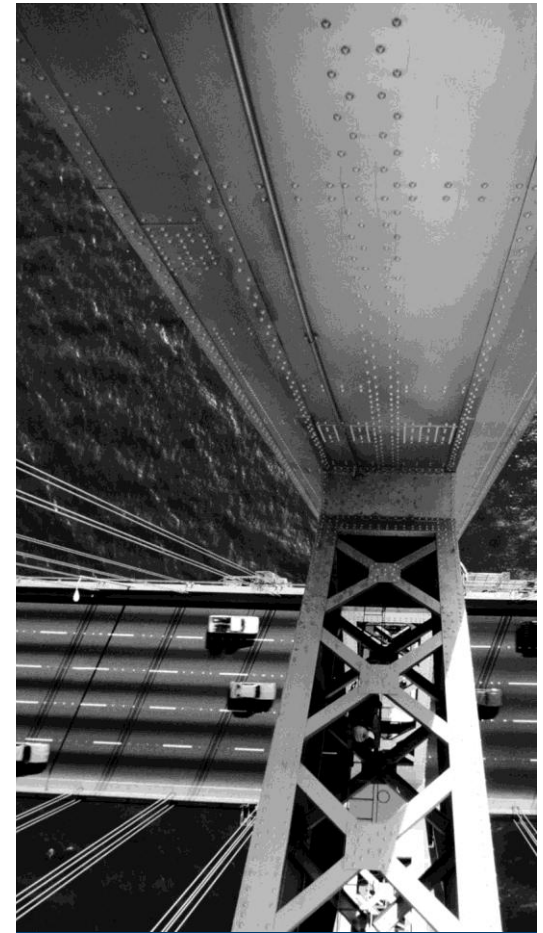


# MSRB Revised Draft Rule G-42: Duties of Non-Solicitor Municipal Advisors

Municipal Securities Rulemaking Board  
August 14, 2014



**MSRB**

Municipal Securities  
Rulemaking Board

# MSRB Presenters

**Ritta McLaughlin**

*Chief Education Officer*

**Michael L. Post**

*Deputy General Counsel*

# Today's Webinar Topics

- I. Overview
  - The Regulatory Framework
- II. Key Provisions of Revised Draft Rule G-42
  - Standards of Conduct
  - Disclosure of Conflicts of Interest
  - Documentation of the Relationship
  - Recommendations
  - Principal Transactions
  - Specified Prohibitions
  - Books and Records
  - Economic Considerations
- III. Participating in the Rulemaking Process
- IV. Questions and Answers

# About the MSRB



- A self-regulatory organization created by Congress in 1975
- Protects investors, municipal entities including issuers of municipal securities, obligated persons and the public interest
- Promotes a fair and efficient municipal market

# The Regulatory Framework



**MSRB**

Municipal Securities  
Rulemaking Board

# Background

- The 2010 passage of the Dodd-Frank Act expanded the MSRB's jurisdiction to include the regulation of municipal advisors and municipal advisory activities
  - Included a broad definition of municipal advisor
  - Deemed municipal advisors to owe a fiduciary duty to their municipal entity clients

## Background (cont.)

- In September 2013, the SEC promulgated a final registration rule (SEC Final Rule) which among other things:
  - Defined the categories and activities of persons deemed to be municipal advisors
  - Established a permanent registration regime
  - Established broad recordkeeping requirements for municipal advisors
  - Provided that the examination of municipal advisory firms would be conducted by SEC and FINRA
- Effective as of July 1, 2014

## Background (cont.)

- Congress granted the MSRB its rulemaking authority in the Securities Exchange Act of 1934, which was amended by the Dodd-Frank Act
- Under this authority, the MSRB previously amended MSRB Rule G-17 on fair dealing to provide that municipal advisors, in the conduct of their municipal advisory activities, must deal fairly with all persons and not engage in any deceptive, dishonest, or unfair practice



## Background (cont.)

- With the adoption of the SEC Final Rule, the MSRB has prioritized the development of municipal advisor rules in key areas:
  - Standards of conduct including fiduciary duty
  - Supervision
  - Pay-to-play
  - Gifts and gratuities
  - Duties of solicitors
- The MSRB is developing a professional qualification exam for all municipal advisor professionals to demonstrate minimum levels of competency

# The Request for Comment

- Initial MSRB Draft Rule G-42 request for comment period closed on March 10, 2014 (MSRB Notice 2014-01)
  - Forty-four comment letters received and taken into consideration
- Request for comment on Revised Draft Rule G-42 was published on July 23, 2014 (MSRB Notice 2014-12)
  - Comment period closes on August 25, 2014

# Submitting Comment Letters

- Public comment period ends August 25, 2014
- Submit comments electronically or by mail
- All comment letters received are published on the MSRB website

## Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors

### Overview

The Municipal Securities Rulemaking Board (MSRB) revised draft MSRB Rule G-42 on standards of conduct for municipal advisors when engaging in municipal advisory services, the undertaking of solicitations, and on associated recordkeeping amendments to MSRB Rules G-8, on books and records, and on the preservation of records (Revised Draft Rules). The Board is requesting comment on an initial draft Rule G-42 and initial draft Rules G-8 and G-9 (Initial Draft Rules). The Revised Draft Rules and modifications made to the Initial Draft Rules after the public comment period have ended.

### Requests for Comment

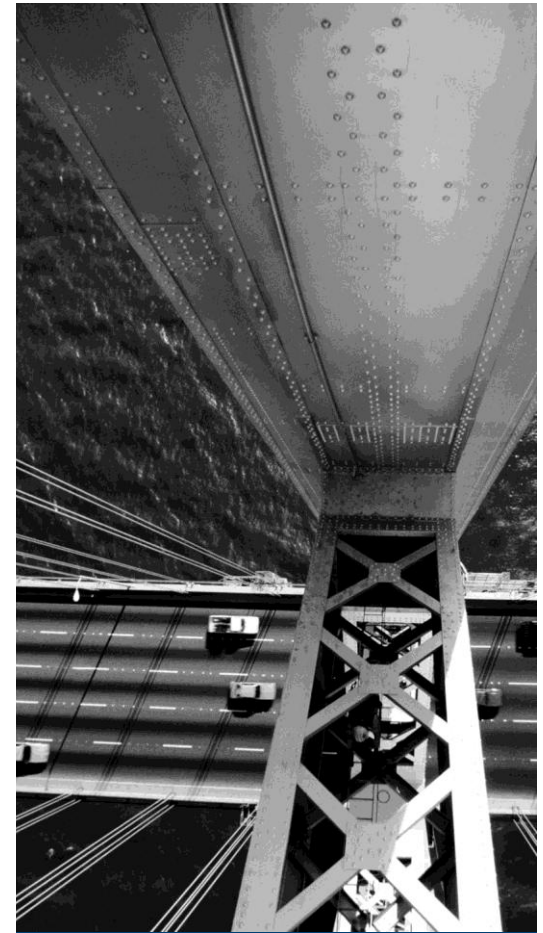
The MSRB requests comment from municipal market participants and the general public about rulemaking proposals. Current and past requests for comment are listed below.



Full Title	Comment	Publication Date	Notice Number	Comment Due by
Request for Comment on Revised Draft MSRB Rule G-42, on Duties of Non-Solicitor Municipal Advisors	<a href="#">Submit   View</a>	7/23/2014	2014-12	8/25/2014

Comments should be submitted no later than August 25, 2014, and may be submitted in electronic or paper form. [Comments may be submitted electronically by clicking here.](#) Comments submitted in paper form should

# Review of Initial Draft Rule G-42: Duties of Non-Solicitor Municipal Advisors



**MSRB**

Municipal Securities  
Rulemaking Board

# Scope of Initial Draft Rule G-42

- Duties and responsibilities of a non-solicitor municipal advisor engaging in municipal advisory activities
  - Standards of conduct
  - Disclosure of conflicts of interest
  - Documentation of the relationship
  - Recommendations
  - Principal transactions
  - Prohibitions related to compensation, fees and the retention of business
- Duties created by the Initial Draft Rule are in addition to fiduciary duties under state or other laws
- Duties of solicitors will be addressed in a separate rule

# Standards of Conduct



**MSRB**

Municipal Securities  
Rulemaking Board

# Initial Draft Rule: Standards of Conduct



- Each municipal advisor in the conduct of its municipal advisory activities:
  - For an obligated person client, is subject to a duty of care;
  - For a municipal entity client, is subject to a fiduciary duty, which includes, without limitation, a duty of care and a duty of loyalty

# Revised Draft Rule: Standards of Conduct



- Revised Draft Rule G-42 (a) has not been modified and continues to follow Dodd-Frank Act in deeming a municipal advisor to owe a fiduciary duty **only** to its municipal entity clients
- Revised Draft Rule retains the duty of care as the standard of conduct that would apply to municipal advisors whose clients are obligated persons

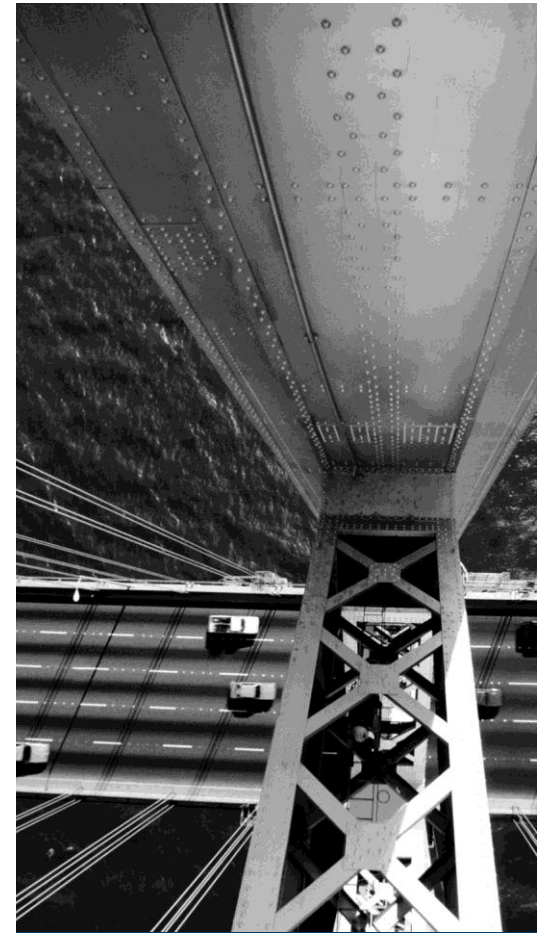


# Revised Draft Rule: Standards of Conduct Duty of Care and Duty of Loyalty



- Inquiry and Investigation
  - Supplementary Material .01 has removed the requirement to thoroughly review the official statement if engaged in connection with an issuance of municipal securities or a municipal financial product related to an issuance
  - Supplementary Material .02 has removed the requirement to investigate or consider other reasonably feasible alternatives to any recommended municipal securities transaction or financial product that might also or alternatively serve the municipal entity client's objectives.

# Disclosure of Conflicts of Interest and Other Information



**MSRB**

Municipal Securities  
Rulemaking Board

# Initial Draft Rule: Disclosure of Conflicts of Interest and Other Information



- Specified conflicts that must be disclosed include:
  - Advice, services or products provided by an affiliate of the municipal advisor if related to the municipal advisory activities
  - Payments to obtain or retain the client’s municipal advisory business
  - Payments received from third parties to enlist the municipal advisor’s recommendation of its services, any transaction or financial product
  - Fee-splitting arrangements with any provider of investments or services to the client

# Initial Draft Rule: Disclosure of Conflicts of Interest and Other Information (*continued*)



- Conflicts related to the form of compensation
- Information pertaining to the scope and amount of the municipal advisor's professional liability insurance, if carried
- Legal or disciplinary events that are material to the client's evaluation or disclosed on the Form MA or Forms MA-I filed with the SEC and provide the client with a copy of the relevant sections

# Revised Draft Rule: Conflicts of Interest and Other Information



- Disclosure of material conflicts of interest arising from compensation only when compensation is contingent on the size or closing of a transaction
- Advisor must affirmatively disclose that it has “no known” material conflicts of interest based on the exercise of reasonable diligence rather than a more categorical statement
- No requirement to disclose information on professional liability insurance
- Legal or disciplinary events that are material to the client’s evaluation or disclosed on the Form MA or Forms MA-I filed with the SEC and where the forms can be electronically accessed
- Date of the last material change to a legal or disciplinary event disclosure on any Form MA or Form MA-I filed with the SEC

# Revised Draft Rule: Conflicts of Interest and Other Information *(continued)*



- Supplementary Material .06 provides in the event that a municipal advisor inadvertently engages in municipal advisory activities and does not intend to continue or enter into a municipal advisory relationship, the advisor must be promptly provided a document that is dated and includes:
  - a disclaimer that the advisor did not intend to provide advice and that effective immediately, it has ceased engaging in municipal advisory activities;

# Revised Draft Rule: Conflicts of Interest and Other Information *(continued)*



- a notification that such municipal entity or obligated person should be aware that the disclosure of material conflicts of interest and other information as required by Rule G-42 has not been provided;
- a representation that the advisor, in good faith, has undertaken reasonable efforts to identify the advice that was inadvertently provided; and
- request confirmation that the municipal entity or obligated person received the documentation.

# Documentation of the Municipal Advisory Relationship



**MSRB**

Municipal Securities  
Rulemaking Board



# Initial Draft Rule: Documentation of the Relationship



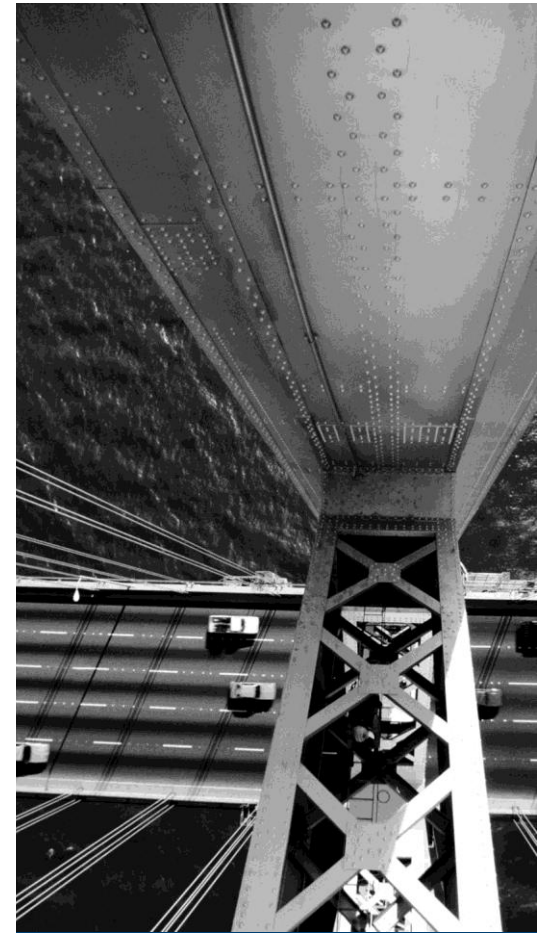
- Municipal advisors must evidence each of their municipal advisory relationships in writing prior to, upon or promptly after the inception of the relationship
- Initial Draft Rule G-42 required certain information to be documented, including:
  - Form and basis of compensation
  - Reasonably expected amount of compensation, if quantifiable
  - Required disclosures, including those relating to material conflicts of interest
  - Scope of the engagement
  - Any terms relating to the termination of the relationship
  - Specific undertakings if requested by the client with respect to the preparation and finalization of the official statement, if the municipal advisory activities relate to a new issue or reoffering

# Revised Draft Rule: Documentation of the Relationship



- Revised Draft Rule G-42 simplifies documentation:
  - Documentation of compensation only to include form and basis of direct and indirect compensation
  - No longer required to document reasonably expected amount of compensation
  - No longer required to detail specific undertakings if requested by the client with respect to the preparation and finalization of the official statement, if the municipal advisory activities relate to a new issue or reoffering
  - Documentation of the advisory relationship must be amended and supplemented only if there are material changes or additions.

# Recommendations



**MSRB**

Municipal Securities  
Rulemaking Board

# Initial Draft Rule: Recommendations Made by the Municipal Advisor



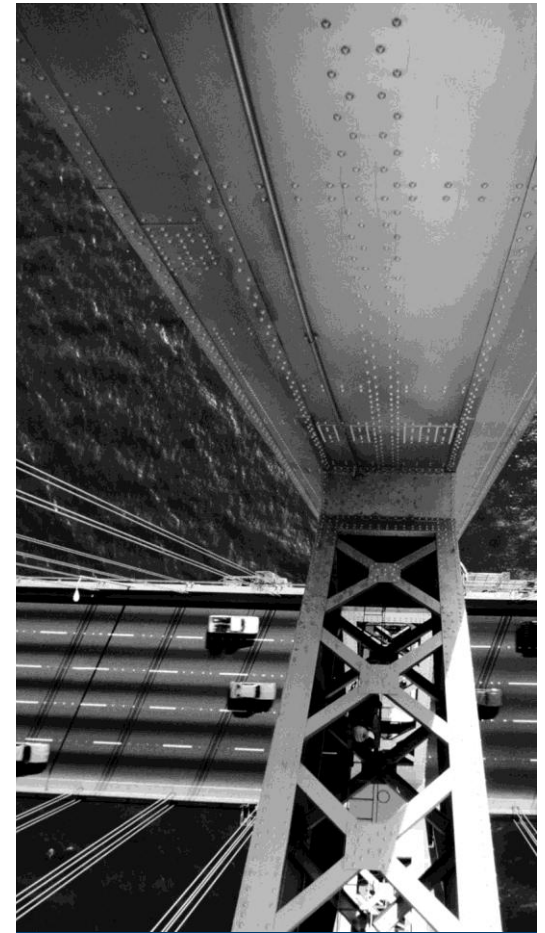
- Initial Draft Rule G-42 provided that:
  - A municipal advisor must have a reasonable basis to believe its recommendation is suitable for the clients
  - If the client is a municipal entity, the municipal advisor may only recommend a municipal securities transaction or municipal financial product that is in the client's best interest
  - A municipal advisor that has a duty of loyalty is required to investigate or consider other reasonably feasible alternatives
  - The advisor must discuss with the client information similar to that which would be required if the recommendation were made by the municipal advisor itself

# Revised Draft Rule: Recommendations Made by the Municipal Advisor or Third Party



- Revised Draft Rule G-42 merges provisions related to recommendations made by the advisor and the advisor's review of third-party recommendations:
  - Retains diligence standard for each kind of undertaking
  - Client retains control of scope of engagement
  - Municipal advisor must determine, based on the information obtained through reasonable diligence, whether a recommended transaction or financial product is suitable for the client

# Principal Transactions



**MSRB**

Municipal Securities  
Rulemaking Board

# Principal Transactions

- Revised Draft Rule G-42(e)(ii) clarifies and narrows the scope of the proposed prohibition of principal transactions:
  - Municipal advisor and its affiliates are prohibited from “engaging in a principal transaction” directly related to the same municipal transaction or municipal financial product as to which the municipal advisor is providing advice
  - No specific prohibition or disclosure and consent requirement in the Revised Draft Rule for a municipal advisor to an obligated person client

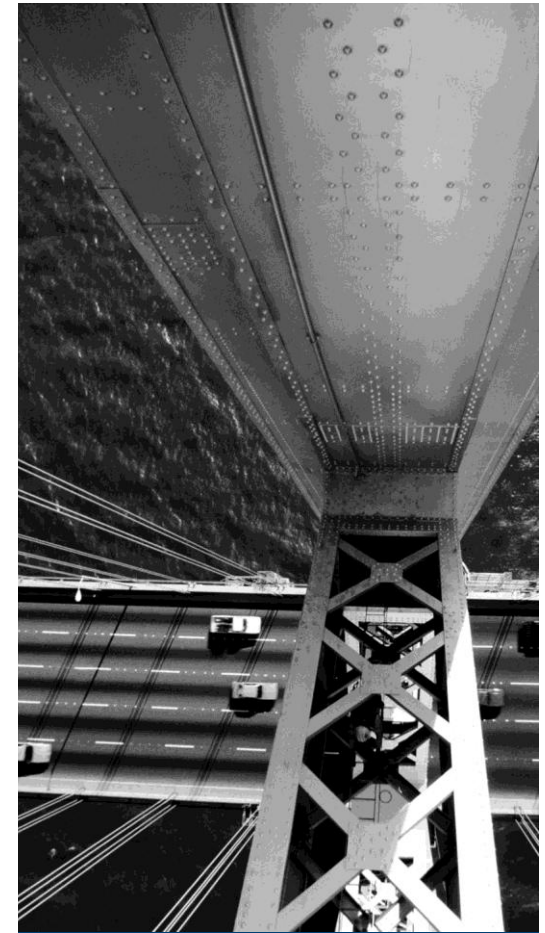
## Principal Transactions *(continued)*

- Revised Draft Rule G-42(f)(ii) provides a definition of the term “engaging in a principal transaction”:

“When acting as a principal for one’s own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client.”



# Specific Prohibitions Related to Compensation, Fees and the Retention of Business



**MSRB**

Municipal Securities  
Rulemaking Board

# Initial Draft Rule: Prohibited Conduct

- Excessive Compensation
- Fees
  - Fee-splitting with underwriters or undisclosed fee-splitting with providers of investments or services
  - Invoices that do not accurately reflect the service performed
- Other Conduct
  - Materially false or misleading representations to obtain or retain municipal advisory business
  - Payments to obtain or retain municipal advisory business other than reasonable fees paid to a registered municipal advisor

# Revised Draft Rule: Prohibited Conduct

- Supplemental Material .11 provides guidance on excessive compensation
  - Expertise
  - Complexity of transaction or product
  - Whether fee is contingent upon closing of transaction
  - Length of time spent on engagement
  - Whether advisor is paying other relevant costs related to transaction
- Revised Draft Rule unchanged from Initial Draft Rule with respect to fees
  - Invoices that do not accurately reflect the service performed
  - Fee-splitting with underwriters or undisclosed fee-splitting with providers of investments or services

# Definitions

- Definitions of “advice,” “municipal advisor,” “municipal entity” and “obligated person” have been modified in the Revised Draft Rule G-42(f) to specifically reference the applicable provisions of the SEC Final Rule

## Definitions (*continued*)

- Revised Draft Rule G-42 (f)(vi) clarifies when the municipal advisory relationship begins and ends
  - Exists when a municipal advisor engages in or enters into an agreement to engage in municipal advisory activities for or on behalf of a municipal entity or obligated person client
  
  - Ends on the date which is the earlier of the date on which:
    - the municipal advisory relationship has terminated pursuant to the terms of the documentation of the municipal advisory relationship

*or*

    - the municipal advisor withdraws from the municipal advisory relationship

# Revised Draft Rule: Application to Other Types of Municipal Securities



- The MSRB, at this juncture, does not intend to create an exemption for advisors of municipal entities regarding municipal fund securities

## Books and Records

- The Initial Draft amendments to MSRB Rules G-8 and G-9 would incorporate the record keeping requirements imposed by the SEC Final Rule
- These provisions are removed and the MSRB plans to include them in a separate rulemaking initiative

# Economic Analysis



**MSRB**

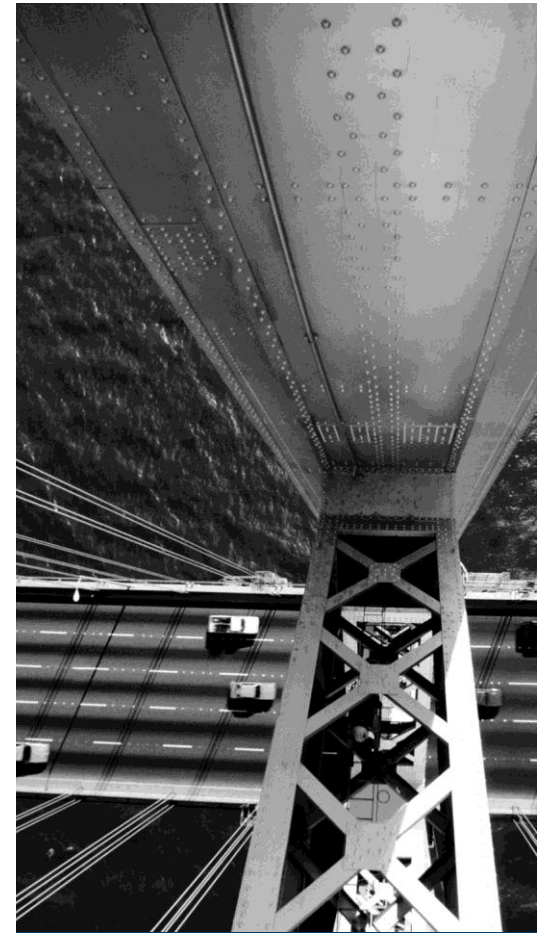
Municipal Securities  
Rulemaking Board



# Economic Analysis

- The Request for Comment on Revised Draft Rule G-42 incorporates the MSRB's preliminary economic analysis, including the following factors:
  - The need for the Draft Rule and how it meets the need
  - Relevant baselines against which the likely economic impact of elements of the Draft Rule can be considered
  - Reasonable alternative regulatory approaches
  - The potential benefits and costs of the Draft Rule and the main alternative regulatory approaches

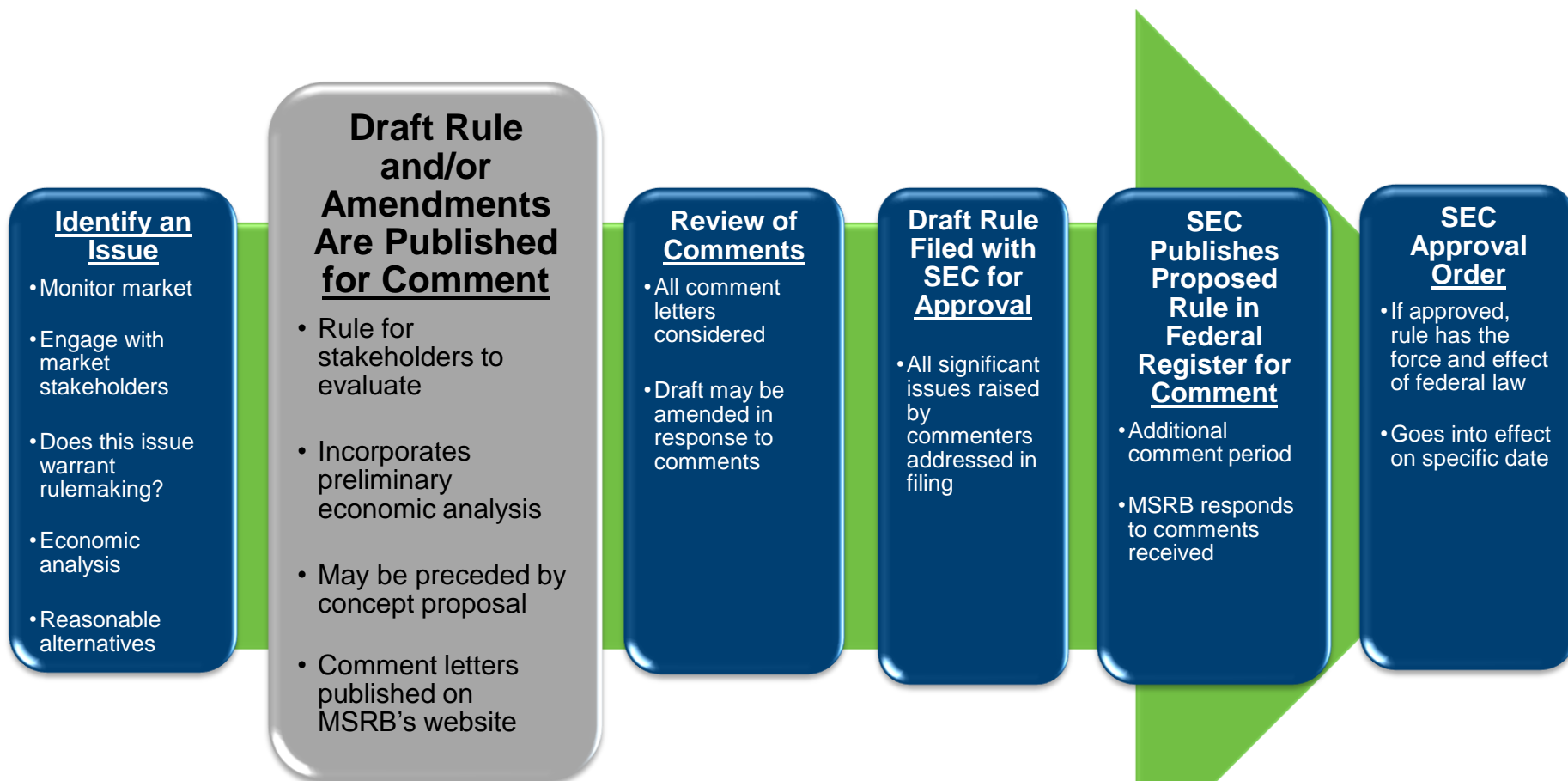
# Participation in the Rulemaking Process



**MSRB**

Municipal Securities  
Rulemaking Board

# MSRB Rulemaking Process



# MSRB Revised Draft Rule G-42: Duties of Non-Solicitor Municipal Advisors



- Review MSRB resources for municipal advisors
- View previous comment letters on the Request for Comment page
- Submit comments no later than August 25, 2014

MUNICIPAL ADVISOR RESOURCE

MUNICIPAL ADVISOR RESOURCE

PRE

PRE

MSRB  
Municipal Securities Rulemaking Board

Login About MSRB Publications Careers Email Updates Contact Us Systems Status File a Complaint

Search  
Advanced Search

Municipal Bond Market Rules Disclosures and Data Market Leadership News, Events and Training Resources for...

Home > Municipal Advisors > News and Resources

Print PDF Email Share

News and Resources for Municipal Advisors

**Advancing Municipal Advisor Regulation**  
The MSRB is advancing a regulatory framework for municipal advisors that includes rules for professional conduct, professional qualification examination requirements as well as education and outreach to municipal advisors. In light of the September 18, 2013 final registration rule from the Securities and Exchange Commission (SEC) defining who is a municipal advisor, which takes effect January 13, 2014, the MSRB has prioritized the development of municipal advisor rules in five key areas. They are:

- Standards of conduct of municipal advisors (*Rule proposed January 9, 2014*)
- Supervision requirements for municipal advisory firms and their employees
- Rules to address the potential for pay-to-play activities by municipal advisors
- Limitations on gifts and gratuities to employees of municipal securities issuers and other market participants
- Duties of solicitors

The MSRB will seek public comment before proposing rules to the SEC for approval. The MSRB will also continue to work with the municipal advisory industry to develop a professional qualification exam to establish standards of competency for municipal advisors. Resources and educational materials will be added to the MSRB's website as the municipal advisor regulatory framework develops.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 expanded the MSRB's jurisdiction to include the regulation of municipal advisors. Dodd-Frank amended Section 15B of the Securities Exchange Act. Read the Exchange Act's main municipal provisions.

**Municipal Advisor Registration**  
Any municipal advisor that has engaged in municipal advisory activities after December 31, 2010 is required to be registered first with the SEC, and then with the MSRB. Learn more about the MSRB's online registration process. Financial professionals and others who want to learn whether they are engaged in such activities and/or whether they are exempt from the permanent registration requirement should review the SEC's final rule for municipal advisors. A current list of municipal advisors registered with the MSRB is available here.

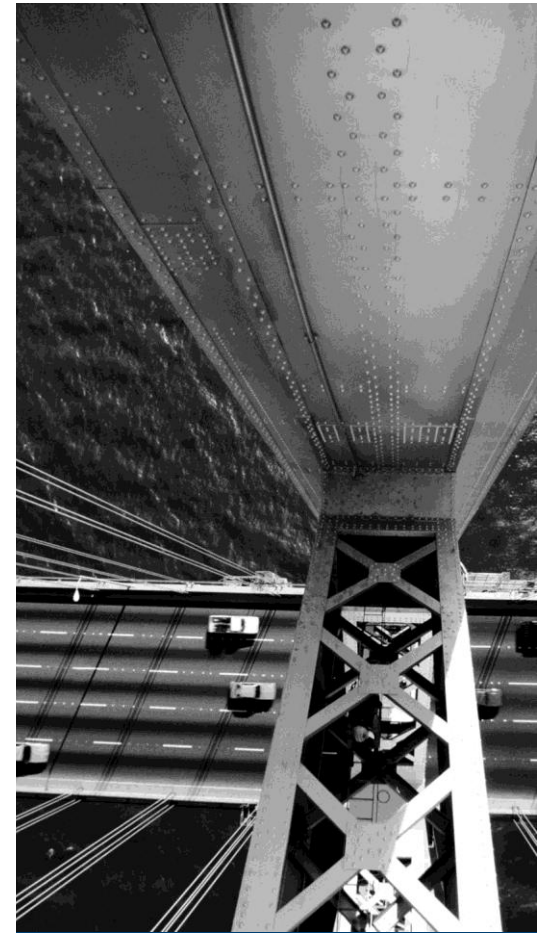
**Municipal Advisor Qualifications**

**Municipal Advisor Review**  
Read the MSRB's quarterly newsletter for municipal advisors.  
Winter 2013 Issue  
Sign up to receive municipal advisor education news.

**Preparing for Regulation**  
This publication can help newly registered municipal advisors understand what it means to be regulated and to prepare.

**Participating in the Rulemaking Process**  
This publication can assist municipal advisors in actively participating in the MSRB's rulemaking process.

# Question and Answer



**MSRB**

Municipal Securities  
Rulemaking Board

# Contact the MSRB

## MSRB Online

[msrb.org](http://msrb.org)

[emma.msrb.org](http://emma.msrb.org)

## MSRB Support

703-797-6668

*Hours of Operation:*

*7:30 a.m. - 6:30 p.m. ET*

## Follow the MSRB on Twitter

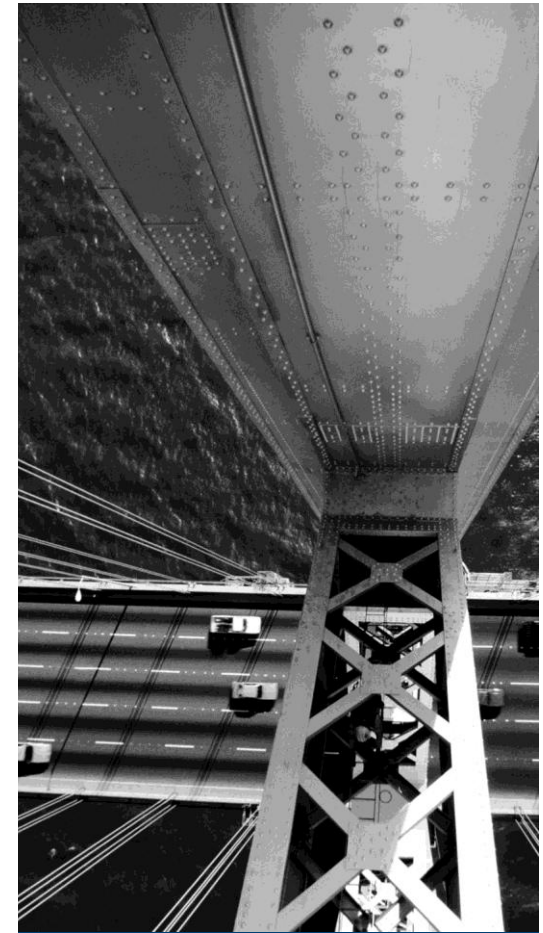
@MSRB\_News

## MSRB Email Updates

Subscribe at [msrb.org](http://msrb.org)

# MSRB Revised Draft Rule G-42: Duties of Non-Solicitor Municipal Advisors

Municipal Securities Rulemaking Board  
August 14, 2014



**MSRB**

Municipal Securities  
Rulemaking Board