MUNICIPAL REGULATORY CONSULTING

telephone | 609.903.1110 fax | 609.936.0068
email | david@muniregconsulting.com

6 Almond Court, West Windsor, New Jersey 08550
www.muniregconsulting.com

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

April 1, 2011

Sent via email to CommentLetters@msrb.org

Re: MSRB Notice No. 2011-16

Dear Mr. Smith:

Thank you for the opportunity to comment on proposed amendments to MSRB Rule G-20. 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 about how to apply those rules in the context of their business.

Among the questions I am sometimes asked is whether there is any guidance now (or proposed to be) applicable to municipal advisors that tells them how they (or even if they) should look at charitable and similar contributions. Because there is nothing directly on point, I propose that the MSRB speak directly to the issue by either incorporating into Rule G-20 itself or in guidance applicable to either Rule G-20 or to Rule G-17 that charitable contributions are not gifts for purposes of Rule G-20 or are not covered by Rule G-20 because Rule G-20 covers only gifts to natural persons. Furthermore, the MSRB should directly acknowledge that there is FINRA guidance with respect to charitable contributions and either adopt it, modify it or state that it is not applicable to charitable and similar contributions for purposes of Rule G-20 or Rule G-17.

## Discussion

### 1. Application of Existing Guidance Under Rule G-20

Proposed Rule G-20 would extend to municipal advisors the gift ban that has been applicable to dealer firms, but the MSRB uses different language than that which applies to dealers. The applicable provision reads:

> *No municipal advisor shall, directly or indirectly, give or permit to be given any thing or service of value, including gratuities, in excess of $100 per year to a person other than an employee or partner of such municipal advisor, if such payments or services are in relation to the municipal advisory activities of (including but not limited to solicitation of potential engagements on behalf of) the municipal advisor.*

Nothing in the existing or amended rule or in the proposing release mentions charitable contributions nor are they addressed directly in any interpretation. Accordingly, one could interpret the Rule to prohibit a municipal advisor from making a charitable contribution to, *e.g.*,

the United Way, that was solicited by the Mayor of a town with which the advisor is seeking to do municipal advisory business on the grounds that it qualifies as "payment . . . in relation to the municipal advisory activities . . . of the municipal advisor."

However, MSRB guidance dating back to 1980 appears to resolve the issue by differentiating gifts to natural persons from gifts to entities.

> *"Person." Your letter regarding rule G-20 has been referred to me. Rule G-20 prohibits a municipal securities professional from giving gifts or providing services to a person in relation to the municipal securities activities of such person's employer, in excess of a specified amount.*
>
> *In your letter, you inquire whether the term "person" in rule G-20 is intended to include "a 'corporate' person as well as a 'real' person." As used in the rule, the term "person" refers only to a natural person. The rule is intended to discourage municipal securities professionals from attempting to induce individual employees from acting in a manner inconsistent with their obligations to, or contrary to the interests of, their employers. MSRB interpretation of March 19, 1980.*

The idea, apparently, is that dealers should not be giving gifts to, for example, the portfolio manager of an institutional investor for fear that it would influence the PM's buying decisions when those decisions ought to be based solely on what is best for the institutional account. Based upon this guidance, it appears that the payment to which I referred in the example set forth above would not qualify as a gift because it was made to an entity (the United Way) and not to an individual. However, because the rationale, *i.e.,* "intended to discourage . . . employees from acting in a manner inconsistent with their obligations to . . . their employers," does not really apply in the context of charitable contributions, the issue is not entirely free from doubt.

For the same reason, contributions or payments to quasi-public but not charitable entities solicited by issuer officials or persons on the board of or employed by an obligated person might raise concerns. For example, an issuer official might solicit a contribution to an association of similar officials, such as a state association of school administrators or a state association of county treasurers. Or the CFO of an obligated person hospital who is also on board of the local Chamber of Commerce might solicit a contribution to support a golf tournament to benefit the town's Little League. In all of these or any number of similar situations, there is the potential that paying – or not paying – could influence (or be perceived to influence) a business decision that is supposed to be based solely on merit.

### 2. Application of Existing FINRA Guidance

When the MSRB proposed amending Rule G-20 in 2005, in its proposing submission to the SEC it said

> *the MSRB intends generally that the provisions of Rule G-20 be read consistently with the analogous NASD provisions, unless the MSRB specifically indicates otherwise. Thus, relevant NASD interpretations would be presumed to apply to the comparable MSRB provision, subject to the MSRB's right to make distinctions when necessary and*

*appropriate in the context of municipal fund securities and other primary offerings of municipal securities.*

The NASD and NYSE (now FINRA) jointly issued Notice to Members 06-21 (the "Notice") in May 2006. The Notice addressed the "solicitation of substantial charitable contributions by employees or agents of a customer acting in a fiduciary capacity" and noted that such solicitation "raises potential conflicts of interest that deserve careful consideration by members." The Notice goes on to suggest "some of the policies and procedures that firms should consider adopting to address these conflicts."

By its terms, the Notice clearly does not apply to municipal advisors who are not FINRA members, nor does it refer to or purport to be an interpretation of any existing NYSE, NASD or other rule. Accordingly, the Notice does not seem to qualify as an interpretation of an analogous SRO rule that might apply to Rule G-20 and therefore does not nor or would not apply to municipal advisors.[1]

### 3. Need for Specific Guidance

I believe the better argument based on the existing guidance is that charitable contributions - even those that appear on their face to be related to the "municipal advisory activities" of a municipal advisor - would not be considered to be gifts for purposes of Rule G-20 because they are not given to natural persons. I also believe that is the correct result even if the stated rationale for drawing the natural person/corporate entity distinction does not really apply. Charitable contributions are simply not gifts just as they are not political contributions for purposes of Rule G-37.[2]

What is unclear is if certain charitable (or similar) contributions – or the circumstances giving rise to them – might constitute an unfair practice and thereby cause the advisor making the contribution to violate Rule G-17. Indeed, even before the MSRB issued specific guidance with regard to certain practices relating to the entertainment of municipal officials, firms were cited for violating either or both of Rules G-20 and G-17 for practices not specifically prohibited by either Rule.[3]

There is no need or reason for any uncertainty in this area. Given the potential that all parties subject to MSRB rules might find that making these payments could subject them to liability for violating the fair dealing standards of Rule G-17, and given that these situations arise routinely in the normal course of business, the MSRB should provide clear guidance to the industry so that all parties know what they may or may not do.

---

[1] Compare with NASD Guidance on Rule 3060, specifically cited by the MSRB and made applicable to Rule G-20 in January 2007. http://www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-20.aspx?tab=2

[2] The MSRB has already made clear that charitable contributions are not political contributions for purposes of Rule G-37. See Q&A IV.5, May 1994.

[3] See fn 1, and cases cited therein.

**Conclusion**

The Board should state as clearly as it did in the context of Rule G-37 that charitable contributions are not gifts for purposes of Rule G-20, and should provide guidance on when and under what circumstances charitable contributions or contributions/payments solicited by issuer officials are or might be a violation of Rule G-17. It can do this either by reference to the existing FINRA guidance, or by issuing guidance of its own under Rule G-20 or under Rule G-17. This guidance should be issued for comment, so that not only dealers and advisors, but charities and issuers, have the opportunity to weigh in on the potential ramifications of any decision that would limit these contributions.

Thank you again for the opportunity to address this issue. If you have any questions, I will be happy to expand upon or clarify my comments.

Very truly yours,

David Levy, Principal