag.ny.gov/media_center/2010/nov/Exhibit_A_ocr.pdf.

[17] Allocution to Violation of New York State's Martin Act by Alan G. Hevesi, http://www.ag.ny.gov/media_center/2010/oct/pdfs/Hevesi_Allocution.pdf (state comptroller who controlled investment decisions of state retirement fund accepted paid vacation for himself and his family paid for by official of private equity fund soliciting business from the retirement fund).

[18] Announcement of Plea Agreement of Elliott Broidy with New York State Attorney General, http://www.ag.ny.gov/media_center/2009/dec/dec3b_09.html (plea to violation of New York State Martin Act by defendant for his involvement in a pay to play kickback scheme at the state comptroller office in connection with the state retirement fund's investment in a fund operated by defendant's firm; defendant paid at least $75,000 for first class airfare, luxury hotel suites, a car and driver, a helicopter tour, and security detail on vacation trips for high ranking official of the state retirement fund and concealed those payments through charities and false invoices).

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[1] All comments received will be made publicly available without change. Personal identifying information, such as names or e-mail addresses, will not be edited from submissions. Therefore, commenters should submit only information that they wish to make publicly available.

[2] "Municipal advisor" is defined in Section 15B(e)(4) of the Exchange Act as "a person (who is not a municipal entity or an employee of a municipal entity) that: (i) provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues; or (ii) undertakes a solicitation of a municipal entity.

[3] The term "municipal entity" is defined by Section 15B(e)(8) of the Exchange Act as: "any State, political subdivision of a State, or municipal corporate instrumentality of a State, including -- (A) any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (B) any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (C) any other issuer of municipal securities."

The term “obligated person” is defined in Section 15B(e)(10) of the Exchange Act to mean “any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities.”

[4] Exchange Act Release No. 63599; File No. SR-MSRB-2010-16 (December 22, 2010).

[5] By separate notice, the MSRB has requested comment on a draft interpretive notice concerning a municipal advisor’s fiduciary duty to a municipal entity client. *See* MSRB Notice 2011-14 (February 14, 2011). The MSRB has also requested comment on the application of Rule G-17 to underwriters of municipal securities. *See* MSRB Notice 2011-12 (February 14, 2011).

Alphabetical List of Comment Letters on MSRB Notice 2011-13 (February 14, 2011)

1. American Federation of State, County and Municipal Employees: Letter from Gerald W. McEntee, International President, dated April 11, 2011

2. American Governmental Financial Services: E-mail from Robert Doty dated April 11, 2011

3. B-Payne Group: Letter from John B. Payne, Principal, dated March 28, 2011

4. Catholic Finance Corporation: Letter from Michael P. Schaefer, Executive Director, dated April 11, 2011

5. Municipal Regulatory Consulting: Letter from David Levy, Principal, dated April 11, 2011

6. National Association of Independent Public Finance Advisors: Letter from Colette J. Irwin-Knott, President, dated April 11, 2011

7. Not for Profit Capital Strategies: E-mail from Ed Crouch, dated February 14, 2011

8. Public Financial Management: Letter from Joseph J. Connolly, General Counsel, dated April 8, 2011

9. Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated April 11, 2011

AFSCME
We Make America Happen

April 11, 2011

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

Re: MSRB Notice 2011-14 Fiduciary Duty of Municipal Advisors
MSRB Notice 2011-13 Fair Dealing Obligations of Municipal Advisors
MSRB Notice 2011-12 Underwriters of Municipal Securities

Dear Mr. Smith:

The American Federation of State, County and Municipal Employees ("AFSCME") is the largest union in the AFL-CIO representing 1.6 million state and local government, health care and child care workers. AFSCME members participate in over 150 public pension systems whose assets total over $1 trillion. In addition, the AFSCME Employees Pension Plan (the "Plan") is a long-term shareholder that manages $850 million in assets for its participants, who are staff members of AFSCME and its affiliates.

AFSCME is pleased to have the opportunity to voice support for the rules proposed by the Municipal Securities Rulemaking Board ("MSRB") which delineate the fiduciary duty of municipal advisors with respect to their municipal entity clients, the obligations of municipal advisors to deal fairly with their current or prospective clients, and the requirements that underwriters have towards issuers of municipal securities. We applaud the efforts of the MSRB to protect municipal entities from self-dealing and other deceptive practices. Strong protections are required for municipal entities.

During consideration of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), AFSCME strongly supported the inclusion of provisions establishing the strongest possible market reforms, oversight and transparency for the "shadow markets" and other major provisions addressing corporate governance and investor protection. Investor protections important to AFSCME members include new market reforms addressing the sale of derivatives products and strategies, duties owed by firms and individuals offering investment advice, greater transparency for the

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advisors to hedge funds and private equity investments, and improved safeguards for municipal markets.

In each of these rulemaking contexts, vendors of various investment products and services have raised concerns that new obligations of disclosure or other investor protection remedies are not workable. Perhaps unsurprisingly, many Wall Street firms and their different lobbying entities argue that new investor protections under Dodd Frank may also trigger obligations under federal pension law. The implementation of market reforms requires both coordinated rulemaking designed to facilitate the operation of well-functioning markets that deserve investor confidence, and a big picture view that prevents evasion by those who would delay and dilute market reforms. We urge the MSRB to keep both of these in mind.

One of the areas targeted by tactics of delay and misdirection is the definition of "investment advice." During passage of Dodd-Frank, workers, seniors, consumers, savers, and investors joined together to urge that the law be strengthened regarding the responsibilities of those who give investment advice, that it be "clarified" where doubt had been raised, and that it be expanded to areas – for example, over-the-counter derivatives – where it has become painfully clear that restrictions on sound market requirements were ill-advised, to say the least.

Entities that give investment advice sell both advice and products (or products and services) bundled together. These firms and their subsidiaries or affiliates sell advice, and products to "implement" that advice, in more than one market. Distinguishing advice from the products it recommends is hard to do. Identifying the accountable provider – the firm with the household name or the call center employee who answers the phone – is hard to do. Distinguishing the price of advice from the price of the product or service – and further distinguishing those prices from the amount "at work in the market" – is hard to do. Distinguishing who got paid what and works under what incentives is hard to do. Distinguishing when the worker or pension plan trustee or buyer responsible for other people's money is talking to an advisor, or another kind of provider, is hard to do. Knowing which hat is being worn by which affiliate is hard to do.

After reviewing the comments submitted by large financial firms to the different regulators, and the efforts to create cover for rolling back reforms one more time through the same old tricks of deregulating and defunding, it is hard to imagine that this difficulty is not exactly their goal. Regulators must be steadfast in order to cut through the smokescreen which permits financial firms to continue operating with serious conflicts of interest, to the detriment of investors.

In spite of the great overlap in the entities that provide advice and products (or strategies) in different markets, Wall Street firms argue that the differences are

huge and that any potential overlap in duties must be avoided. They prefer to redefine – or not define – "advice" anew in every market and every context. They limit the definition of the recipients eligible to receive the duty that comes with providing advice. They work to limit the types of products and strategies to which any advice-related duty could apply. They work to craft language limiting the application of any duty.

The harms to be avoided are always alleged to be these: too much disclosure risks seller liability; sellers withdrawing from the market; competition forces diminishing; investor choice narrowing; and prices rising. So, the argument goes, too much disclosure is bad for investors. We find this difficult to believe, and we urge you to take a very hard look at this logic.

When pension assets are involved, firms that seek to avoid their obligations warn that too much information disclosed by service providers may result in misunderstandings and promote bad decisions. It may intrude on proprietary information (meaning they have no obligation to tell clients), it certainly will cost sellers to disclose more, and they certainly would have to bill investors for that.

The challenges around implementing effective fiduciary duties are clearly present in the ongoing efforts at the MSRB. Dodd-Frank directs the MSRB to establish rules with respect to municipal advisors that "prescribe means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients." And MSRB Notice 2011-14 requesting comment on draft guidance on a fiduciary duty of municipal advisors attempts to do that.

Yet the text itself warns that this guidance was developed based on the statutory language of Dodd-Frank, and that it was developed "without regard to any interpretation of that term proposed by the SEC in its proposed permanent registration rule for municipal advisors", and that MSRB may revise its own proposed guidance and may seek additional comment. Furthermore, the SEC proposal does not define exactly what constitutes the "provision of advice" though it gives examples of the types of "advice" that would trigger "municipal advisor" status and a duty to register under the proposal. At this time there is little that appears definitive. Careful review of the whole record – and continued input - will be very important.

MSRB noted several very important issues in the comment it submitted to the SEC regarding the definition of municipal advisor for purposes of SEC registration. Given the importance of these issues to AFSCME members, and the interplay with the scope of the fiduciary duty on municipal advisors addressed in this rulemaking proposal, we would like to address them here.

First, the MSRB noted that the SEC's proposed rule would benefit from a wording change to narrow the exclusion from municipal advisor registration for CFTC-Registered Commodity Trading Advisors in order to clarify that the exclusion "is available only when the registered commodity trading advisor is providing advice relating to swaps (as defined in Section 1a(47) of the Commodity Exchange Act and Section 3(a)(69) of the Exchange Act, and the rules and regulations thereunder." In other words, "the exclusion would not be available to such registered commodity trading advisors engaged in any other municipal advisory activities, including providing advice relating to any municipal derivative other than a swap".

The MSRB also provides several additional comments that show the complexity of the connection among investment advice obligations:

> The MSRB notes that Section 913 of Dodd-Frank and the effort to hold brokers to a fiduciary standard when giving advice comes into play in this marketplace and that "the Commission may, by rule, provide that the legal standard for securities transactions effected by broker-dealers with municipal entities shall be the same as the standard applicable to investment advisers under the Investment Advisers Act and, pursuant thereto, could replace the existing suitability standard with a fiduciary standard." SIFMA and others have urged that the SEC be given time to act first.
>
> The MSRB further noted its belief that public defined contribution pension plans fall squarely within the description of "investment strategies" and investment activities that trigger SEC registration of municipal advisors. The MSRB also "believes it would be appropriate to include public defined benefit pension plans as well, since they share many of the same potential direct or indirect impact on third-party beneficiaries and generally are exempt from the protections afforded by the Employee Retirement Income Security Act (ERISA) to private pension funds. Thus, in general, investment strategies would include such strategies relating to investments by all types of public pension funds other than broker-dealer recommendations "about a transaction such broker-dealer itself effects that is subject to federal broker-dealer suitability and related business conduct standards."
>
> Finally, the MSRB notes its reading of the language and legislative history of Dodd-Frank as "strongly indicative of a Congressional intent that advice by advisors to municipal entities, particularly in but not necessarily limited to the context of a municipal securities offering, was intended to be regulated under a single comprehensive municipal advisor regulatory construct", under which CFTC would be responsible for "comprehensive regulation . . . of the swap activities of swap dealers and major swap participants (including advice on swaps provided to special entities)", and MSRB would provide for

> "comprehensive regulation . . . of most typical non-dealer advisors to municipal entities (including advisors, other than swap dealers and major swap participants, providing advice on municipal derivatives).'

The MSRB says that strengthened coordination among the MSRB, the SEC and the CFTC would promote a more efficient and effective implementation of the Dodd-Frank Act and would reduce the compliance burden on market participants. This includes small municipal advisors who might provide advice to an issuer on a variable rate demand offering (VRDO) involving an interest rate swap which could be subject to MSRB rules as a municipal advisor in connection with advice on the new issue offering, while simultaneously becoming subject to distinct CFTC rules as a commodity trading advisor in connection with the swap. We again encourage such coordination among the agencies.

Another danger to avoid is that some sellers will carve themselves out of disclosure duties, that they will succeed in scaling back the reach of market reforms and staggering the effective dates, and fall artfully between the cracks. This would leave investors in a "buyer beware" bind, which might be filled by small independent advisors. These small firms would end up stepping into the disclosure breach and facing potential responsibility for unearthing the truth that sellers did not reveal.

The MSRB strongly recommends coordination. That is essential – not delay but real coordinated rulemaking. As a part of that process, both during rule development and after specifics are finalized, the MSRB, the SEC and the CFTC should undertake a series of efforts – similar to those typical of the Department of Labor's ERISA regulators - to issue not only clear explanations of their formal guidance but also informal guidance in the form of Frequently Asked Questions, regional meetings and internet webinars and other forms of explanation that help the market participants – including workers, pension participants, investors, and pension trustees – make informed decisions, knowing both the players and the rules.

Another MSRB Notice, 2011-12, requests comments on proposed interpretive guidance regarding the duty of dealers in their interactions with municipal entities as underwriters of municipal securities, "including integrally-related activities, such as interest rate swap transactions and purchases of defeasance escrow securities". The MSRB states that this duty to deal fairly requires, among other things, disclosure of all material risks and characteristics of the financing of complex municipal securities (such as a VRDO with a swap), as well as disclosure of any incentives for the underwriter to recommend the financing (e.g., third-party payments, certain credit default swaps, and profit-sharing arrangements with investors).

The duty of fair dealing here is also defined as including "an implied representation that the price an underwriter pays to an issuer bears a reasonable relationship to the prevailing market price of the securities. An underwriter's direct and indirect compensation for a new issue must not be excessive (i.e., disproportionate to the nature of the underwriting and related services performed)."

It seems reasonable to anticipate that this notice, too, will require coordination to ensure effective implementation and investor protection. Only that kind of coordinated implementation will fulfill the promise of Dodd-Frank and build back greater trust in the integrity of the financial markets and greater stability in the economy overall.

* * *

We appreciate the opportunity to express our views on this matter. Should you have questions regarding our comments, please contact Lisa Lindsley at (202) 429-1275.

Sincerely,

GERALD W. McENTEE
International President

From: Robert Doty
Sent: Monday, April 11, 2011 7:18 PM
To: Peg Henry
Subject: Comments on Drafts Proposals Relating to Rules G-17 and G-36

Thank you for this opportunity to comment on the Board's draft proposals to issue a new Rule G-36 and interpretative notices relating to Rule G-17 and G-36.

I do not have extensive comment regarding these proposals because I believe that the Board has made sound proposals.

In particular, I appreciate the Board's sensitivity to the subtleties of the fiduciary duty and its inclusive recognition of the duty of loyalty and the duty of care owed by municipal advisors to their clients. For too long, some advisors, purporting to serve municipal issuers, have focused excessively on the closing of the "deal," rather than on the provision of appropriate advice to their clients. The potential for explicit limitations on the scope of the relationships should alleviate concerns that some may have.

Among other things, the proposal to require that firms clarify for clients the advantages and disadvantages of various forms of advisor compensation is excellent. Too many municipal issuers are gullible regarding the use of contingent compensation payable only after transactions are completed. They do not think through the long-term costs and other relevant implications of contingent compensation that can place advisors, upon whom the issuers rely heavily, in the unfortunate position of sacrificing months of work without compensation when it becomes apparent (or should be apparent to a market financial professional) that a transaction is not in the issuers' best interests. Unfortunately, there are advisors who would plow ahead in order to avoid substantial financial loss, rather than informing the issuer clients either (1) not to proceed or (2) to alter the structure or approach.

I commend the Board for its awareness of these issues for market professionals who have a fiduciary duty, and am hopeful that the Board will continue to act with that awareness and sensitivity as it moves forward with the implementation of the fiduciary duty, fair dealing concepts, professional standards and other aspects of municipal advisor regulation.

Robert Doty
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B-Payne Group Financial Advisors

March 28, 2011

To: Securities & Exchange Commission and Municipal Securities Rulemaking Board Regulators,

Re: Proposed Regulations for Independent Municipal Financial Advisors

OVERVIEW:

I have long intended to comment on the MSRB's proposed regulations for independent municipal financial advisors, "FAs". I spent a few hours reading and thinking about the over two-hundred pages of proposed and "explained" regulations, but never got around to commenting for the record. Nevertheless, earlier this week I found your email address in an article by The Bond Buyer, and, as it was convenient to do so, I decided to submit my recommendations through that channel. Please understand that I am not a securities lawyer, so my comments are of a general nature and intended to help all parties understand the impact of this measure on my small business.

Before commenting, I'll summarize my experience. I began my career as a State Budget Analyst with the State of Ohio in 1983. I soon was assigned to assist the legendary Herb Kruse manage and track all state debt issuances that were controlled by the Governor's office. I moved on from there in 1989 to Ehrlich Bober, where I began my career as a public finance investment banker. On Ehrlich's departure from the business in 1991, I moved to A.G. Edwards and built a business and highly respected career for 14 ½ years. My next move was to Robert W. Baird to manage and build a "traditional" public finance operation in Ohio to complement its existing group of Ohio "structured" finance experts. I stayed at Baird for 4 ½ years and left in February 2009 to create my own advisory business. My clients are primarily the least understood in the marketplace – small- to medium-sized school districts, counties, and cities - and my client base is extensive. I believe I am very well known in state circles and that my reputation is excellent. (At least no one has told me otherwise, and I have never had even the smallest complaint about my work.) To further understand my business, please visit my website at bpaynegroup.com.

The bullet points below summarize my thoughts. Details and recommendations follow.

- Regulatory Framework – Using the financial advisor/stock broker regulatory framework to regulate a small handful of FAs in Ohio is impractical. It's like building a billion dollar damn to

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regulate Old Mill Creek. Unlike the damn, however, this overkill is difficult to see, as is the eventual fallout for the small operations like mine that simply fade away under the burden. Keeping emails and correspondence is relatively painless, but the vast number of forms and required procedures are punitive. There is a much more practical and cost efficient way to do this, which I will recommend herein.

- Compliance Costs: I don't pretend to understand the regulators guesses at my compliance costs. The fact is, cost estimates published in the proposed regulations are wild guesses and were obviously generated by analysts who know absolutely nothing about my business. I estimate my costs to be a minimum of fifty thousand dollars or as much as hundreds of thousands of dollars. That would be fine if I employed twenty or more professionals including a lawyer and systems professional. I don't. The paperwork, seminars, lawyer bills, supervisory red tape and excessive opportunity costs in the proposed regulations are a small advisor death sentence in my opinion. Add to this the burden of record keeping for the tax filings I have to make to federal, state, and local levels and you have a regulatory burden with a potential cost of well over a half million dollars a year in cost and lost opportunities.
- Real-life Impact: I have one full-time employee whose job is seriously threatened by the cost of these regulations. She is a single mother who has been with me for years, and she plays a critical part of my business model. I have one part-time employee with good experience in the business, who supplements his education-related income by providing FA services to a select group of issuers, and I have another limited-time (12 hours per week) employee who is in his first job, doing a great job, and trying to build a resume. Not a single one of these jobs is safe now.

DETAILS:

Regulatory Framework Is Flawed - The basic premise of the regulations is tragically flawed. The premise of the FA regulations seems to be that government finance officers and legislative bodies will benefit from the same level of protection and protective procedures that "Sam the retired grocer" needs when dealing with retail stock brokers and his life savings. Using the same regulatory "architecture" for independent FA's and retail brokerage clients is a mistake and an example of extreme regulatory overkill. FAs are much different from registered stock brokers in three very important ways that also make us easier to regulate: 1) there are a relatively small number of FAs and a sea of brokers; 2) brokers manage and have access to clients' accounts and FAs do not, serving almost exclusively as advisor middlemen; 3) FA clients are mostly sophisticated industry professionals who realize that they have a duty of care to the

public, just as we have to them – broker clients are often quite defenseless and have only themselves as a final check.

I ask you to seriously compare my clients' situations to Sam above who may not know the difference between an annuity and a football and who is working with one of possibly thousands of random brokers in the state. I don't touch my clients' money and never have access to their accounts even if I wanted it, yet my clients have the qualifications necessary to know exactly what I'm doing, while Sam is quite defenseless. I realize that many of the perceived FA problems in the business over the past years are the result of poor decision making at the government level, due to lack of oversight and budgetary discipline. Therefore, local issuers should be prodded to recognize that they have a duty of care in this area to choose their advisors and bankers carefully. Federal regulators shouldn't try to "back door" this oversight through the FAs just because they can't get to the government officials. Figure out another method. Work with the states to increase local-finance-officer training and regulation or something along those lines, but don't expect to get better behavior from local government finance officers and elected officials by smothering me with regulations. It won't work.

To be fair to the legislators and regulators, I have asked myself this question: do I have issuer clients who are ill prepared to understand and make sensible decisions about debt issuance? Of course I do. I don't expect any of them to understand what it has taken me twenty-five years to learn simply because I try to explain it to them in a few visits. Therefore, I am intensely aware of my fiduciary responsibility. Are there bad FA apples out there who don't always deal "honestly" and "fairly" (at least as a group of knowledgeable and sensible people would define those two words)? I am saddened to say, perhaps there are. Unfortunately, email tracking, testing, and so on will have no effect whatsoever on FA actions. Those bureaucratic nuisances simply kill private jobs and hurt efficiency. Sure, we could use some oversight. However, the FA world is small and thus can be reviewed much more simply than the brokerage world can. For example, I can name only four active and well-known independent FAs working the Ohio local government market. If you want to find out who among us may need some guidance, if any, get someone on the ground here in Ohio who can ask around. Perform an occasional random transaction review. The point is, you can't prevent abusive behavior with burdensome, irrelevant paperwork, but you can certainly discourage such behavior with occasional inquiries handled by someone on the ground who actually knows the neighborhood. Otherwise, we are simply creating another federally-mandated paper jungle that fails to accomplish its intended goal. To be clear, I am

recommending that you hire an expert for each state or region that you define, one who has an impeccable reputation for fairness and quality, to explore and discourage sloppy or unfair work among the area's FAs. Then, you could discard the bulk of your regulations, needless testing, and paperwork. The standard fraud and fairness laws would be enough.

Compliance Costs – Over my 20 years as an investment banker and independent financial advisor, 70% of my revenue has come from approximately 25% of my clients. Finding and retaining that 25% is critical to survival. The challenge is knowing when and where you will find that opportunity. Therefore, I have to be on the street, at conferences, and on the phone more than I really have time to be. And whenever I am taken away from those activities for regulatory administrative work, the more likely I am to fail. This is particularly worrisome in my position because the bulk of my clients are very small, as are my fees. Unfortunately, transaction work for small governments can be more time consuming and demanding than for larger governments, and the required degree of care is often higher.

Therefore, I expect my compliance costs, including opportunity cost, to be far in excess of my income in any year. I feel like a small business poster child for the crippling effects of onerous federal regulations. Believe me when I say that I am on the very edge of closing my doors rather than confronting this federal attack. And it's the small issuers, who need my services most, who will suffer for that. This will be bad for Ohio's small government issuers, bad for me, and good for the big boys. I'm sure that was the intention of some in Washington, but I doubt it was the intention of Congress.

If you have any interest in helping start-up advisors like me survive this process, I recommend being explicit about exemptions for small independent advisors. I can manage and support fee and conflict disclosures and outgoing email and client file retention, but that is it. And I could write rules to that effect in a sentence or two. Two-hundred and thirty pages seems a bit much.

Fees and Fair Dealing - The regulations focus a great deal on "fair dealing" and fees. I agree that our government finance officers are responsible for managing the fees they pay. They should know what they are agreeing to pay up front when possible, if a fixed fee or percentage fee, and get a cap if an hourly fee. The proposed regulations on fee disclosure are manageable and sensible – perhaps long overdue for all professionals in the public finance business. Rather than just FAs, however, all parties - FAs, bond lawyers, and underwriters - should be required to disclose any and all fees that they or any

partner may charge prior to the engagement. That's where the regulation must stop, however. Judging the "reasonableness" of fees is an impossible duty for any out-of-state regulator, due to the vast differences in required services for unique issues and clients. There isn't a regulator alive, of whom I am aware, who knows enough to tell my clients if my fees are reasonable or not. Please do not misunderstand me, though. If the news reports on fees for the swaps and swaptions executed for certain Pennsylvania schools are true, those who charged those fees and achieved such miserable results should be called out. However, I need fee flexibility not tied to a regulator's uninformed opinion about what the fee should be. Not to be able to charge more for some and less for others will achieve the exact opposite result intended by the regulations; the small issuers most in need of the very best services and expertise will be left to the amateurs; that is, the least experienced and skilled "advisors" on the staffs of the large firms.

Again, my recommendation is to get experienced personnel on the ground in regional markets and charge them with staying on top of situations. They will know where there might be problems and their presence alone will encourage all parties to act in their clients' best interests. It's very difficult to define fairness or fair dealing for this work because the work is so different for each client, but we know what's right as a group of professionals in Ohio (FAs, underwriters, and counsel), and when someone is suspected of violating what's considered right, word gets around quickly. Having a qualified and respected person on the ground in the region would bring things into focus for the long-term benefit of all of us, including the issuers. Again, I am recommending creating an ombudsmen sort of position by local region and filling it with a known and respected individual, then discarding specific regulations in favor of much broader guidance and much less paperwork and bureaucracy.

Testing - Testing is another area I fear will be managed poorly by the regulators if history is any guide. Years ago, I was required to pass the Series 7 Registered Securities Representative test to be a public finance investment banker. The funny thing was that it had nothing to do with my job. Besides that, the test questions were so basic and irrelevant that the tests served no purpose other than to waste an entire day. Likewise, the thinking that bi-annual continuing education and initial licensing tests will help regulate public financial advisors is well-meaning, but Pollyanna. Over the years in the public finance world, testing and continuing education sessions were laughed at as absolute wastes of productive time. I have no suggested alternative other than to just totally discard them.

Summary - The proposed FA regulations are well-intentioned, I'm sure. On the whole, however, they are a perfect example of well meaning but destructive government officials creating significant barriers to business and job growth. Worse yet, they will have absolutely no positive impact. The good news is that it doesn't have to be this way. Please, resist creating another massive bureaucracy with stultifying mounds of paperwork and administrative overkill. Back off and take a close look at who you are regulating before finalizing any rules and procedures. I believe you will realize you can do this much more efficiently simply by hiring an effective employee or two.

After reading the regulations, I had a long conversation with my staff and wife about closing my doors. Those conversations are ongoing and unsettled. It would be a shame to close, because my clients need my help badly and trust me implicitly, and they would be the first to tell you so.

Respectfully submitted for consideration,

John B. Payne

Principal (and serving as cfo, compliance officer, marketing vice president, vice president of accounting, and independent financial advisor)

Copies to:

Securities & Exchange Commission
Municipal Securities Rulemaking Board
Honorable Sherrod Brown
Honorable Rob Portman
Honorable Steve Austria

Catholic Finance CORPORATION

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April 11, 2011

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314
Via email: commentletters@msrb.org

Re: MSRB Notice 2011-13 (February 14, 2011) Request
Municipal Advisors

Dear Mr. Smith:

The following comments are submitted by Catholic Finance Corporation ("CFC") to the Municipal Securities Rulemaking Board ("MSRB") relating to MSRB Notice 2011-13 (February 14, 2011) concerning the Application of MSRB Rule G-17 to municipal financial advisors. CFC appreciates the opportunity to respond to the request for comments by the MSRB.

CFC is a nonprofit corporation and has been determined to be an organization described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the "Tax Code") under the group determination letter of the Internal Revenue Service to the United States Conference of Catholic Bishops by inclusion in the Official Catholic Directory. CFC was formed to provide financial assistance and financial advisory services to other entities within the Catholic Church. Some of the services provided by CFC are municipal advisory services to obligated persons.

This background is presented to provide the context for our comments which relate to nonprofit advisors, advisors created to provide services to a group of related nonprofit entities as obligated persons rather than the actual political subdivision issuing the municipal securities. Additional specificity or clarification in the rules is requested with respect to some unique aspects of municipal advisory activities of the above-described municipal advisors.

The discussion of disclosure of transaction risks should more specifically address transactions with multiple parties potentially subject to the same disclosure requirements or multiple transactions with the same parties and same risks.

The first paragraph entitled "Appropriateness" under "Fair Dealing" states that a municipal advisor recommending a transaction or product to a client must advise the client of material risks and incentives. Pursuant to the draft interpretive notice for underwriters in MSRB Notice 2011-12 (February 14, 2011), such notice must be in writing and described the officials to whom the disclosure must be made. Do the similar disclosure requirements under the draft

interpretive notice for municipal advisors carry implied requirements of being in writing, and to certain officials? Does the municipal advisor need to disclose the risks of a specific negotiated transaction recommended by an underwriter, itself required to disclose such risks? We request that, where an underwriter has proposed a specific transaction in a negotiated financing and has adequately disclosed the risks with that structure, the municipal advisor need not separately again disclose such risks. Likewise, when an advisor has a long standing relationship with a client which has experience with, and a thorough understanding of, the risks of a specific type of transaction, and the advisor has in the past disclosed the applicable risks, the interpretive notice should not require a formal disclosure again on similar subsequent transactions to comply with the rule.

The interpretive discussion of forms of compensation, solicitation and related conflicts should address the disclosures, if any, required in connection with soliciting municipal advisory services by an underwriter who links the engagement and fees with a separate engagement as underwriter on a different financing for the same client. Fees may be quoted on a composite basis or heavily discounted on one aspect of the representation in consideration of fees in the other engagement. The combined fees may also include services not covered by the rule. Thus, the municipal advisory services may be presented as free or at a very low cost.

The interpretive guidance on payments and gifts should specifically address the activities of nonprofit charitable entitles performing some municipal advisory work for clients it deals with in other capacities or for clients which are related entities. We are a non-profit entity with the specific exempt purpose of providing financial advice at no or reduced compensation to related non-profit corporations throughout the country. Further, we have also loaned proceeds of fund raising at subsidized interest rates to such related entities primarily for capital projects within their exempt purpose, participated in loans from other commercial lenders and provided collateral for conventional loans. Most of this activity is unrelated to municipal finance. Financial benefits, reduced charges for services and other items of value provided by a financial advisor, which is a 501(c)(3) charitable entity and which activities are within its exempt purposes, should be specifically exempted. While we do not believe that these activities are, or were intended to be, included within the scope of MSRB rules, dealing with kickbacks, gifts or gratuities, as a charitable organization, we are constantly concerned with compliance with legal requirements. Express requirements addressing the particular situation of nonprofit corporations in this area would be appreciated. Uncertainty may have a chilling effect on our charitable activities.

Furthermore, as a consequence of our successful implementation of our exempt charitable purpose, much of our work comes from referrals by entities for which we have done work. We do not believe referrals from previous or existing clients cause such entities to be considered to be soliciting business on our behalf. However, in light of our charitable activities, free services and other financial assistance to clients in the normal course of business, we would request further clarification that such charitable activities within our exempt purpose under the federal tax code do not result in characterizing clients giving voluntary referrals as paid solicitors.

We thank you for your thoughtful consideration.

Sincerely,

Michael P. Schaefer
Executive Director

cc Paul Tietz, Briggs and Morgan

MUNICIPAL REGULATORY CONSULTING

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April 11, 2011

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

Sent via email to CommentLetters@msrb.org

Re: MSRB Notice No. 2011-12: 2011-13; 2011-14

Dear Mr. Smith:

Thank you for the opportunity to comment on the various matters included within the Requests for Comment on MSRB's Rules G-36 and G-17. Municipal Regulatory Consulting LLC is a professional consulting firm serving the municipal securities industry. In providing regulatory advice to municipal advisors and broker-dealers, I am sometimes called upon to interpret rules of the MSRB and other agencies or SROs. More to the point, my clients often seek advice how to apply those rules in the context of their business.

If anything is clear at this point in the rulemaking process spurred by the Dodd-Frank Act, it is that nothing is clear. Virtually all the rules and guidance proposed by the MSRB in 2011 come with the following explicit or implicit caveat: "Until the SEC settles on a definition that everyone can understand, even we (the MSRB) aren't certain what specific activities qualify as municipal advisory activities, nor do we know for certain when they begin. If we don't know which activities are advisory, we also don't know exactly who the advisors are. But we've been told we have to propose rules, so here they are." Market participants may have sympathy for the position in which the MSRB finds itself, but they have to react to what has been proposed, and many wonder given the circumstances why the MSRB has not chosen to be more circumspect.

I believe the proposals as written do not resolve but exacerbate confusion among market participants, including issuers, and create potential compliance nightmares. The MSRB would do the municipal securities community – including the issuers it is now mandated to protect – a great service if it scales back its proposals, moderates some of its positions and clarifies others.

1. The MSRB Should Do No More than Establish Guiding Principles

The MSRB does well by taking a minimalist approach to Rule G-36. "In the conduct of its municipal advisory activities on behalf of municipal entities, a municipal advisor shall be subject to a fiduciary duty, which shall include a duty of loyalty and a duty of care." It is obviously modeled after Rule G-17, which reads, "In the conduct of its municipal securities or municipal

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advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice."

Unfortunately, the MSRB goes too far and too deep in its efforts to address as many different aspects of the duties of loyalty, care and fair dealing as it can. The goal at this stage in the regulatory cycle, with certain market participants subject to rules and regulations for the first time, should be to promulgate rules everyone can understand and with which they can readily comply. Now is a time for establishing guiding principles. There will be plenty of time later for crawling in the weeds.

For example, the MSRB appropriately addresses the duty of loyalties and care by stating its view of the general principles underlying each. The duty of loyalty "requires the municipal advisor to deal honestly and in good faith with the municipal entity and to act in the municipal entity's best interests without regard to financial or other interests of the municipal advisor." The duty of care requires a municipal advisor to "exercise due care in performing its responsibilities."

The MSRB also does the regulated community a service by aggregating in a series of footnotes a variety of cases in which individuals or firms were found to have violated their fiduciary duty or fair dealing obligations under federal and state law and/or securities regulation. It would be reasonable for the MSRB to state that the activities with which the defendants in those cases were charged would violate Rule G-36 and/or Rule G-17. At least for now, however, the MSRB should stop there.[1]

2. If the MSRB Wishes to Regulate Specific Market Activities, It Should Do So In Rules Designed Specifically to Address that Activity

a. Issues Relating to Advisory Contracts Should Be Addressed in Rule G-23

In my view, the MSRB unreasonably intrudes on the commercial relationship between issuers and advisors when it specifies exactly who needs to say what to whom and when. The error is compounded because the MSRB fails to allow for variance when the facts and circumstances suggest that another approach would better accomplish the stated goals. Indeed, the MSRB's rigid requirements might even have the (presumably) unintended consequences of confusing issuers and creating an unlevel playing field between advisors and underwriters.

[1] An argument can be made that going one step further, *i.e.,* stating as a general proposition that material conflicts of interest should be disclosed, would not be one step too far, but stepping on that slippery slope led to the MSRB sliding all the way down the hill. Micromanaging the disclosure requirements – especially the ones relating to compensation - as the MSRB does would be difficult to justify even after time has passed; at this stage of the process, it makes no sense at all.

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For many years, the MSRB had a straightforward approach to when and under what circumstances a financial advisory relationship existed between an issuer and a dealer firm. In Rule G-23, it said

> (b) *Financial Advisory Relationship.* For purposes of this rule, a financial advisory relationship shall be deemed to exist when a broker, dealer, or municipal securities dealer renders or enters into an agreement to render financial advisory or consultant services to or on behalf of an issuer with respect to a new issue or issues of municipal securities, including advice with respect to the structure, timing, terms and other similar matters concerning such issue or issues, for a fee or other compensation or in expectation of such compensation for the rendering of such services. Notwithstanding the foregoing, a financial advisory relationship shall not be deemed to exist when, in the course of acting as an underwriter, a broker, dealer or municipal securities dealer renders advice to an issuer, including advice with respect to the structure, timing, terms and other similar matters concerning a new issue of municipal securities.
> (c) *Basis of Compensation*. Each financial advisory relationship shall be evidenced by a writing entered into prior to, upon or promptly after the inception of the financial advisory relationship (or promptly after the creation or selection of the issuer if the issuer does not exist or has not been determined at the time the relationship commences). Such writing shall set forth the basis of compensation for the financial advisory services to be rendered, including provisions relating to the deposit of funds with or the utilization of fiduciary or agency services offered by such broker, dealer, or municipal securities dealer or by a person controlling, controlled by, or under common control with such broker, dealer, or municipal securities dealer in connection with the rendering of such financial advisory services.

For some reason, the MSRB did not extend Rule G-23 to non-dealer municipal advisors and/or modify Rule G-23 to address what it views as shortcomings in the contents of advisory contracts. Instead, the MSRB chose to make the content and context of written disclosures a subject of interpretive guidance under the rubric of fiduciary duty and fair dealing. If the MSRB feels so strongly that it needs to specify what goes in contracts, I submit that it should do so by rule and not by interpretation, and subject that proposal to the usual scrutiny and process that apply to rule changes.

b. Issues Relating to Appropriateness or Suitability Should Be Addressed in Rule G-19

The MSRB also has a rule that relates to the obligations of dealers when they recommend transactions to customers. The rule even distinguishes among (i) institutional accounts and non-institutional accounts and (ii) discretionary accounts[2] and non-discretionary accounts. Rule

[2] It is generally accepted that firms have a fiduciary duty with respect to discretionary accounts, though the term fiduciary does not appear anywhere in Rule G-19.

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G-19 imposes obligations on dealers to obtain certain information about its customers and about the products it offers before making any recommendations to customers.

As was the case with contracts, for some reason the MSRB chose not to address recommendations to municipal entity or obligated person clients by amending Rule G-19. Instead, the MSRB proposes to address these issues by issuing interpretive guidance under Rules G-36 and G-17. What is worse, it uses language utterly foreign to municipal regulation. Thus, depending on the circumstances and whether the client is a municipal entity or an obligated person, an advisor might have one or more of the following duties:

- To investigate and advise the municipal entity of alternatives to the proposed financing structure or product that are then reasonably feasible based on the issuer's financial circumstances and market conditions at the time, if those alternatives would better serve the interests of the municipal entity.
- To make a reasonable inquiry as to the facts that are relevant to a municipal entity's determination of whether to proceed with a course of action.
- To act competently and provide advice to the municipal entity after making reasonable inquiry into the representations of the municipal entity's counterparties, as well as then reasonably feasible alternatives to the financings or products proposed that might better serve the interests of its municipal entity client.
- To recommend a transaction or product only if it has concluded, in its professional judgment, that the transaction or product is appropriate for the client, given its financial circumstances, objectives, and market conditions, and advise the client of material risks and characteristics of the structure or product.

If the MSRB believes that municipal advisors have an obligation to municipal entity and obligated person clients to "know their customer," and to have a "reasonable basis" for recommending transactions, products or courses of action, the MSRB should abandon the multiple and confusing formulations quoted above.[3] The MSRB should simply say what it means in Rule G-19 and it should use terminology the industry already understands.[4]

3. The MSRB Should Abandon Appendix A Altogether

Even if the MSRB accepts my suggestion and chooses to address advisor compensation directly in Rule G-23 instead of in interpretive guidance under fiduciary duty or fair dealing, it should get rid of its inappropriate and ill-conceived attempt to demonstrate that all compensation

[3] The same principle applies to the MSRB's disclosure requirements in the context of "complex municipal securities financings," although it does not appear that the MSRB has imposed upon underwriters any suitability or appropriateness obligations when recommending any financing, complex or otherwise. Whatever the requirements, they should be set forth in Rule G-19.

[4] Among the advantages of using Rule G-19 is that there is a wealth of existing interpretive guidance relating to the concept of suitability and what is required to have a reasonable basis for making a recommendation.

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creates conflicts between advisors and issuers. The MSRB does indeed have a mandate to protect issuers, but it seems to me that there are many more important things to worry about than whether an advisor being paid by the hour is padding her bill. And there are better ways to do it than requiring a senior issuer official to attest in writing that he understands this "conflict" and is OK with going ahead anyway.

Conclusion

Writing guidance to establish the parameters of fiduciary duty and fair dealing is not easy. The MSRB should not make the task more difficult than it is by trying to fit so many things into boxes not designed to hold them. Instead, it should concentrate on establishing guiding principles and use the existing regulatory structure where possible to address specific concerns.

Very truly yours,

David Levy, Principal

cc: Martha Haines, SEC

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April 11, 2011

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

Re: MSRB Notice No. 2011-14; No. 2011-13

Dear Mr. Smith:

The National Association of Independent Public Financial Advisors ("NAIPFA") appreciates this opportunity to provide comments to the Municipal Securities Rulemaking Board ("MSRB") on proposed Rule G-36 and related interpretations (the "G-36 Notice") as well as the MSRB's proposed interpretation of Rule G-17 as it would apply to municipal advisors (the "MA Guidance"). NAIPFA addresses the MSRB's proposed interpretation of Rule G-17 as it would apply to underwriters (the "UW Guidance") in a separate letter also filed today.

NAIPFA, founded 21 years ago, is a professional organization composed of independent public finance advisory firms located across the nation. Our member firms solely and actively represent the interests of issuers of municipal securities.

PRELIMINARY STATEMENT:

Congress delegated to the SEC and the MSRB the responsibility to protect the interests of issuers, investors, and the public trust. NAIPFA believes these proposals must be read in light of and together with the various other proposals made by the SEC and the MSRB to meet that responsibility. In prior comment letters addressing (i) the registration of municipal advisors proposed by the SEC and (ii) Rule G-23 and related guidance proposed by the MSRB, NAIPFA has expressed concern that the proposals fail to recognize the realities of the marketplace and the lessons of the past. NAIPFA believes the rules proposed would impose significant regulatory burdens on firms that did not contribute in any meaningful way to the financial crisis or cause harm to issuers. At the same time, firms that directly caused or contributed significantly to the crisis will be largely free to continue the practices that led many issuers to enter into transactions that were not in their best interests but were very lucrative for the firms that recommended them.

Finally, NAIPFA is very concerned that the scope and tenor of MSRB proposed rules relating to municipal advisors reflects the desire of the MSRB's primary constituency, investment banks and

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broker-dealers, to limit the participation and influence of municipal advisors. Independent financial advisors recognize that many broker-dealers consider financial advisors to be a nuisance to the conduct of their business and regularly seek to exclude financial advisors from public finance transactions. The MSRB's proposed rules reflect this perspective by imposing relatively heavier burdens on municipal advisors than on broker-dealers.

The proposals and guidance we address in this comment letter suffer from the same flaws. They do not implement Congressional intent. They inappropriately and unnecessarily intrude on the relationship between advisors and their clients. And, most unconscionably, they fail to constrain the broker-dealers and investment banks. In short, the MSRB has placed shackles on the shepherds and told the wolves they should be nice to the sheep.

The Congressional Mandate:

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. Law No. 111-203) ("Dodd-Frank Act") amended Section 15B(c)(1) of the Securities Exchange Act of 1934 ("Exchange Act") to provide that municipal advisors have a fiduciary duty to their municipal entity clients. Section 15B(b)(2)(L)(i) of the Exchange Act directs the MSRB to establish rules with respect to municipal advisors that "prescribe means reasonably designed to prevent acts, practices, and courses of business as are not consistent with a municipal advisor's fiduciary duty to its clients."

Securities and Exchange Commission Release Number 34-63576; File S7-45-10 states Section 15B(e)(4)(A) of the Exchange Act, as amended by the Dodd-Frank Act, defines the term Municipal Advisor to mean a person (who is not a municipal entity or employee of a municipal entity) (i) that provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, or other similar matters concerning such financial products or issues, or (ii) that undertakes a solicitation of a municipal entity. The Release further states the definition of a Municipal Advisor explicitly excludes "a broker, dealer, or municipal securities dealer serving as an underwriter," as well as attorneys offering legal advice or providing services that are of a traditional legal nature and engineers providing engineering advice.

The Dodd-Frank Act defined municipal advisor activities to mean advising issuers and borrowers with respect to the structure, timing, terms, and similar matters concerning a municipal bond issue and defined underwriting activities to be purchasing and distributing securities. At this point the law and historical and legal distinction between advisory activities and underwriting activities are in accord. Advisors sit on the same side of the table as the issuer with all of the legal responsibilities that go

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along with being an advisor and underwriters sit on the opposite side of the table negotiating an arm's length transaction to purchase bonds.

The Dodd-Frank Act expanded the responsibilities of the MSRB to include the protection of municipal entities. It also required the MSRB to change the composition of its Board to one that is composed of a majority of members not affiliated with regulated entities. Accordingly, the MSRB amended its stated mission to include protection of the interests of issuers, as well as the interests of investors and the public trust. It also brought on new Board members.

The mission of the MSRB implies the duty of a fiduciary to the interests it protects. Changing the composition of the MSRB Board gave hope to issuers and independent advisors that the rules the MSRB promulgates would be less biased in favor of investment banks and broker dealers. Those hopes were dashed on February 9, 2011 when the MSRB filed with the SEC a proposed amendment to MSRB Rule G-23 and related interpretative guidance. That proposal would undermine the rule of law and subject municipal issuers to the same types of conflicts of interest the Dodd-Frank Act was enacted to prevent.

NAIPFA addressed the concerns of the organization regarding proposed Rule G-23 and interpretative guidance in its letter to the SEC dated March 11, 2011, a copy of which is attached to this correspondence. We reiterate those concerns. Furthermore, NAIPFA believes any rules regarding fair dealing, conflicts of interest, and fiduciary duty, or others for that matter, should:

1. Protect the interests of issuers, investors, and the public trust;
2. Avoid inconsistencies that place public interests at risk;
3. Be clear and easily understood by the parties that have to follow them;
4. Minimize the potential for public confusion regarding the law; and
5. Safeguard against the potential for firms to avoid the intent of the Dodd-Frank Act.

NAIPFA believes that the rules and guidance proposed by the MSRB thus far would, taken together, create a body of law which falls far short of providing the protections intended by the Dodd-Frank Act, places issuers, investors, and the public trust at risk to the types of actions the law intended to eliminate, and subjects issuers and the public to confusion and machinations of firms desiring to subvert the law.

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COMMENT:

A. Proposed Rule G-36

NAIPFA supports the proposed rule, as written. However, in view of the dynamic nature of the rulemaking process, and the fact that so much of what is being proposed is subject to the SEC's ultimate definition of "municipal advisory activity," NAIPFA expressly requests that the MSRB provide further opportunities to comment as the SEC's position crystallizes and the implications of that position become more clear.

B. The G-36 Notice and the MA Guidance

1. NAIPFA Seeks Clarification of the Relationship Between Rule G-36 and Rule G-17

The MSRB states in the G-36 Notice that advisors have both a fiduciary duty under G-36 and a responsibility under Rule G-17 to deal fairly with municipal entity clients. The MSRB goes on to note that "this Rule G-17 duty of fair dealing is subsumed within the municipal advisor's fiduciary duty, and a violation of Rule G-17 with respect to a municipal entity client would necessarily be a violation of Rule G-36." NAIPFA notes that the MSRB addresses certain matters in the MA Guidance that are not addressed, or are addressed differently, in the G-36 Notice.[1] NAIPFA notes further that the MA Guidance is, by its terms, applicable to the interactions between advisors and obligated persons. It is unclear, therefore, if the MSRB intended the obligations and/or duties of advisors to obligated persons also to be applicable to municipal entities. Accordingly, NAIPFA requests that the MSRB clarify its intent.

2. NAIPFA Objects to the MSRB's Compensation Disclosure Requirements

There is perhaps no greater example of the MSRB's misplaced zeal to "protect" issuers than its requirement that advisors warn issuers that each and every payment arrangement they enter into with an advisor is fraught with conflicts. The MSRB stated the eminently reasonable proposition that the duty of loyalty owed by an advisor to its municipal entity client "requires the municipal advisor to deal honestly and in good faith with the municipal entity and to act in the municipal entity's best

[1] For example, the MSRB in the MA Guidance cautions advisors that responses to RFPs "must fairly and accurately describe the municipal advisor's capacity, resources, and knowledge to perform the proposed municipal advisory engagement as of the time the proposal is submitted." It cites this as an example of the G-17 duty not to misrepresent or omit material facts in any representation made to an obligated person client. This example is not included in the G-36 Notice.

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interests without regard to financial or other interests of the municipal advisor." Had it stopped there, NAIPFA would happily have supported the principle.

However, the MSRB then goes on to state that "a municipal advisor must disclose all material conflicts of interest, such as those that might impair its ability to satisfy the duty of loyalty to its municipal entity client." The MSRB lists five particular "examples of the types of conflicts that must be disclosed by the municipal advisor:"

(i) Payments by municipal advisors made for the purpose of obtaining or retaining municipal advisory business;
(ii) Payments from third parties to the municipal advisor;
(iii) Payments from third parties to enlist the municipal advisor's recommendation of their services to the municipal entity;
(iv) whether the municipal advisor or an affiliate of the municipal advisor is acting as a principal in matters concerning the municipal advisory engagement; and
(v) form of compensation.

For each of the first four of these examples, the MSRB cites in footnotes various cases in which firms – virtually all of which were multi-service financial institutions – were found to have acted inappropriately and in violation of applicable federal or state law. The only category for which the MSRB did ***not*** cite an example of misconduct was with regard to the form of compensation. That is not surprising, as NAIPFA is aware of no instance in which an independent financial advisor was found to have acted to the detriment of an issuer in order to maximize its compensation under any standard compensation arrangement.

The MSRB's position is that a material conflict exists in fact through virtually any compensation arrangement. This ignores the reality that the conflict ***only*** exists if the municipal advisor is violating its fiduciary duty. Indeed, the MSRB apparently believes that even the most basic forms of compensation, *e.g.*, being paid by the hour, pose a threat to issuers. The MSRB could have highlighted the issue, warned advisors to take care not to allow any compensation arrangement to influence their recommendations to municipal entity clients, and moved on. But that was apparently not sufficient. Instead, the MSRB proposes that advisors be required to disclose these conflicts to issuers. But advisors apparently can't be trusted to do that properly either, so the MSRB wrote the disclosure for them![2] It took the form of a document entitled *Disclosure of Conflicts of Interest With*

[2] Compare the MSRB's approach with to rules put forth by the American Bar Association ("ABA") that deal with the ethical conduct of lawyers, a group of individuals who, like municipal advisors, have fiduciary duties to their clients. Rule 1.5 of the ABA Model Rules of Professional Conduct specifically addresses fees. In particular, Rule 1.5 addresses (i) unreasonable or excessive fees and provides factors for determining reasonableness, (ii) an attorney's ability to limit the scope of his representation, and (iii) contingent fees. At no point in either the rule

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Various Forms of Compensation (referred to in the G-36 Notice and this comment letter as "Appendix A").[3]

Appendix A clearly and concisely states that every form of compensation paid by a municipal entity client to a municipal advisor creates a conflict of interest. Fixed fees, hourly fees, fees contingent on completion of a financing and fees based upon amount financed are all identified by the MSRB as problematic in their own way. It is functionally equivalent to saying "The Surgeon General has determined that using a financial advisor may be hazardous to your health." Thus, whether intended or not, the effect of providing the disclosure in the form "suggested" by the MSRB may well be to make issuers wary of financial advisors, when in fact their interests are most likely to be better served by retaining financial advisors.

The absurdity of the MSRB's approach is highlighted by – and its continued bias towards firms that underwrite bonds is evidenced by – the fact that those parties with whom the issuers deal that have real and actual (as opposed to potential) conflicts not only don't have an Appendix A of their own, but are for all intents and purposes absolved of even the need to disclose the conflicts they have. Burdensome disclosure duties are imposed upon municipal advisors who are accountable for the advice and services provided to municipal entities regarding the structure, terms, timing and other similar matters regarding the issuance of municipal securities. No similar disclosure requirements are placed on dealers serving as underwriters even though they are not accountable for the services they provide with regard to the structure, terms, timing and other similar matters regarding the issuance of municipal securities.

This is important to consider when viewed in conjunction with proposed Rule G-23, which proposes that underwriters are allowed to provide "advice" without having to comply with a fiduciary duty. The result is that an underwriter, who has an inherent conflict of interest by virtue of its role as purchaser and distributor of securities in an arm's length commercial transaction with a municipal entity, does not have to disclose that its compensation creates a conflict of interest. What is more, although municipal advisors are required to disclose matters, in writing, that do not in and of themselves create conflicts of interest, such as compensation, underwriters are not required to disclose anything in writing, even the inherent conflict of interest that exists when an underwriter

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itself or in the interpretive guidance is it required that an attorney disclose that his fee, even if contingent, may create a conflict of interest.

[3] NAIPFA appreciates that the MSRB is not directly mandating use of Appendix A, but it surely realizes – and we believe fully intends – that few firms would choose not to use it.

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provides advice to a municipal entity regarding the structure, terms, timing and similar matters with regard to the issuance of municipal securities.

NAIPFA believes that this double-standard is unacceptable. The MSRB's regulatory framework can be summarized as follows: If an individual **can** be held accountable for the services it provides regarding the structure, timing, terms and other similar matters regarding the issuance of municipal securities, the individual **must disclose**, in writing, certain matters that do **not** in and of themselves create conflicts of interest, such as the form of compensation. However, if the individual **cannot** be held accountable for the services it provides to municipal entities, the individual **may** have to make disclosures, such as those found in G-23, but these disclosures are **never** required to be in writing, even if the matter does create a material conflict of interest, such as where the underwriter is simultaneously serving as financial advisor on one transaction with an issuer and as underwriter on a different transaction with that same issuer.

Although such a regulatory framework may have been acceptable pre-Dodd-Frank, the MSRB's new mandate requires it to protect the interest of municipal entities. Therefore, the test for proposed Rule G-36, and others, is whether the rule adequately protects the interest of municipal entities. Proposed Rule G-36 as interpreted by the MSRB fails to meet this test and therefore the guidance must be amended.

The Rule, when viewed within the broader regulatory framework put forth since the enactment of Dodd-Frank, leads to the conclusion that municipal entities will be unaware as to who is protecting their interest. Based on the disclosure requirements of proposed Rule G-36 and proposed Rule G-23, will municipal entities understand that municipal advisors, who have to disclose conflicts of interest, in writing, act in their best interest, or will municipal officials believe that underwriters, who do not have to disclose anything in writing, are acting in their best interest? NAIPFA believes that the latter is more likely to occur. Rather than placing strong disclosure requirements on unaccountable underwriters, the MSRB has instead placed these requirements on municipal advisors. Doing so gives the impression that municipal advisors, not underwriters, possess the conflicts of interest. This is inconsistent with reality.

NAIPFA respectfully suggests that the G-36 Notice (and the MA Guidance) be amended to no longer require disclosures regarding "conflicts with various forms of compensation" and that Appendix A be eliminated in its entirety. Alternatively, if the MSRB determines that disclosures regarding compensation are required, NAIPFA strongly suggests that, because these disclosures are equally, if

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not more applicable to dealers serving as underwriters, similar disclosures should be required of them.[4]

At first blush, one might be tempted to argue that underwriters are not fiduciaries, and without the duty of loyalty there is no basis to compel underwriters to disclose their conflicts or their compensation. However, the MSRB in its MA Guidance imposes on municipal advisors the same duty to disclose compensation to obligated person clients under Rule G-17 as it does under G-36. It seems that fair dealing means one thing if you are a municipal advisor and something else entirely if you are an underwriter.

3. If Compensation Disclosure is Required, NAIPFA Suggests a Better Way to Do It

As noted above, NAIPFA asserts that the Appendix A requirement is unnecessary because the advisor's fiduciary duty will require that it not put its own financial interests before its client. Furthermore, the MSRB's requirement will confuse issuers because it addresses a problem that doesn't exist and inappropriately intrudes on the relationship between the advisor and its potential client. Leaving the wisdom of the requirement aside, the logistical issues raised by the disclosure proposal are themselves significant.

The MSRB would require that the disclosure be made

(i) In writing;
(ii) To officials of the municipal entity (or obligated person) with the authority to bind the municipal entity (or obligated person) by contract; and
(iii) receive written consent back;
(iv) before the municipal advisor may provide municipal advisory services.

The MSRB apparently assumes that all municipal advisory activity is undertaken only at such time as an issuer formally retains a municipal advisor to perform an agreed upon set of tasks. However, if the SEC's proposal on permanent registration is adopted, a variety of activities that typically occur prior to being retained would qualify as municipal advisory activities. Indeed, one could be deemed an advisor without ever being retained or compensated or ever having even discussed compensation.

For example, it may well be that any one of the following qualifies as municipal advisory activity:

- Meeting the executive director of a non-profit hospital at a conference and discussing with her how they plan to finance a new wing on the hospital;

[4] See NAIPFA's Comment Letter dated March 11, 2011 related to the Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities, submitted together with this Comment Letter.

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- Sending to an issuer official on an unsolicited basis a financing idea for a convention center the city is considering; or
- Responding to an RFP seeking a municipal advisor where the RFP identifies the project(s) to be financed and seeks ideas.

In which of these scenaria would it be remotely practical or even possible to have not only provided Appendix A but have received written consent to the "conflicts" back from the potential client? Obviously, the answer is none of them.

Perhaps the more appropriate way to think about this is that there can be no conflict between an advisor and its client relating to compensation before the advisor is retained for compensation. Indeed, some advisors may offer certain services absolutely free of charge and there can be no compensation-related conflict when there is no compensation. NAIPFA is prepared to accept that a fiduciary duty may attach to those services, but there is no possible benefit to be gained from - or protection afforded to an issuer by - providing Appendix A to the "client" in this circumstance.

NAIPFA also takes issue with the MSRB's overly restrictive definition of which individual(s) at the municipal entity or obligated person is required to receive and acknowledge the compensation disclosure. How is the advisor to know if the individual qualifies? What diligence is required to find out? What happens if it turns out the advisor gets it wrong?

NAIPFA believes a rational alternative to the disclosure requirement proposed by the MSRB would involve disclosure (i) of the conflicts that are actually applicable to a compensation methodology being proposed by a municipal advisor to a municipal entity client (ii) made at the time the compensation methodology is being proposed (iii) to the representative of the municipal entity designated by the municipal entity as the primary contact for the engagement.

This regime would make disclosure more meaningful, because it would relate to what is actually being proposed, when it is being proposed and to whom it is being proposed. Issuers would be free to solicit ideas from advisors and advisors would be free to offer ideas to potential clients. Only at such time as the parties actually consider engagement, and the terms of that engagement are being discussed would the disclosures need to be made, and no disclosure would be made when there is no compensation. Additionally, advisors would be permitted to rely on the apparent authority of an issuer representative when making the disclosure, provided the advisor has no reason to believe the individual with whom it is dealing lacks the requisite authority. Finally, the advisor may presume that consent to the compensation arrangement is granted if it either (a) receives an executed contract (or similar document) or a verbal acknowledgment that the terms of a written engagement letter (or similar document) have been accepted; or (b) receives written or verbal acknowledgment that it has been selected following an RFP process in which the form of compensation was disclosed and the applicable disclosure provided.

4. *The MSRB Should Clarify What it Means By Excessive Compensation*

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The MSRB states that excessive compensation violates both the duty of loyalty under G-36 and G-17's requirement to deal fairly. What the MSRB does not do is provide any guidance as to how a municipal advisor is to determine at what point compensation becomes excessive. The MSRB should provide that guidance. NAIPFA suggests that the following (or similar) criteria or considerations would be appropriate in making a determination about the reasonableness of compensation:

a. the time and labor required, the novelty and difficulty of the issue involved, and the skill requisite to perform the municipal advisory services properly;
b. the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the municipal advisory; (i.e., if you take job A, does it limit your ability to obtain job B; if so, your fee can reflect that reality);
c. the fee customarily charged in the locality for similar municipal advisory services;
d. the amount involved and the results obtained;
e. the time limitations imposed by the client or by the circumstances;
f. the nature and length of the professional relationship with the client;
g. the experience, reputation, and ability of the municipal advisor or municipal advisors performing the services; and
h. whether the fee is fixed or contingent.

5. *NAIPFA Objects to the Presumption that Only Services Specifically Disclaimed Are Outside the Scope of Services Subject to a Fiduciary Duty*

The MSRB recognizes that not all advisory engagements are alike and that some are limited by the express wishes of the client. Nevertheless, the MSRB implies that only those services that an advisor specifically states in writing it is not performing or for which it is not responsible are exempt from the fiduciary duty. As noted above, there are any number of situations in which a municipal advisor may be providing municipal advisory services either without compensation or prior to being formally engaged. Indeed, the potential client may never actually engage this advisor or any advisor with regard to the matter or project that was the subject of discussion between the potential client and the advisor. In such instances, it would be obviously unreasonable for the advisor to be deemed to have had a fiduciary duty that extended beyond the limited boundaries of what the parties discussed. Accordingly, the MSRB should withdraw or clarify its statement that, unless the duty has been "expressly disclaimed . . . a municipal advisor has a duty to investigate and advise the municipal entity of alternatives to the proposed financing structure or product that are then reasonably feasible based on the issuer's financial circumstances and market conditions at the time, if those alternatives would better serve the interests of the municipal entity."

NAIPFA believes the presumption should be reversed, particularly in cases in which there is a writing that describes the services being performed. The issuer has no reason to assume that services will be performed by an advisor that are not specified in a writing when that document purports to set forth

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the services being requested or provided. At the very least, a municipal advisor should be permitted to make a blanket statement such as "only those services specifically set forth herein are within the scope of this engagement" without having to enumerate – even if it could identify - every other possible service that it is not performing.

6. *The MSRB Should Clarify the Various Due Diligence Requirements Set Forth Under Both the Fiduciary Duty of Care and the Fair Dealing Rule*

The MSRB states in various places and using different language several requirements that can be described as due diligence obligations. One, noted above, is the fiduciary "duty to investigate and advise the municipal entity of alternatives to the proposed financing structure or product that are then reasonably feasible based on the issuer's financial circumstances and market conditions at the time, if those alternatives would better serve the interests of the municipal entity." Another is the fiduciary duty to "make a reasonable inquiry as to the facts that are relevant to a municipal entity's determination of whether to proceed with a course of action." In a section titled *Advisor Not a Guarantor*, the MSRB states that the fiduciary duty of care "requires only that the advisor act competently and provide advice to the municipal entity after making reasonable inquiry into the representations of the municipal entity's counterparties, as well as then reasonably feasible alternatives to the financings or products proposed that might better serve the interests of its municipal client." And the fair dealing rules require that an advisor recommend a transaction or product to an obligated person client only if it has "concluded, in its professional judgment, that the transaction or product is appropriate for the client, given its financial circumstances, objectives, and market conditions, and must advise the client of material risks and characteristics of the structure or product."

NAIPFA believes these different formulations are unnecessarily obtuse. If, as we believe, the purpose of the guidance is to establish the general principle that an advisor must have a reasonable basis for recommending a course of action, whether because it has a fiduciary duty or under the rubric of fair dealing, the MSRB should simply say so. Similarly, if the MSRB believes that an advisor can only have a reasonable basis if it has obtained certain essential facts about the client and its objectives, it should say that, too. And, finally, if the MSRB believes that any recommendation of a course of action should include a description of the risks of that course of action, it should be equally clear about that.

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CONCLUSION:

NAIPFA believes the MSRB's entire approach to its new mission to protect issuers is wrong as a matter of law. It simply does not further and in some cases runs counter to the express provisions of the Dodd-Frank Act. The approach is also misguided because it focuses less on real-world problems than on those that the MSRB imagines issuers care about. By seeking to impose significant disclosure and other requirements on independent advisors while conspicuously exempting underwriters from similar requirements, the MSRB creates the patently false impression that independent advisors pose a greater threat to an issuer's health than underwriters do. For the reasons stated above and in NAIPFA's prior comment letters, we respectfully request that the MSRB re-think these and other rule proposals and develop a comprehensive regime that fulfills its mission.

Sincerely,

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

cc: The Honorable Mary L. Schapiro, Commissioner
The Honorable Kathleen L. Casey, Commissioner
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Troy A. Paredes, Commissioner
Michael Coe, Counsel to Commissioner Aguilar
Martha Haines, Assistant Director and Chief, Office of Municipal Securities
Lynnette Hotchkiss, Executive Director, Municipal Securities Rulemaking Board

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March 21, 2011

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File Number SR-MSRB-2011-03

Dear Ms. Murphy:

The National Association of Independent Public Finance Advisors ("NAIPFA") appreciates this opportunity to provide comments to the Securities and Exchange Commission ("SEC") on proposed Rule G-23 and the accompanying interpretive notice submitted for consideration by the Municipal Securities Rulemaking Board ("MSRB").

NAIPFA, founded 21 years ago, is a professional organization of independent public finance advisory firms that provide public finance advice to municipal and non-profit entities. NAIPFA comprises thirty two member firms serving all fifty states from locations in twenty–six states. Independent public finance advisors offer a wide variety of consulting services to issuers and obligated persons. In 2009, NAIPFA members represented clients on over 2,800 separate bond issues with approximately $75 billion in proceeds.

Preliminary Statement

Since its adoption in 1977, MSRB Rule G-23 has been the subject of much discussion within the industry and in the financial press. The Rule has been modified - or ***not*** modified - several times. The concerns raised primarily related to the conflicts of interest inherent in permitting broker-dealers to serve as financial advisors then later resign to become the underwriter of the issue they helped structure. It is problematic because the firm in its role as advisor sets out to and does, in fact, gain the trust and confidence of its client. When a broker-dealer advisor suddenly resigns and shifts its role to that of an underwriter, the firm's interests are then at odds with its former municipal entity client (the issuer), because it is negotiating to purchase the bonds with a goal to resell them to investors for a profit.

On several occasions, NAIPFA has asked the MSRB to consider whether it was appropriate for a broker-dealer to provide the kind of advice that financial advisors typically provide, *i.e.*, advice with regard to the structure, timing and similar matters related to a financing, and then switch roles.[1] Among the concerns raised were that broker-dealer firms were developing relationships of trust and confidence through their actions and statements, but disclaimed legal responsibility when their municipal clients sought under local law to hold them to the fiduciary standards that others who provided similar advice were held.

In 2010, having seen that numerous municipalities suffered significant losses in connection with sometimes extremely complex financial transactions promoted by underwriters or underwriters acting as financial advisors, Congress determined that some issuers were not sophisticated enough to make

[1] See, *e.g.*, letters from NAIPFA dated October 28, 2005 and May 18, 2007, copies of which are attached.

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informed financial decisions or were taken advantage of by unscrupulous market participants. Through passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), and particularly Section 975 thereof, Congress created a new class of regulated entity – the municipal advisor – and directed the SEC and the MSRB, among others, to adopt rules to protect issuers and obligated persons. Understanding Congressional concerns and SEC initiatives, the MSRB in August 2010 proposed for comment changes to its Rule G-23. It received 73 comments, including a letter from NAIPFA supporting changes to the Rule.[2] In its current filing with the SEC, the MSRB proposes to modify Rule G-23 (the "Proposed Rule") and also to issue interpretive guidance (the "Guidance").

NAIPFA commends the MSRB for revisiting this issue. The proposed Rule takes some steps in eliminating conduct that NAIPFA and others have long recognized puts issuers and the public at risk. NAIPFA supports those changes that prohibit firms from acting as advisors and then switching roles. NAIPFA agrees with the following MSRB responses set forth in SEC Exchange Act Release No. 34-63946:

- The MSRB does not believe the proposed rule change would impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act;
- The MSRB believes current Rule G-23 permits inherent conflicts of interest, which are not cured by disclosure and waiver provisions of the Rule;
- The MSRB believes that the potential negative impact on fees and market accessibility for small and/or infrequent issuers would be minimal compared to the protections that will be afforded to such issuer;
- The MSRB does not believe that exceptions should be provided for smaller offerings;
- The MSRB does not believe the use of electronic bidding platforms mitigates the conflict of interest posed by a dealer financial advisor's switching to an underwriter role;
- The MSRB does not believe requiring advance notice of competitive sale would provide adequate protections against conflicts of interest;
- The MSRB agrees that the role and interests of the dealer financial advisor are "significantly different" from the role and interests of a dealer acting as the underwriter for the same governmental unit; and
- The MSRB agrees that the issuer does not fully understand the implications of the ending of the financial advisory relationship with the issuer (which ends the dealer's fiduciary obligation to the issuer) and the arm's length relationship that is necessary due to the dealer's financial advisor becoming the underwriter of the transaction.

Unfortunately, notwithstanding clear direction from Congress, the MSRB failed to recognize the important distinction between providing advice and acting as an underwriter. Accordingly, NAIPFA objects to the Proposed Rule and Guidance to the extent it exempts from the definition of a municipal advisor all underwriters that render "advice to an issuer, including advice with respect to the structure, timing, terms and other similar matters concerning the issuance of municipal securities." Underwriters would still be able to provide the same advice as a municipal advisor without a fiduciary duty to the issuer.

As NAIPFA understands the purpose of Dodd-Frank, advice is only to be rendered to issuers by licensed municipal advisor professionals, registered with the Commission, who have appropriate expertise. Congress intended that those providing advice with respect to the *issuance of municipal securities,*

[2] See Letter dated September 30, 2010, from Steven F. Apfelbacher (the "2010 Comment Letter"), a copy of which is attached.

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including advice with respect to the structure, timing, terms, and other similar matters concerning such issues would be deemed fiduciaries with a duty to act in the best interests of the issuer client. This MSRB proposal is at variance with the purpose of the Act because the one party with potentially the most significant conflicts of interest - the underwriter – would still be permitted to give issuers advice with respect to the *issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such issues* without a corresponding fiduciary duty.

NAIPFA therefore reiterates its request set forth in the 2010 Comment Letter that the final sentence of section (b) of Rule G-23 be amended to read:

> *Notwithstanding the foregoing, for purposes of this rule, a financial advisory relationship shall not be deemed to exist when, in the course of acting as an underwriter, a broker, dealer or municipal securities dealer provides information to an issuer relating to the sale of the securities to investors such as transactional structures, the underwriter's capabilities to sell various securities, how particular terms of a security structure may affect rates and yields, and matters incidental to the underwriting of a new issue of municipal securities.*

In addition, the Guidance should make clear that the phrase "in the course of acting as an underwriter" means that the firm has either been retained by an issuer to purchase and distribute its securities, or is responding to requests for proposals or requests for qualifications from a potential issuer seeking an underwriter and has requested that such information be provided by the responding firms. In all other instances, providing "advice with respect to the structure, timing, terms and other similar matters concerning the issuance of municipal securities" would constitute financial advisory activities for purposes of Rule G-23.

NAIPFA's suggested changes to proposed Rule G-23 are consistent with the law, and consistent with the views we expressed in our comment letter to the SEC relating to municipal advisor registration.[3] Should the SEC disagree with our views and construe the underwriter's exception under §15B(e)(4)(C) of the Exchange Act to permit underwriters to provide advice to municipal entities regarding the issuance of municipal securities without either having to register or act with a fiduciary duty, NAIPFA urges the SEC to compel the MSRB to include in either Rule G-23 or the Guidance:

- Underwriters must decide prior to communicating with an issuer whether the underwriter will offer its services as an advisor or underwriter. The underwriter should not be allowed to rebut the role of municipal advisor "if the dealer clearly identifies itself as an underwriter from the earliest stages of the relationship with the issuer with respect to that issue."

- Brokers, dealers and municipal securities dealers ("underwriters") providing advice to issuers must disclose in no uncertain terms – in a document similar to Appendix A proposed within the MSRB's Proposed Rule G-36 and Rule G-17 Guidance to Municipal Advisors - that they:

[3] See letter dated February 22, 2011 from Colette Irwin-Knott, a copy of which is attached.

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- Are not acting as advisors but as underwriters;
- Are not fiduciaries to the issuer but rather counterparties dealing at arm's length;
- Have conflicts with issuers because they represent the interests of the investors or other counterparties which may result in benefits to other transaction participants at direct cost to the issuer;
- Seek to maximize their profitability and such profitability may or may not be transparent or disclosed to the issuer; and
- Have no continuing obligation to the issuer following the closing of transactions.

NAIPFA further urges that the rule changes be effective immediately upon SEC approval and not in six months as proposed. Additionally, underwriters should be prohibited from serving as municipal advisor and underwriter for an issuer at the same time. Last, changes to Rule G-23 should be considered only after the market has absorbed all regulatory changes and regulators can review objective evidence to assess any impact due only to Rule G-23.

Discussion

1. **NAIPFA objects to the MSRB's expansive view of the advisory activities in which dealers can engage without being deemed financial advisors.**

Congress was very clear about the activities that it considers to be advisory in nature. These changes are to be made in the municipal market and not within other markets. A municipal advisor is a person

> *who provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues; or undertakes a solicitation of a municipal entity.*

Congress also drafted its legislation to specifically include certain market participants and exempt others, at least when they are acting in certain defined and limited capacities. Thus, in the Exchange Act, Congress states that a "broker, dealer or municipal securities dealer serving as an underwriter (as defined in section 2(a)(11) of the Securities Act of 1933) is not a municipal advisor. Section 2(a)(11) provides that an "underwriter" is

> *any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission. As used in this paragraph the term "issuer" shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.*

In short, Congress has clearly defined municipal advisory activities to mean advising issuers and borrowers with respect the structure, timing, terms and similar matters concerning a municipal bond issue. At the same time, it has defined underwriting activities to mean purchasing and distributing securities.

The distinction between advisory activities and underwriting activities has always had legal significance. Advisors sit on the same side of the table with the issuer, with all the legal responsibilities that go along with being an advisor, while the underwriter sits at arm's length on the other side of the table, negotiating

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the terms pursuant to which it will purchase the bonds with the end goal of making a profit when they are resold.[4] This distinction is further confirmed within the standard form of Bond Purchase Agreement developed by the industry. The purchase agreement makes it clear the underwriter is in an arm's length relationship with the underwriter.

The MSRB acknowledges the provisions in the law set forth above, but tries to draw lines that are inappropriate in concept and likely unworkable in practice. In the Guidance, the MSRB states that "a dealer that provides advice to an issuer with respect to the issuance of municipal securities will be presumed to be a financial advisor with respect to that issue." However, it goes on to say that the

> *presumption may be rebutted if the dealer clearly identifies itself as the underwriter from the earliest stages of its relationship with the issuer with respect to that issue. Thus, a dealer providing advice to the issuer with respect to the issuance of municipal securities (including the structure, timing and terms of the issue . . .) generally will not be viewed as a financial advisor for purposes of Rule G-23, if such advice is rendered in its capacity as underwriter for such issue. Thus, a dealer providing advice to an issuer with respect to the issuance of municipal securities (including the structure, timing and terms of the issue and other similar matters, such as the investment of bond proceeds, a municipal derivative, or other matters integrally related to the issue) generally will not be viewed as a financial advisor for purposes of Rule G-23, if such advice is rendered in its capacity as underwriter for such issue. Nevertheless, a dealer's subsequent course of conduct (e.g., representing to the issuer that it is acting only in the issuer's best interests, rather than as an arm's length counterparty, with respect to that issue) may cause the dealer to be considered a financial advisor with respect to such issue. In that case, the dealer will be precluded from underwriting that issue by Rule G-23(d).*

As a result of the way business is conducted today, the Guidance is unworkable in most situations. However, one plausible scenario in which the Guidance can work is a scenario in which the issuer has retained a financial advisor to represent its interests in connection with a contemplated financing. The advisor recommends and the issuer agrees that the best course of action is to pursue a negotiated financing. The issuer (with the assistance of the advisor) then conducts an RFP/RFQ process for the purpose of selecting the underwriter. The RFP solicits, among other things, ideas about the "structure, timing and other terms of the issue" being proposed. NAIPFA posits that providing information in that context should not cause the potential underwriter – whether it is ultimately selected or not – to be an advisor. Nor, after it is selected, should the underwriter be deemed an advisor for providing ideas about the "structure, timing and other terms of the issue." In this scenario, the issuer can readily distinguish between the roles of the advisor and the underwriter because it has engaged one of each. Where the Guidance becomes problematic is in the much more frequent scenario, the one where a potential issuer does not yet have – and may never have – an independent advisor working with it.

Issuers are routinely contacted by independent financial advisors, by firms that act only as underwriters and by firms that provide both advisory and underwriting services. Sometimes, but not always, the issuers have a prior relationship with a firm that has or is soliciting them for the purpose of obtaining their business. These contacts are often in writing but are just as likely to be oral. Topics addressed are likely to include the issuer's current financial situation and opportunities that may exist to accomplish one or more of what the firm knows or supposes to be the objectives of the issuer. The firm's communication

[4] For detailed discussions and analysis on this point, see, *e.g.,* submissions to the SEC relating to Exchange Act Release No. 34-63576 (File No. S7-45-10) from Robert Doty and Nathan R. Howard.

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with the issuer may well suggest that a particular transaction, described generally or in detail, might be advantageous to the issuer. In addition, the firm may offer to discuss the financial matters of a particular transaction more fully at a later time. Assuming that the communications described above – or an ensuing discussion – contains "advice with respect to the structure, timing, terms or other similar matters concerning the issuance of municipal securities," then, based on the Guidance as proposed, if the firm that contacted the issuer was a dealer, that firm would be presumed at that time to be a financial advisor unless it expressly identified that it was acting as an underwriter. However, the firm could *not* be acting as an underwriter at that time, because no such role would then exist.[5] **The only possible role that could exist at such a preliminary stage is that of advisor.**

In the normal course, the issuer may have discussions with several firms, some of which may be independent financial advisors who only provide financial advice and others may be dealers who sometimes serve as financial advisors and sometimes as underwriters. At the time these conversations are taking place, the issuer may not have even decided whether to pursue a transaction, let alone made any of the decisions about whether it will pursue a private loan or similar financing, a private placement or a public offering of bonds and, if the latter, whether the offering will be a competitive or negotiated bond sale. How is the dealer firm to indicate what role it is playing at such a preliminary stage? More importantly, what is the issuer supposed to think? The opportunity for confusion is great, as is the possibility that the issuer might decide to pursue a transaction using the dealer firm and never retain a financial advisor to provide the independent advice that it may have believed it already received.[6]

Congress intended to insulate municipalities from obtaining advice from individuals whose interests are contrary to those of the issuer. Therefore, NAIPFA respectfully suggests that this intent can only be realized if the exemption for underwriters under §15B(e)(4)(C) of the Exchange Act applies only when the underwriter has made clear what role it is playing in the transaction and thereafter does not influence the decision making process by providing advice or by providing information in a manner that could be perceived as advice. Notably, however, proposed Rule G-23 fails to accomplish this intent. Accordingly, we suggest, as we did in September 2010, that the final sentence of section (b) of Rule G-23 be amended to read:

> *Notwithstanding the foregoing, for purposes of this rule, a financial advisory relationship shall not be deemed to exist when, in the course of acting as an underwriter, a broker, dealer or municipal securities dealer provides information to an issuer relating to the sale of the securities to investors such as transactional structures, the underwriter's capabilities to sell various securities, how particular terms of a security structure may affect rates and yields, and matters incidental to the underwriting of a new issue of municipal securities.*

Proposed Rule G-23 only perpetuates the *status quo.* This will frustrate Congress' intent as it will leave the most vulnerable issuers open to the same abuses Congress sought to prevent with the passage of Dodd-Frank. What is more, when proposed Rule G-23 is taken together with proposed rules G-17 and G-

[5] *See* Letter from Nathan R. Howard, Esq., Municipal Advisor, WM Financial Strategies, to the Securities and Exchange Commission, dated February 22, 2011.

[6] As the MSRB itself states in its submission to the SEC supporting the proposed Rule changes, "[s]mall and infrequent issuers are, in many cases, unable to appreciate the nature of the conflict they are being asked to waive by the very dealer financial advisor that will benefit from the waiver."

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36, the potential for underwriters to wield dangerous levels of influence over municipal entities becomes clear, a result unequivocally contrary to the purpose of Dodd-Frank. As NAIPFA reads proposed Rule G-36, municipal advisors would have duties of loyalty and care to their municipal entity clients, which would include requirements that they take steps to learn the essential facts about the client's financial circumstances and objectives, only undertake assignments which they have the expertise and resources to perform, agree on the services to be performed and the compensation to be paid, disclose all conflicts, including any applicable to their compensation arrangement, and provide advice about all the feasible financing options then reasonably available. At all times the advisor must act in the best interests of the client without regard to its own financial and other interests.

Conversely, underwriters will not be bound by the dictates of proposed Rule G-36, and will be bound instead by the limited duties imposed by Rule G-17. Under proposed Rule G-17, underwriters would merely have a duty to deal fairly with the issuer, which the MSRB states is akin to a 10b-5 duty. In other words, an underwriter may not misrepresent the facts but its obligations do not include any affirmative duty to inquire into the financial circumstances and objectives of the issuer, to disclose the risks associated with a transaction it recommends or even to have any basis – reasonable or otherwise – for any transaction it recommends.[7]

Given the very limited duties the MSRB believes underwriters owe to municipal issuers, NAIPFA would argue that it not only contravenes Congressional intent but is affirmatively dangerous to extend to firms acting as underwriter the right to provide advice to issuers. Instead, as NAIPFA has stated on numerous occasions, an issuer should have the benefit of advice provided by a regulated municipal advisor whose interests are, and always will be, to do what is best for the client.

2. **NAIPFA objects to the notion of a rebuttable presumption when dealers provide advice but, if the presumption is rebuttable, dealers should be required to make affirmative disclosures of the conflicts inherent in their role as underwriter.**

For the reasons set forth above, NAIPFA asserts that the exemption from the definition of financial advisor in Rule G-23 is contrary to Dodd-Frank. However, should the SEC adopt the expansive view of what constitutes "acting as an underwriter" advanced by the MSRB, we believe that underwriters acting as financial advisors should be required to decide which role they will play with the issuer before they talk with the issuer and affirmatively disclose the conflicts inherent in their underwriting role to the issuer if that is the role they decide to purse. The MSRB highlights the conflict at the heart of the issue:

> *While underwriters have a duty of fair dealing to issuers under Rule G-17, they also have a duty to investors, whose interests are generally adverse to those of issuers.*

The MSRB also recognizes that the opportunity for confusion on the part of those issuers dealing with firms that provide a variety of services when it stated "that a dealer may not avail itself of the underwriter exception unless it maintains an arm's length relationship with the issuer." Nevertheless, the only affirmative requirement that the MSRB proposes to impose on a dealer providing advice to an issuer regarding matters related to the issuance of municipal securities is that the dealer "clearly identif[y] itself as an underwriter from the earliest stages of its relationship with the issuer with respect to that issue."

NAIPFA notes in this context the MSRB's proposals related to Rules G-36 and G-17. In particular, we note the extensive affirmative disclosure obligations the MSRB would seek to impose on municipal

[7] Underwriters have somewhat greater disclosure obligations when the transaction they recommend is "complex."

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advisors, and the lack of similar disclosures required of dealers. NAIPFA asserts that dealers providing advice should be required to do more than merely state they are acting as an underwriter to avoid being deemed a financial advisor for purposes of Rule G-23 (and otherwise). Instead, they should be required to state– in a document similar to Appendix A proposed within the MSRB's Proposed Rule G-36 and Rule G-17 Guidance to Municipal Advisors - that they:

- Are not acting as advisors but as underwriters;
- Are not fiduciaries to the issuer but rather counterparties dealing at arm's length;
- Have conflicts with issuers because they represent the interests of the investors or other counter parties which may result in benefits to other transaction participants at direct cost to the issuer;
- Total revenues and profitability may not be transparent or disclosed to the issuer; and
- Have no continuing obligation to the issuer following the closing of transactions.

NAIPFA calls on the SEC to also modify G-23 in a way that requires the underwriter acting as a financial advisor to decide before the underwriter approaches the issuer that the underwriter is presenting its services as an advisor or underwriter. This would avoid confusion on the part of the issuers as to the intentions of the underwriters acting as an advisor. Further similar conflict disclosure to the disclosure proposed for municipal advisors should be required by the underwriter if this is the role they have decided to pursue.

In addition, NAIPFA has seen situations where the underwriter acting as a financial advisor has resigned to purchase the debt issue but its financial advisor contract with the issuer remains in effect. The underwriter would then revert back to its role as financial advisor once the bonds were closed. This contract maneuver does not allow for another firm to assume the role of the financial advisor during the transaction or an opportunity to compete for the financial advisor role. Any regulatory actions should require that any contract the underwriter acting as an advisor had with an issuer be terminated when the dealer firm is hired or seeks to be hired as an underwriter to the issuer, swap counterparty or in any other role that is inconsistent with the role of a fiduciary.

3. NAIPFA objects to the MSRB's proposal that the proposed changes to Rule G-23 be effective for new issues awarded six months following approval of the Rule by the SEC.

The MSRB proposes that "the proposed rule change be made effective for new issues for which the Time of Formal Award . . . occurs more than six (6) months after the SEC approval." The stated reason for this effective date is "to allow issuers of municipal securities time to finalize any outstanding transactions that might be affected by the proposed rule change." NAIPFA believes – as apparently does the MSRB – that the substantive changes to Rule G-23 relating to role-switching are mandated by the imposition of a federal fiduciary duty and accordingly, that dealers acting in the role of advisor breach their fiduciary duty to an issuer when they switch roles to become a financial advisor. Because they had such a fiduciary duty under federal law effective October 1, 2010, NAIPFA asserts that any role-switching that occurred after that date was a violation of the Exchange Act.

Even assuming that issuers and underwriters were waiting for guidance on how the MSRB viewed Rule G-23 in light of Dodd-Frank, they were on notice in August 2010 when the MSRB proposed for comment the very changes it has now formally proposed to the SEC for adoption. The changes should be effective immediately upon approval by the SEC.

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The MSRB believes that the proposed rule would principally affect dealer financial advisors that are not small municipal advisors. Applying the rule effective on adoption would have provided sufficient time for the underwriter acting as an advisor to determine its appropriate role with an issuer. It would also provide immediate clarity to the issuer who is the party that is to benefit most from Dodd-Frank.

4. NAIPFA believes an underwriter should be prohibited from serving as a municipal advisor and underwriter for an issuer at the same time.

Within the MSRB filing, the MSRB agrees that the role and interests of the dealer financial advisor are "significantly different" from the role and interests of a dealer acting as the underwriter for the same governmental unit. Yet upon review of the comment letters, the MSRB has determined:

- Not to impose a cooling off period between the time a dealer completes a financial advisory engagement with an issuer and the time the dealer may serve as underwriter for a different issue by the same issuer. Rule G-23 is to be applied on an "issue by issue basis" so that the dealer financial advisor could serve as advisor on one issue and then serve as the underwriter on another issue for the same client even if the two issues are in the market at the same time; and
- It is appropriate that there be a one year cooling off period during which a dealer financial advisor could not serve as remarketing agent for the same issue of municipal securities. The MSRB goes on to state that a one year timeframe would more than adequately address any potential or actual conflicts of interest.

NAIPFA does not understand how there can be a conflict between the advisor/underwriter roles and a need for a cooling off period from the role as dealer financial advisor and yet the modified Rule G-23 change would allow for the underwriter acting as an advisor to undertake both activities at the same time with the same issuer. We all agree there is a conflict between the advisor/underwriter roles. Proposed Rule G-23 should be modified in a way that would force the underwriter acting as an advisor to decide which role they will play for the issuer and not be able to play both roles at the same time. NAIPFA further believes that if the one year cooling off period for remarketing conflicts is appropriate, there should be a one year cooling off period from the time an advisor underwriter terminates its role as municipal advisor and the advisor underwriter would be allowed to negotiate an issue with the issuer, act as swap counterparty or serve in any other role that is inconsistent with the role of a fiduciary. This modification would ensure that Rule G-23 would be fair and consistent in its application.

5. NAIPFA believes future changes to Rule G-23 should be considered only after the market has absorbed all regulatory changes and regulators can definitively assess any impact due only to Rule G-23.

Because the industry is having to react to and incorporate so many changes, NAIPFA respectfully requests that the SEC and MSRB not revisit Rule G-23 changes until sufficient time has elapsed to truly assess whether future changes will have the effect intended. The regulatory changes being discussed are significant and will likely change the current business models of advisors and underwriters. After the final rules of regulation have been established, there will be a period of time for the advisor and underwriters to adjust to the changes. Only when the market has adjusted to these significant changes and objective evidence has been gathered will regulators be able to assess the real impact of G-23.

Summary

We understand the pressure there is to adopt rules that meet the intent of Dodd-Frank. The fact is that Congress has determined to accept that, within the municipal market, there are municipal advisors and

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broker-dealers that serve as both municipal advisors and underwriters. In a less complicated scenario, advisors advise issuers and underwriters buy issuer bonds. This is a part of the conflict Congress intended to correct with Dodd-Frank. The MSRB agrees that the role and interests of the broker-dealer financial advisor are "significantly different" from the role and interests of a broker-dealer acting as the underwriter for the same governmental unit; yet the proposed Rule G-23 will allow broker-dealers acting as advisors to continue business as usual. NAIPFA's concern is that broker-dealers would be allowed to provide the same advice as municipal advisors without municipal advisor obligations. Broker-dealers could still be engaged by an issuer and then decide if they want to be the advisor or underwriter. Broker-dealers could work as the advisor and underwriter on different issues at the same time. It is clear that broker-dealers who act as advisors want to continue their lucrative business model. This business model of the past, however, must change if the full intent of Dodd-Frank is executed into regulation.

NAIPFA believes broker-dealers should not be allowed to provide unlimited advice without being an advisor with fiduciary duty to the issuer. As a result NAIPFA believes section (b) of Rule G-23 must be amended to provide guidance on the type of advice an underwriter can provide. Should the SEC believe, however, that underwriters have a broader exemption to provide advice, underwriters must be required to decide before they approach an issuer whether they will present themselves to the issuer as a municipal advisor or an underwriter. NAIPFA believes broker-dealers should be required to decide if they are in the advisor business or underwriting business. The broker-dealer should be able to do both but each role should follow the appropriate rules and regulations. Broker-dealers acting as advisors should not be allowed to confuse issuers as to their true role. Additionally, appropriate conflict disclosure should also be required for either role when they talk with the issuer and the rule should be effective immediately.

NAIPFA once again expresses its appreciation for the opportunity to submit its views on the MSRB's proposed Rule G-23 and interpretive guidance. We would be pleased to discuss any issues or concerns raised in this letter with representatives of the SEC. If we can be of any assistance or answer any questions, please feel free to contact me.

Sincerely,

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

cc: The Honorable Mary L. Schapiro, Commissioner
The Honorable Kathleen L. Casey, Commissioner
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Troy A. Paredes, Commissioner
Michael Coe, Counsel to Commissioner Aguilar
Martha Haines, Assistant Director and Chief, Office of Municipal Securities
Lynette Hotchkiss, Executive Director, Municipal Securities Rulemaking Board

From: Ed Crouch
Sent: Monday, February 14, 2011 12:41 PM
To: Comment Letters
Subject: Rule G-17 and Rule G-36 Commentary...

Greetings—

Thank you for the opportunity to provide commentary to the development of Rules G-17 and G-36. As these rules are drafted, finalized and interpreted, it should be clearly stated how these two similar (but distinct) rules interact with one another, and are separately or together applied, in the instance where a municipal advisor's client is an obligated person and the municipal entity is a conduit to a financing. More specifically, I am imagining a circumstance where a non-profit organization engages a municipal advisor to assist it in examining all possible financing scenarios that may be available to the organization including the use of conventional financing and tax-exempt bond financing. In this instance, the municipal advisor's client could become an obligated person, defined under that Act, but in the event that the financing that is ultimately consummated is in the form of a conventional loan, is there a question of whether client would ever be an obligated person if it would ultimately have no relationship to a municipal entity? Clearly defining this grey area is critical for municipal advisors to understand which regulatory construct applies at any given point in time.

Also, a potential conflict could materialize in instances where an obligated person could benefit from a transaction or structure that is not in the interest of the municipal entity. In circumstances where the municipal advisor's client is not the municipal entity but rather an obligated person (or as described above, an entity considering using municipal bonds but perhaps outside the definition of an obligated person at a certain point in time) the municipal advisor may believe that not using the municipal entity is in the client's best interest for a variety of interests. For instance if outstanding municipal bonds could be refinanced with a conventional loan, the municipal entity would receive less (or no) fees and therefore be financially impaired to the benefit of the obligated person. Again, the municipal advisor, its client and the municipal entity should be clearly informed as to the fiduciary and fair dealing duties of the municipal advisor under rules G-17 and G-36.

As I review these rules now, such delineation in these circumstances does not appear clear.

I hope this input is useful as the rules are developed. Please contact me if you would like to discuss this e-mail or need clarification.

Regards,
Ed Crouch

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Public Financial Management

April 8, 2011

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

Re: MSRB Notices 2011-13 and 2011-14

Draft Interpretive Notice Applicable to Rule G-17 and
Draft Interpretive Notice to Proposed new Rule G-36

Dear Members:

The Municipal Securities Rulemaking Board ("Board") has requested comments on draft Interpretive Notice Applicable to Rules G-17 and new Rule G-36. Kindly treat this letter, two copies of which are submitted, as a response to each of MSRB Notice 2011-13 and Notice 2011-14.

I serve as General Counsel to Public Financial Management, Inc. ("PFM"), a municipal advisor registered with the Board. The following comments are submitted on behalf of PFM.

PFM has no comment with respect to the substance of Rule G-17 and proposed Rule G-36. PFM recommends, however, as to the final version of the Board's Interpretive Notice which will accompany Rule G-17 and that which will accompany the final version of Rule G-36, that the Board make clear that Rule G-36 applies fully to a broker dealer who engages in municipal advisory activities with a municipal entity exclusive of the purchase of municipal securities, as described in Section 2(a)(11) of the Securities Act. The Board's only reference to the duties of brokers acting as municipal advisors is the obscure comment in Notice 2011-14 that if the Commission revises its position stated in Release No. 34-63576, the Board would "reconsider the provisions of the notice concerning limitations on principal transactions."

PFM objects to the Board's interpretation of Rule G-17 and Rule G-36 to require a financial advisor to rehearse with its obligated person/client (and obtain the client's written waiver to) a litany of hypothetical, potential "conflicts of interest" alleged to be presented by nearly every form of compensation

employed in advisory engagements. That proposed requirement is insulting to both financial advisors and to municipal governments and seems to demean financial advisors as compared with the Board's treatment of underwriters (as we note below). If the Board truly believed that such alleged conflicts of interest were real, rather than speculative, the remedy would be to prohibit the compensation arrangement, rather than put a municipal government to the choice of consenting to something which the Board says is bad for it, or foregoing the financial advice which it desires to improve its negotiating position vis-à-vis the underwriters.

In substantially all of our financial advisory engagements, our client sets the rules for our compensation, without any room for negotiation. We accept that structure, and we perform our job professionally to satisfy our own high standards, which are mirrored in Rules G-17 and G-36. And in substantially all instances, we do not get paid for services relating to a bond offering unless the offering is sold. Prior to the publication of MSRB Notices 2011-13 and 2011-14, it would have been bizarre indeed for PFM to admonish an experienced municipal government financial officer, as the Board demands, to "be careful" because we may be motivated to "fail to do a thorough analysis of alternatives" or because we may urge the government to sell more bonds than it really needs.

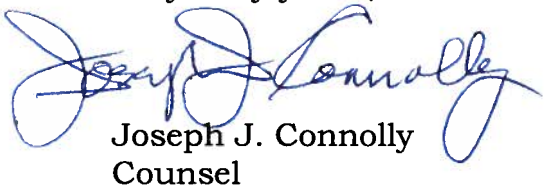
When compared with the treatment of government engagements of underwriters, on the other hand, the Board has shown some confidence in the skill of local financial officials. Municipal dealer underwriters have been subject to Rule G-17 for 35 years, but the Board has never required underwriters to admonish municipal issuers that "we will squeeze every nickel - - your nickels - - out of this deal that we possibly can." That's not a hypothetical, possible conflict of interest. That's a reality that every municipal issuer faces. However, the Board has seen no reason to be sure that the municipal government is on alert - - although, to be sure, we expect that the Board contemplates that the proposed admonitions of potential conflicts of interest will equally be required of brokers who engage in municipal advisory activities with government issuers.

Finally, the requirement that a financial advisor unroll a scroll of Board-conceived "conflicts of interest" to set the table for discussions with a municipal client seems unprecedented. To begin with, in most instances the municipal financial officials set the compensation rules even before a financial advisor is selected. Moreover, we know of nowhere else in the federal securities law in which regulation injects into a private transaction a formality which

necessarily rests on the sole presumption that one of the parties will violate the law. If the federal regulator, as it must, assumes that a financial advisor will observe the fiduciary duties which the law imposes, a regulation requiring an advisor to admonish its client as to situations in which the advisor allegedly might be tempted to subordinate the interests of the client cannot be said to be contemplated by statute. If, on the other hand, the federal regulator assumes that the financial advisor will violate the law, the admonitions to the client invented by the Board that every form of compensation that the client may select can be problematic can do nothing to protect the client from the advisor's invisible self-service - - the "waiver" of the client is, of course, useless. And the enforcement regulator is in exactly the same position as it would be if the admonitions and the waiver had never taken place.

For the foregoing reasons, PFM submits that the provisions of the subject Notices relating to alleged conflicts of interest in the method of computation of compensation of municipal advisors should be deleted.

Very truly yours,



Joseph J. Connolly
Counsel

JJC:plj

sifma
Invested in America

April 11, 2011

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

Re: MSRB Notice 2011-14 – Draft MSRB Rule G-36 (On Fiduciary Duty of Municipal Advisors) and Draft Interpretive Notice (Feb. 14, 2011)

MSRB Notice 2011-13 – Draft Interpretive Notice Concerning the Application of MSRB Rule G-17 to Municipal Advisors (Feb. 14, 2011)

Dear Mr. Smith:

The Securities Industry and Financial Markets Association ("**SIFMA**")[1] appreciates the opportunity to comment on the Municipal Securities Rulemaking Board's ("**MSRB**") draft Rule G-36 and related draft interpretive notice (the "**G-36 Proposal**") and the MSRB's draft interpretive notice concerning the application of Rule G-17 to municipal advisors (the "**G-17 Proposal**" and together with the G-36 Proposal, the "**Proposals**").

I. Executive Summary

SIFMA supports the MSRB's desire to provide guidance to municipal advisors as to the contours of the fiduciary duty owed by municipal advisors to their municipal entity clients (the G-36 Proposal) as prescribed by Section 975

[1] 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).

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("**Section 975**") of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "**Dodd-Frank Act**"),[2] as well as to the contours of the duty of fair dealing owed by municipal advisors to obligated person clients in the context of advisory engagements and owed to municipal entities solicited by municipal advisors on behalf of others (the G-17 Proposal). However, SIFMA believes that because the Securities and Exchange Commission ("**SEC**") has not yet adopted final rules that would define the scope of activities that trigger municipal advisor registration,[3] and therefore the universe of potential registrants, the Proposals interpreting how a fiduciary duty and duty of fair dealing apply to this as-of-yet undefined universe are premature. Indeed, in each of the Proposals, the MSRB itself acknowledged that the proposal did not take into account the Pending SEC Proposal and would, in fact, require revision if the Pending SEC Proposal was adopted. Of first importance, we believe the Proposals are unworkable if the Pending SEC Proposal were adopted. Therefore, SIFMA is unable to fully and meaningfully comment on the Proposals without knowing to whom, and during what activities, the duties would apply. Therefore SIFMA requests an opportunity to provide further comments once the SEC has completed its rulemaking defining the scope of activities subject to municipal advisor registration.

In addition to the question of ripeness of the Proposals in light of the Pending SEC Proposal, there are numerous interpretive positions contained in the Proposals that SIFMA believes the MSRB should reconsider. Specifically, with regard to the G-36 Proposal, it is critically important that the MSRB not adopt a ban on principal dealing by advisors to municipal entities; such a ban is not required to protect investors and is not consistent with Congressional intent or similar regulatory regimes. The imposition of such a ban would effectively limit many municipal entities' access to critical products and services, including the ability to purchase securities out of inventory. There is no justification for imposing a more restrictive fiduciary standard in the municipal advisor context.

The MSRB should also not view itself as regulating in a vacuum. Municipal advisors, as currently defined, will often be subject to regulation by other regulators that are also currently considering rules for fiduciary or fiduciary-like duties that would apply to providers of financial services in various contexts. These include the Commodity Futures Trading Commission ("**CFTC**") and SEC business conduct rules for swap dealers and security-based swap dealers, respectively, Department of Labor ("**DOL**") proposed fiduciary duties for

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[2] *See* Securities Exchange Act of 1934 ("**Exchange Act**") § 15B(b)(2)(L)(i).

[3] *See* Exchange Act Release No. 63576 (Dec. 20, 2010) (the "**Pending SEC Proposal**").

providers of investment advice to retirement plans, and the SEC's consideration of a fiduciary standard for broker-dealers providing personalized investment advice to retail customers. The MSRB should coordinate its interpretation with these other regulators to make sure that municipal advisors are not subject to inconsistent and irreconcilable standards.

In addition, many of the duties imposed by the Proposals are only applicable to one narrow form of municipal advisor—the traditional independent municipal advisor formally engaged by the municipal entity, which was largely unregulated prior to the adoption of Section 975. But Section 975 sweeps in other entities as municipal advisors to whom many of the proposed duties would not reasonably apply.

Further, many affirmative obligations that the Proposals would impose on municipal advisors appear to be merely paperwork exercises that add little value for a municipal entity or obligated person, but impose great costs on municipal advisors that will be passed along to their clients in higher fees. Municipal advisors and obligated persons should be permitted to contract for those services that they want, and not have other services mandated to them, presumably, at an additional cost.

Finally, the G-17 Proposal imposes many fiduciary duty-like obligations on a municipal advisor even though Section 975 did not specifically apply a fiduciary duty except when advising a municipal entity. The G-17 Proposal does so by interpreting a municipal advisor's duty of fair dealing with obligated persons. The G-17 Proposal's affirmative obligations go far beyond the common understanding of "fair dealing" and beyond what the MSRB has previously interpreted "fair dealing" to require of brokers, dealers and municipal securities dealers.

SIFMA respectfully requests the MSRB to reconsider the Proposals after SEC has adopted final rules governing the scope of municipal advisory activities and to reissue modified proposals after carefully considering the practical consequences the proposals would have on municipal advisors, municipal entities, and obligated persons.

II. G-36 Proposal – Duties to Municipal Entities

A. The MSRB Should Delay Its Rulemaking Until the SEC Determines the Definition of "Municipal Advisor."

The MSRB should delay its rulemaking and interpretive guidance regarding municipal advisors and their duties until the SEC adopts final rules defining what activities require registration as a "municipal advisor" and reopen

its comment period on the G-36 Proposal at that time. The Pending SEC Proposal would interpret the scope of activities covered by Section 975 very broadly, particularly in the definition of "investment strategies," that the MSRB itself believes is greater than Congress intended.[4] Indeed, the Chairman and staff of the SEC have each indicated that the scope of the Pending SEC Proposal is perhaps broader than even the SEC had intended.[5] For example, the Pending SEC Proposal contemplates that a broker-dealer transacting with a municipal entity as principal may be required to register as a municipal advisor.[6] At the same time, the G-36 Proposal would prohibit outright acting as principal with a municipal entity client as an unmanageable conflict of interest.

While SIFMA appreciates the MSRB's attempt to provide guidance as to the statutory fiduciary duty currently owed, it seems ultimately unproductive to propose rules and interpretations that would apply to an unknown group of persons engaged in unknown activities. The MSRB is effectively proposing rules and interpretations for a moving target. Such an approach is unfair to municipal advisors, including those who do not yet know they fall into that definition, as they cannot possibly consider and provide meaningful comments on the Proposals until they know to whom, and during what activities, the proposals will apply.

As the MSRB acknowledged in the Proposals, the Proposals would almost certainly need to be reconfigured depending on how the SEC ultimately defines municipal advisor activities. Because it is impossible at this time to predict what the SEC's final rules will look like, the MSRB should not, in the meantime, attempt to adopt rules and interpretations that in all likelihood will not reflect the regime being implemented. Once the SEC has issued its final rules, the MSRB should reopen the comment period on the G-36 Proposal so that SIFMA and

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[4] *See* Comment Letter from Michael G. Bartolotta, MSRB, to Elizabeth M. Murphy, SEC, (Feb. 22, 2011) at 4–6, *available at* http://sec.gov/comments/s7-45-10/s74510-586.pdf.

[5] In fact, the Chairman and staff of the SEC have each indicated that they are looking closely at the scope of their proposal, including potential regulatory overlap, in light of significant comments received. *See Budget Hearing – Securities and Exchange Commission: Hearing Before the House Committee on Appropriations, Subcommittee on Financial Services and General Government*, 112th Cong. (Mar. 15, 2011) (testimony of Mary Schapiro, Chairman, SEC) ("[W]e're looking very carefully at whether we may have cast the net too widely and taking the comments very, very seriously"); *see also Oversight of the Securities and Exchange Commission's Operations, Activities, Challenges and FY 2012 Budget Request: Hearing Before the House Committee on Financial Services, Subcommittee on Capital Markets, Insurance and Government-Sponsored Enterprises*, 112th Cong. (Mar. 10, 2011) (testimony of Robert Cook, Director, SEC Division of Trading and Markets).

[6] *See* Pending SEC Proposal at 53.

others may more completely consider the implications of the G-36 Proposal in light of what activities will require municipal advisor registration.

B. The Scope of the Fiduciary Duty Under the Proposal Should be Reconsidered.

1. Fiduciary Duty Should Apply to Municipal Entity Clients Only.

The MSRB should clarify that the fiduciary duty of a municipal advisor applies only to a municipal entity client in the context of providing municipal advisory services, and does not apply to the solicitation activities of a municipal advisor (which are covered by MSRB Rule G-17) or to activities with respect to obligated persons. This appears to have been the MSRB's intention,[7] although draft Rule G-36, as proposed, may not be consistent with that intent.

Under its terms, draft Rule G-36 applies to a municipal advisor's conduct of "municipal advisory activities." The term "municipal advisory activities" is not defined in draft Rule G-36, but is defined in MSRB Rule D-13, which states that "'[m]unicipal advisory activities' means the activities described in Section 15B(e)(4)(A)(i) and (ii) of the [Exchange Act]." This section of the Exchange Act describes both the "advisory" and "solicitation" prongs of the definition of "municipal advisor." As currently proposed, draft Rule G-36 might be read to include a municipal advisor's solicitation of a municipal entity on behalf of a third party within the scope of activities that are subject to the fiduciary duty. The MSRB should clarify draft Rule G-36 to clearly only apply to a municipal advisor's conduct in providing advice to its municipal entity client.

In addition, the MSRB should further clarify that the fiduciary duty under draft Rule G-36 does not apply when a municipal advisor solicits a municipal entity on its own behalf—rather than on behalf of a third party. A fiduciary duty should not apply to this solicitation, because at the time of the solicitation, the municipal entity is not yet the municipal advisor's client. Instead, Rule G-17's fair dealing standard should apply until such time as the municipal entity actually engages the municipal advisor to provide its services.

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[7] *See* MSRB Webinar, *MSRB Fiduciary Duty and Fair Dealing Requests for Comment* (Mar. 1, 2011) at slides 3, 6 and 16 (indicating the fiduciary duty applies where the client is a municipal entity and not where a municipal advisor solicits on behalf of third parties).

2. The MSRB Should Coordinate its Fiduciary Duty Standard with Other Regulators.

The MSRB should coordinate with the SEC, CFTC and the DOL regarding the various fiduciary duties and similar obligations that may be applicable to a person that is also a municipal advisor. For example, a municipal advisor may also (i) be an investment adviser already subject to a fiduciary duty, (ii) provide advice to a retirement fund subject to a DOL fiduciary standard, (iii) be a swap dealer or security-based swap dealer required to act in the "best interests" of a client when advising a "Special Entity" (which includes municipal entities),[8] or (iv) be a broker-dealer that may become subject to a fiduciary standard when providing personalized investment advice to retail customers. It would be unworkable for one entity to be subject to competing and different standards imposed by different regulatory schemes while engaged in the same or similar activities.

C. Activities Subject to the Fiduciary Duty; Duration of the Fiduciary Duty.

1. The MSRB Should Define "Engagement."

Many of the obligations imposed by the G-36 Proposal (*e.g.*, when the fiduciary duty will be deemed to apply, disclosure of payments a municipal advisor will receive, and prohibitions on acting as principal) are triggered by, or are related to the existence of an "engagement." However, the G-36 Proposal does not actually define the contours of when an engagement is deemed to exist, when it begins or when it is considered to have ended.

Because of the significant obligations and restrictions that are triggered by the existence of an engagement, municipal advisors must have clarity as to when they must conform their conduct to these requirements. To this end, the MSRB should clarify that a municipal advisory engagement is only deemed to exist once a written engagement letter is entered into between the municipal advisor and the municipal entity. This clarity would align Rule G-36 with Rule G-23, which requires that the commencement of a financial advisory relationship be evidenced in a writing. The engagement letter may itself specify the term of the engagement, and may set clear terminating events, so that all parties can agree and have certainty regarding whether an engagement is in effect. Absent a written

[8] *See* Commodity Exchange Act § 4s(h)(4)(B) (added by Section 731 of the Dodd-Frank Act); Exchange Act § 15F(h)(4)(B) (added by Section 764 of the Dodd-Frank Act).

engagement letter, the engagement should terminate based on the reasonable expectations of the parties.

If the MSRB declines to interpret the beginning and end of the engagement to be based on the parties' engagement letter, it should nonetheless clarify that the fiduciary duty does not continue in perpetuity, but ends once the particular transaction to which it related had concluded.

2. Fiduciary Duty Should Apply to Specific Engagements Only.

The MSRB should clarify that, absent documentation to the contrary, a person that is a municipal advisor has a fiduciary duty to its municipal entity client only with respect to individualized advisory services rendered pursuant to, or in the context of, a specific engagement, transaction or assignment, and not with respect to non-advisory, ancillary or unrelated activities or other dealings with the municipal entity, even if the same personnel are involved in the activities. For example, even if there is a limitation on principal activities by advisors to municipal entities (which we comment on in Section II.F.1 below), a municipal advisor and its affiliates should be permitted to continue to act as principal in relation to transactions with the municipal entity that are unrelated to the municipal advisor's advisory engagement. Similarly, a municipal advisor's fiduciary obligations should end upon the termination of the engagement, unless agreed otherwise.

3. Fiduciary Duty Should Not Apply to Any Affiliates of the Municipal Advisor.

The MSRB should confirm that, notwithstanding the definition of "person associated with a municipal advisor" under Section 975, which includes "any person directly or indirectly controlling, controlled by, or under common control with such municipal advisor,"[9] the fiduciary duty owed by a municipal advisor is not also owed by any of such advisor's affiliates, unless such an affiliate is itself otherwise engaged in municipal advisory activities and independently qualifies as a municipal advisor with respect to the municipal entity (in which case the affiliate will have an independent fiduciary duty to its municipal entity client).

SIFMA notes that under Rule D-11, "municipal advisor" is defined to include its "associated persons," as that term is defined in Section 3(a)(18) of the Exchange Act (which also includes entities under common control). For purposes

[9] Exchange Act § 15B(e)(7).

of its fair practice rules, the MSRB has nonetheless interpreted "associated persons" under Rule D-11 to *not* include persons who are associated "solely by reason of a control relationship."[10] This interpretation is sensible in the context of a municipal advisor's fiduciary duty to its municipal entity clients as well. While the individual natural persons associated with a municipal advisor should be subject to the fiduciary duty owed by the municipal advisor to its municipal entity clients, extending this duty to all entities under common control would be unworkable and burdensome, especially in the context of large financial institutions that have various entities which, while technically under common control, do not actually coordinate their activities.[11]

4. Activities Excepted from the Definition of "Municipal Advisor" Should not be Subject to a Fiduciary Duty.

The MSRB should clarify that the fiduciary duty under draft Rule G-36 does not extend to those activities that are excluded or exempted from the definition of "municipal advisor," whether by statute, rule or interpretation, (*e.g.*, the underwriter exception).

Draft Rule G-36 provides that a municipal advisor is subject to a fiduciary duty "[i]n the conduct of its municipal advisory activities on behalf of municipal entities." As noted above, Rule D-13 defines "municipal advisory activities" as those activities described in Section 15B(e)(4)(A)(i) and (ii) of the Exchange Act. However, these provisions do not refer to the statutory exceptions from being considered a municipal advisor under Section 15B(e)(4)(C) of the Exchange Act, for example, for underwriters, registered investment advisers or registered commodity trading advisors.

As proposed, draft Rule G-36 could therefore be read to apply a fiduciary duty to an underwriter whenever the underwriter engages in the activities described in Section 15B(e)(4)(A)(i) and (ii). Clearly, by exempting certain activities from municipal advisor registration, Congress also intended the persons engaging in those activities to be exempted from being subject to the duties specific to municipal advisors, including the fiduciary duty.

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[10] *See* Interpretive Notice, Approval of Fair Practice Rules (Oct. 24, 1978).

[11] *C.f.* By-Laws of FINRA, art. I, § (rr) (defining "associated person of a member" as limited to natural persons, rather than any entity under common control).

The MSRB should clarify that a potential underwriter, registered investment adviser or registered commodity trading advisor, or other person that would be eligible for an exception from the definition of "municipal advisor," either by statute or rule, is not required to comply with MSRB Rule G-36 or any aspect of the G-36 Proposal by virtue of that activity.

D. Disclosure of Conflicts and Informed Consent.

1. Only *Actually Known* Conflicts Should be Disclosed.

The G-36 Proposal would require a municipal advisor to provide written disclosure to its municipal entity client of its conflicts of interest and obtain written informed consent.

The MSRB should clarify that the obligation to disclose conflicts and obtain informed consent is not subject to a strict liability standard, but is rather based on reasonableness and relates only to the *actual* knowledge of the personnel of a municipal advisor who are specifically involved in municipal advisory activities.

SIFMA believes that any other standard would be unworkable and burdensome, requiring the creation of massive information gathering systems without any corresponding benefit to municipal entities. For example, a large financial institution could have many potential conflicts of interest, of which the institution's municipal advisory personnel are not even aware. In order to provide organization-wide disclosures, large firms would be required to develop detailed information-gathering processes across the organization to gather information regarding transactions and relationships that could be seen as raising a potential conflict for the organization as a whole. Without undertaking this massive centralization of information, it would be impossible for such a firm to be able to identify every possible conflict of interest that exists. Worse, attempting to do so could itself risk compromising information barriers and the firm's client confidentiality obligations.

Therefore, the municipal advisor should be permitted to disclose generally expected conflicts and disclose only those additional specific conflicts about which at least one member of the firm's municipal advisory group has actual knowledge. This limitation is sensible, as a conflict of interest that is not actually known to the individuals providing the advisory services to the municipal entity could not, in fact, color their judgment or impact the advice or services they provide.

2. Non-Individualized Disclosures Should Be Permitted.

The MSRB should make clear that its requirement that disclosures be "sufficiently detailed to inform the municipal entity of the nature and implications of the conflict" can be satisfied by disclosing conflicts through disclosures that are not individualized to the municipal entity. Many types of conflicts of interest will be common to many engagements, such as a municipal advisor that has an affiliate that engages in principal transactions in securities of the issuer. Generalized disclosure would be sufficient to alert the municipal entity to such conflicts. However, imposing on municipal advisors an obligation to undertake an individualized investigation and consideration of the exact implications of the conflict to that particular municipal entity would be time consuming and expensive, causing delays and increased costs, which will ultimately be borne by the municipal entity client. Of course, once non-individualized disclosures were provided, a municipal entity could request more detailed and individualized information before entering the engagement. The municipal entity would then itself be able to decide whether the costs and delay of such individualized analysis were warranted in its particular situation.

In addition, the MSRB should clarify that a municipal advisor is permitted to disclose conflicts to a municipal entity only once, at the outset of its first municipal advisory engagement, such as by providing a brochure that outlines its material conflicts of interest. Thereafter, the municipal advisor would not be required to re-deliver these disclosures and re-obtain informed consent on a periodic, transaction-by-transaction, or assignment-by-assignment basis, unless a new, material conflict were discovered. This clarification would reduce the paperwork burden on both municipal advisor and the municipal entity that frequently deal with each other, without any loss of protection for the municipal entity.

3. Disclosures Need Not be Repeated.

The MSRB should confirm that, with respect to any conflicts of interest required to be disclosed and informed consent to be obtained under the G-36 Proposal, a municipal advisor need not re-disclose such information if the information was contained in the municipal advisor's response to a municipal entity's request for proposals or otherwise provided to the municipal entity before the municipal advisor was formally engaged. In such a case, the municipal entity's engagement of the municipal advisor after receipt of such disclosures would provide evidence the municipal entity's informed consent.

4. Official Providing Informed Consent.

The G-36 Proposal would require a municipal advisor to obtain written informed consent to conflicts of interest from its municipal entity client prior to providing (or continuing to provide) municipal advisory services to the municipal entity. This informed consent would need to be provided by an official with the authority to bind a municipal entity.

The MSRB should clarify what level of diligence a municipal advisor would be required to undertake in order to determine whether the official providing the consent has the "authority to bind the municipal entity by contract with the municipal advisor." A municipal advisor should not be viewed as having breached its fiduciaries duties simply because it erred in its understanding of the signing authority of a municipal entity's official. Instead, SIFMA suggests that a municipal advisor's reasonable belief that the official has such authority should satisfy its duty. A representation to this effect by the signing official should be a sufficient basis for the municipal advisor to form this reasonable belief, absent the advisor's actual knowledge that such representation is false.

E. Compensation Conflicts and Disclosure.

The G-36 Proposal would require municipal advisors, as part of their duty of loyalty, to provide their municipal entity clients with disclosures regarding the municipal advisor's compensation and the conflicts inherent in various forms of compensation.

In implementing the fiduciary duty that municipal advisors owe to municipal entities they advise, the MSRB should ensure that its guidance does not restrict the choices available to municipal entities. Municipal entities should be free to choose among various compensation models, including fee-based and commission-based compensation. MSRB rules should not intentionally or effectively foreclose any particular mode of compensation.

SIFMA believes the MSRB should reconsider its proposed requirement that, in order to comply with its fiduciary duty, a municipal advisor disclose conflicts that arise from the municipal advisor's form of compensation. Even if the required disclosures were limited to the general disclosures in the form of Appendix A to the interpretive notice (Disclosure of Conflicts of Interest With Various Forms of Compensation), they should not be required.[12] The conflicts

[12] If the disclosure is to be required at all, it certainly should not be required when the municipal entity requires that a particular manner of compensation be used. Providing a form disclosure that is of no interest to the municipal entity cannot be said to further the municipal (…continued)

described in Appendix A are well understood by municipal entities, and the only meaningful effect of requiring this disclosure will be to obscure more pertinent disclosures and create risks of non-compliance by unwary municipal advisors.

F. Unmanageable Conflicts.

The G-36 Proposal would deem certain conflicts of interest to be "unmanageable." Unmanageable conflicts would be prohibited, even when fully disclosed and consented to by the municipal entity. This policy is based on the MSRB's view that a municipal entity is incapable of actually providing informed consent due to the nature of certain conflicts, even with full and complete disclosure and notwithstanding the sophistication of the municipal entity.

1. Principal Transactions Should Not be Prohibited.

The MSRB should reconsider its position that it is an unmanageable conflict for a municipal advisor to "act[] as a principal in matters concerning the municipal advisory engagement" (with a limited exception for a qualified competitive bid situation). Reasonable disclosure of, and informed consent to, potential conflicts associated with principal activities should be sufficient.

Even investment advisers, which have long been recognized as owing a fiduciary duty and the utmost good faith in dealings with their clients,[13] are not subject to an immutable prohibition on transacting with a client as principal. Rather, consistent with its fiduciary duty, an investment adviser may engage in a principal transaction with a client so long as the adviser obtains the client's consent after disclosing the capacity in which the adviser will act, any compensation the adviser will receive and any other relevant facts.[14]

Similarly, the Dodd-Frank Act requires that swap dealers and security-based swap dealers, when acting as advisors to "Special Entities" (which include

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advisor's duty of loyalty. Rather, such a requirement risks reducing the entire disclosure and consent process to a pure paperwork exercise divorced from any practical purpose or benefit to municipal entities.

[13] *See* SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180 (1963)

[14] *See* Investment Advisers Act of 1940 (the "**Advisers Act**") § 206(3). *See also* SEC Staff Study on Investment Advisers and Broker-Dealers (Jan. 2011) ("**SEC Staff Study**") at 24–26.

municipal entities), have a duty to act in the best interests of the Special Entity.[15] Requiring that these dealers act in the best interest of Special Entities reflects a congressional view that acting as both an advisor and a principal on the same transaction is not an unmanageable conflict of interest.

In fact, in another instance where the Dodd-Frank Act contemplated the imposition of a fiduciary duty, it did not prohibit principal transactions. Section 913 of the Dodd-Frank Act permits the SEC to promulgate rules subjecting broker-dealers to a fiduciary duty when providing personalized investment advice about securities to retail customers. However, Congress instructed the SEC that any such fiduciary duty rule should require disclosure and consent of any material conflicts of interest, rather than an outright prohibition on principal transactions. If Congress believed that broker-dealers could, consistent with a fiduciary duty, transact as principal with *retail* investors, surely it did not intend for municipal entities to be subject to greater protection.

There seems to be no logical distinction why a principal transaction would not be an unmanageable conflict of interest when it occurs between an investment adviser and its client, a swap dealer or security-based swap dealer and a client, or a broker-dealer providing personalized investment advice to a retail client, but the same transaction would be unmanageable when it occurs between a municipal advisor and a municipal entity client. Indeed, because registered investment advisers engaged in municipal advisory activities are exempt from the definition of "municipal advisor,"[16] the effect of the G-36 Proposal would be to impose stricter standard on municipal advisors than investment advisers when each are engaged in the exact same municipal advisory activity.

Congress could not have intended a municipal advisor's fiduciary duty to include a absolute prohibition on principal transactions. Rather, the MSRB should look to the example of existing fiduciary duty regimes, which permit principal transactions with appropriate disclosure and consent.

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[15] *See* Commodity Exchange Act § 4s(h)(4)(B) (added by Section 731 of the Dodd-Frank Act).

[16] *See* Exchange Act § 15B(e)(4)(C).

2. If Principal Transactions are Prohibited, the MSRB Should Limit the Scope of the Prohibition.

Even if principal transactions are generally considered to be unmanageable conflicts in some municipal advisor contexts, municipal advisors should not be generally prohibited from principal transactions, nor should their affiliates.[17] A complete prohibition on municipal advisors transacting as principal with their municipal entity clients would deprive the municipal entity of access to certain financial products, such as fixed income products the municipal advisor sells in its brokerage capacity, or swaps the municipal advisor enters into in its swap dealer capacity. Instead, the MSRB should consider limiting those principal transactions that are considered unmanageable to those few narrow instances where disclosure and consent may actually be ineffective.

In particular, the ban should not apply to common principal activities of persons that, in addition to being a municipal advisor, conduct other principal-based regulated businesses, such as banks taking deposits; broker-dealers selling fixed income securities; swap dealers or security-based swap dealers entering into swaps or security-based swaps that comply with applicable CFTC or SEC business conduct rules; or foreign exchange transactions. These activities are already subject to comprehensive oversight and regulation by their respective regulators.[18]

A complete prohibition on principal transactions would harm, rather than protect municipal entities. For example, if deposit-taking and other traditional banking services are not excluded from the prohibition on principal transactions, it will greatly restrict municipal entities from obtaining banking services from banks that are also municipal advisors, harming municipal entities' ability to obtain necessary and beneficial financial products and services. Similarly, if a municipal advisor that is also a broker-dealer is prohibited from selling securities out of inventory to its municipal entity client, the municipal entity will face increased costs to obtain those securities.[19]

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[17] *See also* Section II.C.3 above.

[18] For example, SEC and FINRA rules permit broker-dealers to transact as principal, but they may only do so consistent with "best execution" obligations and may not charge excessive markups or markdowns.

[19] *See*, *e.g.*, SEC Staff Study at 159–60 (noting that "costs associated with purchasing certain securities, particularly less liquid securities, as agent, may increase execution costs for (…continued)

The MSRB should also reconsider the extension of this ban to affiliates of the municipal advisor that act as a principal with the municipal entity on the same transaction. Such a prohibition would prove burdensome and unworkable in a large financial institution engaged in the provision of multiple services to municipal entities through a number of related affiliates. In any case, this ban should be measured by a reasonableness rather than strict liability standard, such that one person would not be prohibited from acting as principal on a transaction because a distant corporate cousin that is nominally, but not practically, under common control acts as the municipal entity's municipal advisor. Instead, the prohibition should only apply to those personnel of the municipal advisor who actually deal directly with the municipal entity and have actual knowledge of the facts of the engagement giving rise to the prohibition. Requiring persons to conduct an investigation of what relationships all of its affiliates and their personnel have with a municipal entity before transacting as principal with that municipal entity would create great expense and delay, while providing little, if any, additional protection to the municipal entity.

The MSRB should also clarify that this prohibition on principal transactions would not bar a municipal advisor or its affiliates from performing other *services* for a municipal entity (*e.g.*, acting as a trustee, collateral agent, calculation agent or broker).

3. Further Guidance is Needed Regarding Kickbacks and Fee-Splitting Arrangements.

Among conflicts that are "unmanageable," the G-36 Proposal highlights "kickback arrangements, or certain fee-splitting arrangements, with the providers of investments or services to municipal entities." Because of the variety of legitimate compensation arrangements that may exist, the MSRB should provide additional clarification of how it would define impermissible "kickbacks" and "fee splitting," or confirm that these impermissible arrangements are limited to the types of referral fees, excessive mark-ups and fee splitting described in footnote 7 to the G-36 Proposal.

The MSRB should also take care not to classify common and generally accepted arrangements as "unmanageable conflicts," thereby disrupting legitimate business arrangements. For example, financial institutions that hold funds of municipal entities often sweep cash balances into money market mutual funds. In

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some investors, namely those customers of broker-dealers who otherwise had maintained inventories of such securities").

a fully disclosed arrangement, to which the municipal entity provides informed consent, the financial institution may receive a 12b-1 fee or a revenue sharing fee from the fund or its adviser.[20] This and similar common arrangements do not present an unmanageable conflict—when full disclosure is provided, municipal entities are capable of considering the conflict and providing informed consent. To assure that these types of programs—which provide benefits to municipal entities—remain available, the MSRB should provide specific guidance as to which "certain" fee-splitting arrangements are proscribed. Otherwise, municipal advisors will be forced to curtail their offerings and municipal entities will be faced with fewer investment options.

4. Further Guidance is Needed Regarding Prohibited Payments to Solicitors.

Under the G-36 Proposal, it would be an unmanageable conflict for a municipal advisor to make a payment "for the purpose of obtaining or retaining municipal advisory business other than reasonable fees paid to a municipal advisor described in Section 15B(e)(9) of the Exchange Act" (defining solicitation). As an initial matter, to the extent that the MSRB intends for this provision to serve to regulate pay-to-play activity, SIFMA believes that the MSRB should instead address pay-to-play issues through its pay-to-play rules, and not in an indirect manner by classifying pay-to-play activity as an unmanageable conflict.

SIFMA has separately commented on MSRB and SEC pay-to-play proposals, and does not believe that it is appropriate to reiterate its comments here.[21] However, we note that any prohibition on payments to *affiliated* solicitors is highly problematic in the context of multi-service financial institutions and contrary to the apparent intent of Section 975, which defines solicitation of a municipal entity as certain solicitations undertaken for one of certain types of

[20] Although not reflected in the G-36 Proposal, a bank that advises a municipal entity to invest its cash deposit balances in a money market mutual fund may be considered municipal advisor if the Pending SEC Proposal is adopted. *See, e.g.*, Pending SEC Proposal at 42 .

[21] *See* Comment Letter from Leslie M. Norwood, SIFMA, to Ronald W. Smith, MSRB (Feb. 25, 2011), *available at* http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2011/~/media/Files/RFC/2011/2011-04/SIFMA.ashx; Comment Letter from Leslie M. Norwood, SIFMA, to Elizabeth M. Murphy, SEC (Feb. 25, 2011), *available at* http://www.sec.gov/comments/s7-45-10/s74510-657.pdf.

entities "that does not control, is not controlled by, or is not under common control with the person undertaking such solicitation…"[22]

Additionally, the MSRB should clarify that any provision governing payments for solicitation does not apply to activities that are not regulated by the MSRB, such as when a person that is also a municipal advisor makes payments to a third party, whether affiliated or unaffiliated, in connection with a commodity futures or even a non-financial transaction.

G. Prohibition on Excessive Compensation.

1. Further Guidance is Required on When Compensation will be Considered "Excessive."

The G-36 Proposal states that a municipal advisor violates its duty of loyalty to the municipal entity if its compensation is "so disproportionate" to the services performed such that it is "excessive." While the proposed interpretation acknowledges that what constitutes reasonable compensation will vary depending on many factors, the proposal gives no guidance as to where the line between reasonable and excessive lies.

Without further guidance, municipal advisors are at risk of having a standard established only in hindsight. Consider a situation where, after full disclosure, a municipal entity agrees to an hourly fee for advice relating to the issuance of municipal securities. Due to various factors unrelated to the municipal advisor's services, the transaction does not close. In hindsight, the municipal advisor's fee may appear to have been excessive in light of the services performed on a failed offering. Although this may not be the MSRB's intent, municipal advisors will need to be constantly concerned that their compensation could be deemed "excessive" at a later date, which may cause them to limit the services or compensation arrangements they offer to municipal entities.

Instead, a fully disclosed and negotiated compensation arrangement, absent fraud, should not be subject to hindsight review for potentially being "excessive" or "disproportionate" unless the MSRB provides clear objective measures that can be applied prospectively.

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[22] Exchange Act § 15B(e)(9).

H. Duty to Evaluate Alternatives and to Assess Whether a Transaction Is in a Municipal Entity's Best Interest.

1. Municipal Advisors Should Not be Required to Consider Alternatives Unless Specifically Engaged to Do So.

The G-36 Proposal provides that, as part of a municipal advisor's duty of care, the municipal advisor has a general duty to investigate and advise a municipal entity of alternatives to a proposed financing structure or product that are reasonably feasible based on the issuer's financial circumstances and the prevailing market conditions, if those alternatives would better serve the interests of the municipal entity.

The MSRB should reconsider imposing such implied affirmative obligations. Rather, the presumption of this duty should be reversed, such that a municipal advisor need only do what the municipal entity contracts for it to do, and only undertakes additional investigation and advisory activities at the request of the municipal entity. A municipal entity should not have to pay for services beyond those for which it expressly engaged the municipal advisor. Were the MSRB to retain this duty as drafted, municipal advisors would extensively negotiate the forms of engagement letters in order to fit into the "limited engagement" exception.

In addition, if any duty is to be implied, it should not apply in the context of a request for proposals where the form of engagement letter is non-negotiable. The imposition of such a duty by rule, coupled with the inability to negotiate a limited engagement clause in the engagement letter, would likely cause municipal advisors to limit the services that they offer, which would reduce competition in the marketplace and raise the cost of services.

2. More Guidance is Needed Regarding Duty of Inquiry When Providing a Certificate.

Under the G-36 Proposal, the MSRB would interpret a municipal advisor's fiduciary duty to its municipal entity client to include a duty to "make a reasonable inquiry as to the pertinent facts" when asked to provide a certificate that will be relied on by the municipal entity or by investors in the municipal entity's securities.

If the MSRB retains this requirement, the MSRB should clarify the required scope of a municipal advisor's factual investigation in connection with such municipal advisor's provision of a "certificate." The MSRB should also clarify whether any qualifications on the nature and scope of the investigation will

be permitted, and whether a municipal advisor may limit the scope of its engagement to disclaim such duty in the initial engagement letter or at any point thereafter. Indeed, it is impossible at the outset of an engagement to anticipate all of the limitations on the duty of inquiry that may be relevant in the context of providing a certificate. The examples contained in footnote 20 to the G-36 Proposal illustrate how large this universe of potential duties is (*e.g.*, reckless certifications of compliance with a "minimum credit requirement" and failure to exercise due care in its appraisals used in official statements).

3. The MSRB Should Not Impose New Due Diligence Requirements for Official Statements.

Under the G-36 Proposal, the MSRB would interpret a municipal advisor's fiduciary duty to its municipal entity client, when the municipal advisor undertakes the preparation of an official statement, to include a duty to "exercise due diligence as to the facts that are material to the offering."

The MSRB should reconsider this interpretation. Even where a municipal advisor participates in preparing the official statement, it is but one of many parties—and their counsel—involved in the process. While many parties contribute, it is understood by all that the official statement is the issuer's document and that ultimately, it is the issuer's obligation to ensure that the official statement contains all facts material to the offering. The MSRB should not reverse this fundamental principle under the guise of a duty of care. While the municipal advisor should be responsible for any information it provides, it should not—based on an interpretation of its fiduciary duty to the issuer—have responsibility for the accuracy or completeness of the entire official statement.

If the MSRB concludes to require municipal advisors to conduct this due diligence, the MSRB should clarify how exhaustive a municipal advisor's factual investigation must be. For example, the MSRB should clarify whether the municipal advisor may limit the scope of its engagement and qualify the nature and scope of the investigation, or whether a municipal advisor may contract out of such duty in the initial engagement letter or at any point thereafter. The MSRB should also clarify, where an underwriter assists in the preparation of an official statement, how the underwriter exception interacts with this duty.

In addition, the interpretive notice is ambiguous as to whom this duty of due diligence is owed. The MSRB should clarify that in interpreting a municipal advisor's fiduciary duty to its municipal entity client, the MSRB does not intend to impose on municipal advisors any direct obligations or potential liability to investors. The MSRB should not create due diligence requirements or new liabilities for official statements beyond those already existing under federal

securities laws. The MSRB should not create new sources of liability to investors; rather it should interpret the duty of care owed to the municipal entity. The MSRB should also clarify that any such duty would not be applicable in the case where the municipal entity serves as a conduit issuer for an obligated person, such as a private corporation or other private entity.

4. Municipal Advisors Should Not be Required to Conduct an Inquiry into Counterparty Representations Unless Specifically Engaged to Do So.

The G-36 Proposal would require that the municipal advisor "conduct a reasonable inquiry into representations of a municipal entity's counterparties." This duty would be unprecedented and burdensome and should not be imposed absent a specific request from the municipal entity client for the municipal advisor to do so. This duty seems to view a municipal advisor as an independent advisor to an issuer, rather than the many other roles that could give rise to municipal entity status, such as providing advice as a swap dealer.

At very least, the MSRB should provide clear guidance regarding the scope of a municipal advisor's duty to engage in a "reasonable inquiry." Because the MSRB has recognized that the municipal advisor is "not a guarantor" of the transaction, the MSRB should clarify that the municipal advisor is not required to undertake the type of investigation that would be required of a person that would be strictly liable for the success of the transaction. In addition, the MSRB should clarify that a municipal advisor would not be required to inquire into a counterparty's representations if the advisor's engagement is limited to advising the municipal entity as to the type of transaction in which the municipal entity should engage, and does not include advice regarding the specific counterparty with whom the municipal entity should conduct the transaction.

5. Limited Scope Engagements Should Be Limited in Scope.

Under the G-36 Proposal, the MSRB would permit an engagement to be limited in scope by specifying the limitation in the engagement letter or other written communication.[23] However, even in the face of a limited scope

[23] The MSRB's recognition that engagements may be limited in scope by providing for the limitation in the engagement letter further supports the position that the beginning of an "engagement" should be defined by entering into an engagement letter, as discussed in Section II.C.1 above. Otherwise, the limitations on scope that the Proposal permits would be impossible to implement during what the parties otherwise view as preliminary informal discussions.

engagement that specifically excludes the service, the G-36 Proposal would require a municipal advisor to (i) advise its municipal entity client if it has formed a broader judgment about the appropriateness of a financing or product, or (ii) expand the scope of its engagement based on the "course of conduct."

The MSRB should reconsider these positions, which would, by law, force municipal advisors to perform services that municipal entities contractually declined, thereby raising costs on municipal entities.

Where an engagement is specifically limited in scope to exclude advice regarding the appropriateness of a financing or product, municipal advisors should not nonetheless be required to inform its municipal entity client if it has formed a judgment about the financing or product. Even though, by its terms, this interpretation would only apply where the municipal advisor has actually formed a view, the practical effect of this interpretation would be that municipal advisors, in order to protect themselves from hindsight second-guessing, would be required to affirmatively consider the advisability of a financing or product. Otherwise, were a financing or a product to turn out to have been inappropriate for the municipal entity, the municipal advisor would always be subject to questioning and potential litigation about whether it had failed to disclose a view to the municipal entity.

Instead, where the parties have specifically contracted for a limited engagement that does not cover advising on the appropriateness of a financing or product, MSRB should not force it upon them. Otherwise, the municipal advisor's certification of its competence as part of its registration as a municipal advisor could be called into question. Adopting this interpretation would prevent municipal entities from effectively limiting the scope of the engagement and force municipal entities to bear the increased costs for services they have specifically decided they do not require.

Further, the MSRB should reconsider its position that, in the face of documentation limiting the scope of an engagement, a municipal advisor's "course of conduct" could "cause the municipal entity to expect that the advisor will be advising on appropriateness" and thereby re-impose the municipal advisor's duty to consider alternatives. This type of interpretation invites hindsight review of the course of conduct and will prevent municipal advisors from ever having certainty as to the extent of their duties. To protect themselves, municipal advisors will be forced to take on duties that their municipal entity clients have specifically declined, the cost of which will be borne by the municipal entities.

Indeed, the MSRB should adopt the position that if the engagement letter or other documentation between the parties expressly limits the scope of the engagement, then the scope of the engagement will be so limited, even if the municipal advisor's "course of conduct" could, notwithstanding the documentation, be viewed as broader than the scope of the engagement.

III. G-17 Proposal – Duties to Obligated Persons and Solicited Municipal Entities

Under Rule G-17, "[i]n the conduct of its . . . municipal advisory activities, each . . . municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice." This duty of fair dealing extends to municipal advisory dealings with all persons, and the G-17 Proposal applies to (i) municipal advisors that advise obligated person clients and (ii) municipal advisors that solicit business from municipal entities on behalf of third parties.

A. Duty of Fair Dealing to Obligated Persons.

1. Absent a Fiduciary Duty, Municipal Advisors Should Not Owe a Duty of Care or Duty to Disclose Conflicts and Obtain Informed Consent.

The G-17 Proposal would interpret a municipal advisor's duty to "deal fairly" with obligated persons to include a duty of care, a duty to assess the appropriateness of a transaction and a duty to disclose material conflicts of interest and obtain informed consent. As proposed, the duties imposed on a municipal advisor engaged by an obligated person are barely distinguishable from the fiduciary duty owed to municipal entities under the G-36 Proposal. Because the duty of fair dealing, both by its nature and the words used in Rule G-17, is not the same as a fiduciary duty, the MSRB should impose significantly fewer obligations on a municipal advisor engaged by an obligated person under Rule G-17.

The G-17 Proposal is a novel and expansive interpretation of what constitutes "fair dealing." Rule G-17 is not a new rule, but was recently amended, only slightly, to simply add reference to municipal advisors.[24] This minor amendment made municipal advisors engaged in municipal advisory activities subject to the same standard of fair dealing that brokers, dealers and municipal

[24] *See* MSRB Fair Dealing Rule For Municipal Advisors Approved, MSRB Notice 2010-59 (Dec. 23, 2010).

securities dealers engaged in municipal securities activities were already subject to under the rule. However, the fiduciary concepts of a duty of care and a duty to disclose conflicts and obtain informed consent have never before been interpreted to be part of the duty to deal fairly that applied under Rule G-17. Additionally, such an interpretation is neither required nor proper under Section 975, which only deems a municipal advisor to have a fiduciary duty only when it is engaged by a municipal entity, not when it is engaged by an obligated person or engages in a solicitation of a municipal entity on behalf of a third party.[25]

SIFMA notes that the MSRB made no indication in its proposal to the SEC to amend Rule G-17 that it intended to take such an expansive interpretive view of how the existing Rule G-17 would apply to municipal advisors. To the contrary, the MSRB stated to the SEC that the purpose of the proposed rule change was merely "to apply the MSRB's core fair dealing rule to municipal advisors *in the same manner that it currently applies* to dealers."[26] In fact, the MSRB posited that the change to Rule G-17 would impose no burden on municipal advisors because "most municipal advisors already comport themselves in accordance with the standards of behavior required by Rule G-17 and no municipal advisor has a legitimate interest in engaging in behavior that is fraudulent or otherwise unfair."[27] However, the implied affirmative obligations that the G-17 Proposal would impose on municipal advisors clearly go far beyond simply refraining from engaging in fraudulent or unfair behavior, and is entirely foreign to the manner in which G-17 applies to other entities. As a result, SIFMA was unable to provide meaningful comments on the MSRB's amendment to Rule G-17 when it was published for comment by the SEC.

The MSRB should reconsider imposing a duty of care and duty to disclose conflicts and obtain informed consent as a part of Rule G-17's obligation of fair dealing. Such additional duties are not provided for by the language of MSRB Rule G-17 and should not be implied. Rather, the MSRB should state that a municipal advisor's duty of fair dealing requires it to fully and faithfully provide the services contracted by an obligated person and not engage in fraudulent or deceptive conduct. Further, by imposing its additional implied duties, the MSRB's interpretive notice and the obligations thereunder may be inconsistent with existing obligations of currently regulated persons, such as broker-dealers and investment advisers, as well as persons such as swap dealers that will be

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[25] *See* Exchange Act § 15B(c)(1).

[26] *See* Exchange Act Release No. 63309 (Nov. 12, 2010) (emphasis added).

[27] *Id.*

subject to similar duties in the near future. For example, a swap dealer, whose primary regulator is the CFTC, owes different duties depending on whether or not a counterparty that it is also advising is an obligated person. Because Section 975 imposes a fiduciary duty on a municipal advisor only with respect to its municipal entity clients, there does not appear, in the absence of a statutory mandate, to be any basis or justification for imposing a duty of care on a municipal advisor that advises an obligated person that is not otherwise a municipal entity.

2. Requested Clarifications Regarding the G-36 Fiduciary Duty Should Apply to Similar Obligations Under the Duty of Fair Dealing.

To the extent that the MSRB maintains its interpretation that Rule G-17 includes a duty of care and duty to disclose conflicts and obtain informed consent under, then it should clarify that any part of the application of Rule G-17 to municipal advisors that is similar to an obligation that would be incurred under Rule G-36 would be subject to the clarifications and contours (including with respect to the disclosure of fee arrangements) discussed above with respect to the G-36 Proposal.

3. The MSRB Should Not Create a New "Appropriateness" Standard.

The G-17 Proposal would require a municipal advisor that recommends a municipal securities transaction or municipal financial product to its obligated person client to have "concluded, in its professional judgment, that the transaction or product is appropriate for the client, given its financial circumstances, objectives and market conditions."

The MSRB should consider whether this "appropriateness" standard is effectively creating a new "suitability" standard, and if so, whether it is necessary to do so. Where possible, SIFMA believes the MSRB should avoid creating new, potentially conflicting, standards, the contours of which cannot be known in advance—especially when familiar and well recognized standards already exist. To the extent that the MSRB imposes such a new "appropriateness" duty, it should define this duty so that it is consistent with other suitability, fiduciary, fair practice or other already applicable obligations, as the case may be, to such persons as broker-dealers, municipal securities dealers and investment advisers.

In particular, the MSRB should reconsider imposing an "appropriateness" duty on a municipal advisor where the municipal advisor is already regulated and subject to a competing standard. For example, broker-dealers subject to the Financial Industry Regulatory Authority's ("**FINRA**") suitability standard and

investment advisers subject to a fiduciary duty should be deemed to have complied with the appropriateness standard when they comply with the standard that is otherwise applicable to them.

4. Duty to Inform of Material Risks of Transaction and Services.

In order to meet the "appropriateness" standard, the G-17 Proposal would require municipal advisors to advise their obligated person clients regarding the "material risks and characteristics" of any recommended transaction or product. Specifically, a municipal advisor that recommends to an obligated person that it enter into a municipal derivative contract is required to disclose the material risks (including market, credit, operational, and liquidity risks) and characteristics of the derivative.

In order to avoid duplicative and potentially conflicting regimes, the MSRB should clarify that a municipal advisor's duty to disclose material risks will be deemed satisfied where it complies with a similar requirement of another applicable regulatory regime. For example, in the case of a municipal advisor that recommends a swap or a security-based swap, the municipal advisor's disclosure obligation regarding material risks would be deemed satisfied if the municipal advisor satisfies applicable CFTC or SEC business conduct requirements.[28] In addition, this duty should be limited to specified types of transactions, and not extend to the full range of ordinary course transactions, such as bank deposits and the issuance of fixed or floating rate debt.

5. Municipal Advisors Should Not be Subject to Additional Implied Obligations When Reviewing Municipal Securities Transactions.

When a municipal advisor has been engaged by an obligated person to review a municipal securities transaction or municipal financial product recommended by another party (*e.g.*, an underwriter), the G-17 Proposal would imply an obligation of the municipal advisor to "evaluate and advise the client of the material risks and characteristics of the transaction or product and its appropriateness for the client, based on the client's financial circumstances, objectives, and market conditions."

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[28] *See*, *e.g.*, CFTC Proposed Rule, Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 75 Fed. Reg. 80638 (Dec. 22, 2010).

The MSRB should reconsider imposing such an implied obligation on municipal advisors. Rather, the municipal advisor should only be obligated to do what the municipal entity has contracted for it to do in connection with reviewing the transaction. In this regard, the MSRB should clarify that a municipal advisor need not "expressly disclaim" the obligation to advise its client as to the appropriateness of the transaction or product, as, absent explicit agreement between the parties, the municipal advisor need not provide any services or undertake any analysis other than that for which the municipal advisor is hired by the obligated person.

Moreover, any duty to analyze the appropriateness of transactions should be limited to those facts that the municipal advisor is expressly required to obtain under MSRB rules or which municipal advisory personnel already have in their possession; no additional due diligence or fact gathering should be required.

6. Misrepresentation Requirements and Disclosures.

The G-17 Proposal would consider it a "misrepresentation" if, in a response to a request for proposals or qualifications, a municipal advisor failed to "fairly and accurately describe [its] capacity, resources and knowledge to perform the proposed municipal advisory engagement." The MSRB should reconsider this interpretation, as these requirements and their related prohibitions may be difficult for a municipal advisor to comply with when discussing a potential engagement with an obligated person.

To the extent that this interpretation is maintained, the MSRB should provide guidance as to how a municipal advisor may presently determine its capacity, resources and knowledge to perform the proposed municipal advisory engagement on a forward-looking basis. Further, the MSRB should confirm that municipal advisors may satisfy this disclosure obligations by providing generalized disclosures concerning their qualifications for an assignment in connection with the request for proposal or engagement process. In any case, the MSRB should clarify that a municipal advisor will not be deemed to have breached this duty if, it becomes apparent in hindsight that the municipal advisor was not properly qualified.

B. Duty of Fair Dealing When Soliciting on Behalf of Others.

1. Disclosures Regarding Solicitation and Offered Products and Services.

As part of a municipal advisor's duty of fair dealing when soliciting a municipal entity on behalf of a municipal advisor (in such capacity, a "**solicitor**"), the G-17 Proposal would require a solicitor to provide the municipal entity it solicits with various disclosures regarding the solicitation, the solicitor's client, the solicitor's compensation and the solicitor's relationships. Further, if the solicitor is soliciting with respect to a particular product or service, the proposal would require the solicitor to "disclose all material risks and characteristics of the product or service."

The MSRB should reconsider what disclosures a solicitor will be required to provide about the solicitation itself and the products or services being offered by its client to the municipal entity. In particular, disclosures of all relationships that the solicitor may have with influential employees, board members or affiliates of the municipal entity may be particularly extensive (and possibly unknowable) for large organizations—and of dubious value. Additionally, while a solicitor will typically familiarize itself with its municipal advisor client's products and services for purpose of making solicitations, it will not be in the best position to disclose all "material risks and characteristics" of the products or services being offered by its client and it should not have the obligation to do so. In any case, such disclosure is unnecessary and duplicative because a municipal advisor retained by the municipal entity will itself be required to provide this and various other disclosures in order to satisfy its own fiduciary duty to the municipal entity under Rule G-36.

2. Lavish Gifts and Gratuities.

The G-17 Proposal indicates that a solicitor would be considered to engage in deceptive, dishonest or unfair practices if the solicitor provides "lavish gifts and gratuities" to officials of a municipal entity or affiliated parties. A gift or gratuity will be considered "lavish" if it exceeds the limits imposed under Rule G-20 ($100 per year).

Gifts and gratuities is a complex topic that is not appropriately dealt with in the short-hand manner presented here. Notably, though Rule G-17, which also applies to brokers, dealers and municipal securities dealers, could be interpreted as implying a prohibition on lavish gifts and gratuities, nonetheless the MSRB dealt directly with this issue in Rule G-20. Rather that making a passing

reference to a prohibition on lavish gifts in the G-17 Proposal, if the MSRB believes solicitors should be subject to Rule G-20, it should include appropriate rules tailored to municipal advisors that solicit municipal entities on behalf of third parties in its proposal to amend Rule G-20.[29]

3. Duties Should Not Apply to Affiliated Solicitors.

As noted in Section II.F.4 above, Section 975 excludes from the definition of "municipal advisor" persons that solicit municipal entities on behalf of a persons under common control with the solicitor.[30] As such, even when a person is otherwise registered as a municipal advisor, such person should not be considered to be engaged in a municipal advisor activity when it solicits on behalf of its affiliate. The MSRB should therefore clarify that any requirements imposed by the G-17 Proposal would apply only to a solicitor that is unaffiliated with the entity on whose behalf it solicits, while a solicitor soliciting for an affiliate—even if otherwise registered as a municipal advisor—would not be subject to the obligations imposed by the G-17 Proposal while engaged in that solicitation. If the MSRB intended this provision to subject such persons to its pay-to-play rules, it should do so directly through its pay-to-play rulemaking, rather than indirectly through the G-17 Proposal.[31]

IV. Implementation Period.

Each of the Proposals would obligate municipal advisors to comply with detailed and specific requirements to which they are not currently subject. Many of these requirements, depending on whether they are adopted as proposed, will require significant lead time in order for municipal advisors to create systems to ensure compliance. Therefore, SIFMA requests that when a final Rule G-36 and related interpretive guidance and final interpretive guidance on Rule G-17 are adopted, the MSRB provides for a reasonable implementation period, which would certainly be no less than one year, before the Proposals become effective.

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[29] *See* Request for Comment on Gifts and Gratuities Rule for Municipal Advisors, MSRB Notice 2011-16 (Feb. 22, 2011).

[30] *See* Exchange Act § 15B(e)(9).

[31] *See supra* note 21 and accompanying text.

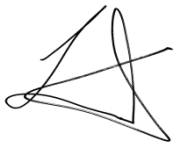
V. Conclusion

SIFMA supports the MSRB in its efforts to clarify the duties owed by municipal advisors to municipal entities and obligated persons. However, as discussed above, the MSRB Proposals are premature until the SEC has adopted final rules concerning what activities constitute acting as a "municipal advisor." In any case, the MSRB Proposals impose too many implied affirmative obligations that will prove unworkable and overly burdensome on municipal advisors, while expensive and unhelpful to municipal entities and obligated persons, these will ultimately lead to increased costs for municipal entities and obligated persons and decreased availability of beneficial products and services.

* * *

SIFMA appreciates this opportunity to comment upon the MSRB Draft Rule G-36 (on Fiduciary Duty Of Municipal Advisors) and related Draft Interpretive Notice and the MSRB Draft Interpretive Notice Concerning the Application of Rule G-17 to Municipal Advisors. Please do not hesitate to contact me with any questions at (212) 313-1130; or Robert L.D. Colby and Lanny A. Schwartz, of Davis Polk & Wardwell LLP, at (202) 962-7121 and (212) 450-4174, respectively.

Sincerely yours,



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cc: ***Securities and Exchange Commission***
The Honorable Mary L. Schapiro, Chairman
The Honorable Kathleen L. Casey, Commissioner
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
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