MSRB
Municipal Securities Rulemaking Board

October 17, 2014

Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Response to Comments on SR-MSRB-2014-06

Dear Secretary:

On July 24, 2014, the Municipal Securities Rulemaking Board ("MSRB") filed with the Securities and Exchange Commission ("SEC") a proposed rule change consisting of proposed Rule G-44, on supervisory and compliance obligations of municipal advisors; and proposed amendments to Rule G-8, on books and records to be made by brokers, dealers and municipal securities dealers; and proposed amendments to Rule G-9, on preservation of records (the "proposal"). The SEC published the proposal for comment in the Federal Register on August 5, 2014[1] and received eight comment letters.[2] This letter responds, as appropriate, to the comments, most of which are substantially similar to previous comments on the related MSRB requests for comment[3] and are addressed in the filing discussing the proposal, fully incorporated herein by reference.

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1 *See* Exchange Act Release No. 72706 (Jul. 29, 2014), 79 FR 45546 (Aug. 5, 2014) ("SEC Notice").

2 *See* letters from Cristeena G. Naser, Vice President, Center for Securities, Trust & Investments, American Bankers Association ("ABA") dated August 26, 2014; Anonymous Attorney ("Anonymous Attorney") dated August 26, 2014; Michael Nicholas, Chief Executive Officer, Bond Dealers of America ("BDA"); Joshua Cooperman, Cooperman Associates ("Cooperman") dated August 30, 2014; Tamara K. Salmon, Senior Associate Counsel, Investment Company Institute ("ICI") dated August 19, 2014; Nathan R. Howard, Counsel, National Association of Independent Public Finance Advisors ("NAIPFA") dated August 26, 2014; Dave A. Sanchez ("Sanchez") dated August 25, 2014; and David L. Cohen, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association ("SIFMA") dated August 21, 2014.

3 ABA, BDA, ICI, NAIPFA, and SIFMA submitted comments in response to MSRB Notice 2014-04 (Feb. 25, 2014) (requesting comment on a draft Rule G-44 and draft amendments to Rules G-8 and G-9) ("Request for Comment"), and Cooperman submitted comments in response to MSRB Notice 2014-01 (Jan. 9, 2014) (requesting comment on

Most commenters generally continue to support the rulemaking initiative and the proposal, although some suggest the MSRB modify the proposal in certain respects. Despite some differences in approach discussed below, there remains a broad consensus for the establishment of a municipal advisor supervision and compliance rule. BDA believes the effort to craft an appropriately-tailored rule is extremely important to the entirety of the municipal advisor regulatory regime. SIFMA continues to support the effort to ensure that municipal advisors are properly supervised and that all municipal advisors adopt a supervisory structure for engaging in municipal advisory activities, and SIFMA specifically supports the requirements contained in the proposal because they follow a widely-accepted model in the securities industry. Similarly, ICI believes the proposal is appropriate and that subjecting municipal advisors to supervisory and compliance obligations inasmuch as other securities professionals are subject to similar obligations, including federally-registered broker-dealers and investment advisers, is in the interest of municipal advisor clients. NAIPFA and Sanchez also support many aspects of the proposal as noted more specifically herein.[4]

Flexibility for Small Municipal Advisors

Proposed Rule G-44, which is the first dedicated municipal advisor rule to be filed with the SEC since the adoption of the SEC's final registration rules, is designed to provide flexibility to small municipal advisor firms, including those with only one associated person, allowing municipal advisors to tailor their supervisory procedures to, among other things, their size, particular business model and structure. BDA believes proposed Rule G-44 provides too much flexibility to small firms by allowing them to determine and make accommodations for themselves simply because of their size, and that those accommodations should be circumscribed. Cooperman would prefer more prescriptive requirements or guidance for small firms, particularly sole-proprietorships. NAIPFA believes proposed Rule G-44 strikes the appropriate balance between a principles-based approach and a prescriptive approach to supervision, though NAIPFA suggests that the MSRB consider exempting single-person firms from developing a compliance manual.

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additional draft amendments to Rules G-8 and G-9 that were initially published in connection with draft Rule G-42 on standards of conduct and duties of municipal advisors when engaging in municipal advisory activities other than the undertaking of solicitations).

4 NAIPFA believes its previous comments to the Request for Comment did not appear to result in any substantive changes to the proposal, so it re-submitted, in response to the SEC Notice, its April 28, 2014, comment letter to the MSRB. Although the MSRB believes it adequately addressed NAIPFA's comments previously, it will address some of them again in this response, as appropriate. Additionally, some commenters express concerns regarding the MSRB's analysis of the implementation costs and other economic implications of the proposal. The MSRB notes that these concerns are substantially similar to comments made in response to the Request for Comment, which the MSRB has addressed previously in the filing discussing the proposal.

The MSRB acknowledges that proposed Rule G-44 contains standards that may vary based on firm size. The MSRB believes the appropriateness of supervisory procedures is affected by a firm's size and deliberately drafted the rule to give firms flexibility to tailor their supervisory systems accordingly, striking an appropriate balance between burdens on, and flexibility for, small municipal advisors. Moreover, the approach set forth in proposed Rule G-44 seems particularly appropriate for an industry in which many participants are becoming regulated at the federal level for the first time.

Requiring sole-proprietors to have a supervisory system in place is important because effective oversight of a firm's municipal advisory activities is essential regardless of firm size. Proposed Rule G-44 deliberately does not contain specific prescriptions as to the procedures a sole proprietor should have, as such detail would undermine the proposed rule's flexibility and the primarily principles-based approach utilized. However, proposed Rule G-44 establishes a minimum standard for supervisory and compliance obligations that all municipal advisors, regardless of size, must meet. Accordingly, the MSRB is declining, at this time, to provide more prescriptive requirements or guidance, in part, because it may be impracticable for the MSRB to develop such requirements or guidance to address the scope and diversity of business models and particular practices of the numerous municipal advisor firms.

A provision in paragraph .02 of the Supplementary Material to proposed Rule G-44 requires that the written supervisory procedures of municipal advisors with a single associated person address the manner in which, in the absence of separate supervisory personnel, such procedures are nevertheless reasonably designed to achieve compliance with applicable rules. Sanchez believes this provision is vague and probably unnecessary. NAIPFA similarly believes this provision is vague and ambiguous, and would present a significant challenge for firms seeking to develop a sufficient policy. Sanchez suggests that compliance with proposed Rule G-44(a) and (b), paragraph .04 of the Supplementary Material, and the associated recordkeeping requirements should be deemed a sufficient supervisory system for municipal advisors with a single associated person, or, in the alternative, he suggests deleting this particular provision in paragraph .02 entirely.

The MSRB believes this provision is important to ensuring all municipal advisors establish meaningful procedures that will satisfy the minimum standard established by proposed Rule G-44. Developing appropriate systems and documenting and following written procedures is a well-established practice among businesses, regardless of size, for facilitating compliance with regulation in a broad range of other areas (*e.g.*, taxes, human resources). Additionally, the MSRB notes that Financial Industry Regulatory Authority's ("FINRA") consolidated supervision rule (FINRA Rule 3110) includes a substantially similar requirement.[5] Although this provision will always apply to sole-proprietorships, the MSRB believes it is relevant to other firms in which associated persons may be otherwise permitted to supervise their own activities.

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[5] *See* FINRA Rule 3110(b)(6)(C); Exchange Act Release No. 71179 (Dec. 23, 2013), 78 FR 79542 (Dec. 30, 2013) (approving FINRA Rule 3110) ("FINRA Rule 3110 Approval Order").

Accordingly, the MSRB is filing with the SEC an amendment to the proposal to revise the rule text to expand the applicability of the requirement to all firms with associated persons who supervise their own activities.

Annual Certification

Several commenters address the proposed annual self-certification requirement as to compliance processes in proposed Rule G-44(d). Previously, in response to the MSRB's Request for Comment, BDA stated that proposed Rule G-44 should require all municipal advisors, regardless of size, to complete a periodic self-certification regarding the meeting of professional qualification standards by their associated persons, as well as the ability to comply, and history of complying, with all applicable regulatory requirements.[6] BDA further suggested exempting broker-dealers subject to a FINRA certification requirement in order to avoid a duplicative burden on such firms. FINRA Rule 3130 requires member firms to certify annually that it has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures; it does not require certification regarding the meeting of professional qualification standards by associated persons or the ability to comply and history of complying with all applicable regulatory requirements. This FINRA requirement is limited in scope as compared to the broader certification suggested by BDA.

The MSRB revised proposed Rule G-44 to create a self-certification in response to the BDA comment submitted to the MSRB and provided for the suggested exemption for FINRA members. The scope of the proposed certification, however, is substantially similar to the FINRA requirement and, therefore, not of the greater breadth that BDA suggested. In its comment submitted to the SEC, BDA supports the MSRB's effort to ensure the self-certification aligns with FINRA Rule 3130, but again suggests the broader certification requirement. ICI supports the proposed annual certification requirement as drafted and its effect on business line responsibility (paragraph .08 of the Supplementary Material), as those provisions are consistent with requirements imposed on FINRA members pursuant to FINRA Rule 3130(b) and paragraph .07 of the Supplementary Material to that rule. Anonymous Attorney, who represents a municipal advisor that is also an investment adviser ("MA/IA Firm"), also supports the exception from the annual certification provision for municipal advisors that are subject to FINRA Rule 3130.

Sanchez questions the regulatory purpose and the additional benefit of an annual certification. Sanchez does not believe the annual certification would foster discussion between persons responsible for compliance matters and upper management, and he questions the necessity of such a provision for small municipal advisors, particularly sole-proprietors, in light

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6 MSA Professional Services, Inc., in response to the MSRB Request for Comment, also supported requiring such a self-certification.

of Section 15B(b)(2)(L)(iv) of the Securities Exchange Act of 1934 ("Exchange Act").[7] Sanchez also does not believe harmonization would be achieved by imposing an annual certification obligation similar to FINRA's requirement because the vast majority of registered municipal advisors are not FINRA members, and FINRA members would be specifically exempted from proposed Rule G-44(d).

In response to the comments, the MSRB believes that requiring the broader certification, as BDA suggests, would reduce the harmonization between the MSRB and FINRA certifications, which is an aspect of the proposal that BDA and ICI specifically support. The MSRB believes that a harmonization would be achieved in that municipal advisors, who are not registered broker-dealers with FINRA, would be subject to a similar annual certification requirement as those municipal advisors that are subject to the FINRA requirement and exempt from proposed Rule G-44(d). The MSRB also believes the certification requirement, as proposed, would result in the creation, maintenance and modification of robust written supervisory procedures that would promote compliance with all applicable rules. Therefore, the MSRB believes it would be an unnecessary burden, at this time, to require the broader certification BDA suggests regarding compliance with professional qualifications requirements and an ability and history of complying with requirements with which municipal advisors are already expected to comply.

In addition, the MSRB believes that requiring each firm's chief executive officer(s) ("CEO") (or equivalent officer(s)) to provide an annual certification would help ensure that compliance processes are given sufficient attention at the highest levels of management and would help promote compliance, without adding a significant burden. The MSRB believes the annual certification requirement will foster discussion between compliance personnel and upper management, as it creates accountability for, and incentivizes, the CEO(s) (or equivalent officer(s)) to ensure that the certification is truthful and otherwise satisfies proposed Rule G-44(d). While, as Sanchez notes, the benefit from certification of fostering discussion regarding compliance does not exist in sole proprietorships and perhaps not in some very small firms, the benefits from certification can extend beyond fostering such discussion. The MSRB believes the annual certification requirement would help ensure that municipal advisors have in place a compliance framework that would allow them to adapt compliance efforts to an evolving business and regulatory environment, and promote prompt maintenance and modification of compliance programs. Finally, the MSRB believes this requirement, as a part of proposed Rule G-44 with its multiple accommodations for small municipal advisors, is consistent with Section 15B(b)(2)(L)(iv) of the Exchange Act. While proposed Rule G-44(d) would affect small

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[7] 15 U.S.C. 78o-4(b)(2)(L)(iv). Section 15B(b)(2)(L)(iv) of the Exchange Act requires that rules adopted by the MSRB:

> 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.

municipal advisors, it would be a necessary and appropriate regulatory burden in order to promote compliance with all applicable rules by all municipal advisors, regardless of size.

Comparison to Rule G-27

Proposed Rule G-44 parallels the requirements of Rule G-27, on supervision for brokers, dealers and municipal securities dealers, where appropriate, and maintains differences from Rule G-27 to account for differences in the types of firms the two rules regulate. Sanchez believes the approach of proposed Rule G-44 is appropriate because it creates a dedicated supervision rule for municipal advisors, and SIFMA commends proposed Rule G-44 for being similarly robust to the requirements of Rule G-27. Sanchez, however, suggests replacing the current proposed timing standard for amending written supervisory procedures and communicating such amendments to associated persons (*i.e.*, "promptly") to the standard in Rule G-27(c)(iii) (*i.e.*, "as appropriate within a reasonable time after changes occur"). Sanchez believes the Rule G-27 standard is more reasonable and will be less confusing for entities that are registered as both broker-dealers and municipal advisors.

The provision requiring prompt amendments of written supervisory procedures and prompt communication of such amendments to associated persons is intended to harmonize proposed Rule G-44 with FINRA's rule on the maintenance of supervisory procedures in its consolidated supervision rule.[8] The SEC approved the same standards proposed here for amending procedures and communicating amendments in the FINRA supervision rulemaking matter on December 23, 2013.[9] The MSRB recognizes the proposed timing standards are different than those provided in the analogous provision in Rule G-27, and the MSRB may consider amending Rule G-27 in the future to harmonize it with proposed Rule G-44(a)(i) and the FINRA rule.

Outsourcing Chief Compliance Officer Function

Paragraph .05 of the Supplementary Material to proposed Rule G-44 provides that the chief compliance officer ("CCO") designated pursuant to proposed Rule G-44(c) can be either a principal of the firm or a person external to the firm. BDA reiterates its request that the language in paragraph .05, providing that a municipal advisor retains the ultimate responsibility for its compliance obligations, whether the CCO is outsourced or not, should be incorporated into the rule text, as it believes some firms will take a strict reading of the rule text without appropriately considering the Supplementary Material as a component of their compliance with proposed Rule G-44.

The Supplementary Material would be part of new Rule G-44, if approved, and the provision's location there is intended to improve the readability of the rule and does not affect

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8 *See* FINRA Rule 3110(b)(7).

9 *See* FINRA Rule 3110 Approval Order, *supra* note 5.

the weight, significance or enforceability of the provision. Therefore, the MSRB is not relocating the provision into the rule text in response to BDA's comment. BDA's comment that some firms would not appropriately consider the Supplementary Material when reading proposed Rule G-44 is speculative in nature and, if fully accepted, could suggest a need to remove all supplementary material from the rules of the MSRB and other regulatory organizations.

Bank Trust Departments and Trust Companies

In response to a previous comment from ABA, which proposed an exemption from the obligations in proposed Rule G-44 and the corresponding recordkeeping requirements for banks that certify they are subject to federal supervisory and compliance obligations, the MSRB added proposed Rule G-44(e), exempting federally-regulated banks accordingly. ABA reiterates its comment that the MSRB should consider the fiduciary regulatory regimes of state bank regulators applicable to bank trust departments and trust companies as grounds for a similar exemption.

The need for proposed Rule G-44 arises from the MSRB's regulatory oversight of municipal advisors as provided under the Dodd-Frank Wall Street Reform and Consumer Protection Act, which grants the MSRB broad rulemaking authority to develop a new, federal regulatory framework for municipal advisors. Therefore, the MSRB believes all municipal advisors should be required, at a minimum, to adhere to *federal* supervisory and compliance obligations that are substantially equivalent to those set forth in proposed Rule G-44, regardless of their other business activities and regulatory obligations. The ABA states that "many individual state banking regulators have adopted fiduciary regulations which are substantially based on OCC's rules,"[10] but the MSRB notes that, as ABA acknowledges, not all states have made that adoption and not all such state regulations are identical to the OCC's rules. Due to this lack of consistency between, and potential gaps in, state regulatory regimes, the MSRB is not extending the exemption of proposed Rule G-44(e) to bank trust departments or trust companies that are not federally regulated with regard to relevant activities.

Recordkeeping Requirements

The proposed amendments to Rules G-8 and G-9 are intended to make the recordkeeping requirements related to municipal advisors' supervisory and compliance obligations consistent with existing MSRB and SEC rules for similar records. SIFMA supports the proposed amendments, which it believes are reasonable and in line with existing MSRB recordkeeping and record retention requirements. Sanchez believes the extended six-year period of record retention for designation of supervisory persons and CCOs is an unnecessary complexity, and that it should be amended to impose a consistent five-year requirement for all records. Similarly, NAIPFA states that establishing a six-year retention requirement when other similar retention

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10 The Office of the Comptroller of the Currency ("OCC") requires national banks to comply with fiduciary regulations for all fiduciary clients, including municipal entities. *See* 12 CFR Part 9.

requirements are five years creates an inconsistent and overly complex regulatory regime, and requests that proposed Rule G-9 be amended to harmonize it with record retention requirements of Exchange Act Rule 15Ba1-8, relating to the "names of persons who are currently, or within the past five years were, associated with the municipal advisor."

As discussed in the Request for Comment, there is a six-year retention period for records relating to designations of persons responsible for supervision and as CCO to be consistent with the current provisions of Rule G-9 for records of similar designations by brokers, dealers and municipal securities dealers. This longer requirement is also supported by the importance of such records in ascertaining the identity of responsible persons during particular periods of time, including for purposes of examination and enforcement. The proposed amendments to Rules G-8 and G-9 would require the other records related to municipal advisor supervisory and compliance obligations to be preserved for five years to be consistent with the preservation requirements of Exchange Act Rule 15Ba1-8. Therefore, the MSRB is not proposing any revisions in response to the comments regarding the retention periods.

Requests for Clarification and Guidance

Anonymous Attorney seeks clarification on three issues: 1) whether an MA/IA Firm's compliance manual must have two separate sets of written supervisory procedures for municipal advisor and investment adviser activities, and, if so, whether it would be permissible to incorporate by reference applicable existing procedures that apply to investment adviser activities; 2) whether the annual review of the municipal advisor and investment adviser compliance processes may be conducted jointly; and 3) whether a principal, designated pursuant to proposed Rule G-44(a)(ii), may be designated by title or position, instead of as a specific individual, and, if so, whether it would be acceptable to identify a principal by reference to a separate document or record.

The primarily principles-based approach used in proposed Rule G-44, without such specific prescription by the MSRB, affords municipal advisors flexibility in determining the lowest-cost means to meet regulatory objectives. Accordingly, an MA/IA Firm could establish, and conduct its review of, written supervisory procedures and compliance policies, in the manner it deems best, and where requirements are substantially similar, referencing how the firm will comply with applicable municipal advisor and investment adviser standards may be appropriate. However, given that the regulatory regimes are not identical, separate written supervisory procedures for municipal advisors will need to exist. The flexibility of proposed Rule G-44 similarly extends to a firm's designation of the appropriate principal(s). In all cases, the written supervisory procedures and compliance policies, the review of those policies and procedures, and any designations of the appropriate principal(s) would be required to meet the minimum

standards of proposed Rule G-44 and the related recordkeeping requirements of proposed revised Rules G-8 and G-9.[11]

Implementation Date

The proposal sets forth an implementation period of six months[12] following the SEC's approval of the proposal, which the MSRB believes would provide sufficient time for municipal advisors to develop or modify supervisory systems and compliance processes. This general period meets SIFMA's request for no less than six months and is longer than NAIPFA's requested implementation period of at least ninety days from its effective date. BDA continues to believe the implementation of the proposal and all other municipal advisor rules should be delayed until six months after the SEC has approved all such rules and regulations.

As previously addressed, the MSRB does not intend to delay implementation of the proposal until all municipal advisor rules have been approved by the SEC. Municipal advisors are currently subject to a host of applicable federal securities laws, and the MSRB believes it is important for firms to have a supervisory system and compliance processes in place to foster compliance with those laws and that can be updated as new rules are adopted. Supervision and compliance functions are fundamental to preventing securities law violations from occurring and to promoting early detection and prompt remediation of violations when they do occur.

If you have any questions regarding this matter, please contact me or Carl Tugberk, Assistant General Counsel, at (703) 797-6600.

Sincerely,

Michael L. Post
Deputy General Counsel

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11 In addition to the comments discussed in this section, SIFMA and Anonymous Attorney suggest two technical amendments to rule cross-references in the proposal. The MSRB is filing with the SEC an amendment to the proposal to revise the rule text accordingly.

12 As explained in the proposal, the MSRB would require municipal advisors to comply with proposed Rule G-44(d), on annual certifications as to compliance processes, by a date eighteen months following SEC approval.