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Invested in America

September 11, 2015

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: File Number SR-MSRB-2015-03:

Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change Consisting of Proposed New Rule G-42, on Duties of Non-Solicitor Municipal Advisors, and Proposed Amendments to Rule G-8, on Books and Records to be Made by Brokers, Dealers, Municipal Securities Dealers, and Municipal Advisors

Notice of Filing of Amendment No. 1 to Proposed Rule Change Consisting of Proposed New Rule G-42, on Duties of Non-Solicitor Municipal Advisors, and Proposed Amendments to Rule G-8, on Books and Records to be Made by Brokers, Dealers, Municipal Securities Dealers, and Municipal Advisors

Dear Mr. Fields:

The Securities Industry and Financial Markets Association ("**SIFMA**")[1] appreciates the opportunity to provide further comments to the Securities and Exchange Commission (the "**SEC**") in connection with Municipal Securities Rulemaking Board ("**MSRB**") Proposed Rule G-42 ("**Proposed Rule G-42**"), and in particular, in response to (i) the SEC's Order Instituting Proceedings to Determine Whether to Approve or Disapprove Proposed Rule G-42 (the "**OIP**");[2] (ii) the MSRB's Amendment No. 1 to

[1] SIFMA is the voice of the U.S. securities industry, representing the broker-dealers, banks and asset managers whose 889,000 employees provide access to the capital markets, raising over $2.4 trillion for businesses and municipalities in the U.S., serving clients with over $16 trillion in assets and managing more than $62 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, DC, is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

[2] Exchange Act Release No. 75628 (Aug. 6, 2015).

Proposed Rule G-42 ("**Amendment No. 1**");[3] and (iii) the MSRB's letter to the SEC in response to comments on Proposed Rule G-42.[4]

While SIFMA believes the MSRB has made important strides in making Proposed Rule G-42 workable since its original draft proposal,[5] there are significant outstanding issues that would need to be amended or clarified before Proposed Rule G-42 would meet the standards for MSRB rulemaking under the Securities Exchange Act of 1934 (the "**Exchange Act**"). In light of this, SIFMA urges the SEC to disapprove Proposed Rule G-42 as it has currently been proposed.

SIFMA commented in detail on the Proposed Rule G-42 as originally filed with the SEC, as well as on prior drafts of the rule.[6] Although the MSRB proposed minor revisions to Proposed Rule G-42 in Amendment No. 1, these changes do not address the vast majority of SIFMA's previously stated objections, or those of other commenters. SIFMA continues to have significant concerns regarding certain aspects of Proposed Rule G-42, which render it unreasonably burdensome and anti-competitive in ways that do not clearly promote the fundamental policies of the municipal advisor provisions of the Exchange Act. As such, Proposed Rule G-42, as currently drafted, continues to be inconsistent with the standards for MSRB rulemaking under Sections 15B(b)(2)(C) or (L) and fails to meet the standards for SEC approval under Section 3(f) of the Exchange Act.[7]

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[3] Exchange Act Release No. 75737 (Aug. 19, 2015).

[4] Letter from Michael L. Post, MSRB, to Secretary, SEC (Aug. 12, 2015) (the "**MSRB Response Letter**"), *available at* www.sec.gov/comments/sr-msrb-2015-03/msrb201503-19.pdf.

[5] *See* MSRB Regulatory Notice 2014-01.

[6] *See* Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA, to Brent J. Fields, SEC (May 28, 2015), *available at* www.sifma.org/issues/item.aspx?id=8589954935 (the "**SIFMA May 2015 Letter**"); Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA, to Ronald W. Smith, MSRB (Aug. 25, 2014), *available at* www.sifma.org/issues/item.aspx?id=8589950587; Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA, to Ronald W. Smith, MSRB (Mar. 10, 2014), *available at* www.sifma.org/issues/item.aspx?id=8589947958.

[7] Section 15B(b)(2)(C) of the Exchange Act requires that the MSRB's rules, among other things, be designed "to protect investors, municipal entities, obligated persons, and the public interest; and not be designed to permit unfair discrimination among customers, municipal entities, obligated persons, municipal securities brokers, municipal securities dealers, or municipal advisors … or to impose any burden on competition not necessary or appropriate in furtherance of the purposes of" the Exchange Act. Section 15B(b)(2)(L) of the Exchange Act further requires that the MSRB's rules**,** among other things, "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." In addition, under Section 3(f) of the Exchange Act, whenever the SEC is engaged in the review of a rule of a self-regulatory organization and "is required to consider or determine whether an action is necessary or appropriate in the public interest," the SEC must consider "whether the action will promote efficiency, competition, and capital formation." Therefore, because the SEC must consider whether Proposed Rule G-42 is "necessary or appropriate in the public interest" under (…continued)

The MSRB Response Letter, while purporting to respond to commenters, in most regards simply dismissed commenters' concerns with conclusory and superficial responses that simply restate the MSRB's view that the particular provision is appropriate, without addressing the substance – or whether the provision in question is "reasonably designed" to achieve its objectives or operate in the public interest, in accordance with the applicable statutory requirements cited above. Unfortunately, the MSRB does not appear to have taken seriously the significant issues that SIFMA and others have raised, including the fact that Proposed Rule G-42 would impose significant and unnecessary costs and burdens on many small and mid-size municipal entities who will lose access to critical financial services. Further, while at times offering its view that "the potential benefits provided to municipal entities" of a particular requirement "will outweigh the costs,"[8] the MSRB has neglected to attempt to quantify those costs and burdens, in direct conflict with the MSRB's own policy.[9] Indeed, SIFMA members have already heard municipal entities report that they are unable to find providers willing to perform certain services, in anticipation of Proposed Rule G-42 being adopted.

SIFMA renews and reasserts the comments contained in the SIFMA May 2015 Letter, and wishes to highlight, in particular, its most pressing concerns in Part I below.[10] In Part II below, SIFMA raises some additional comments based upon its members' experience to date in connection with developing policies and procedures to implement

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Section 15B(b)(2)(L), it must also consider whether the rule will "promote efficiency, competition and capital formation" as required under Section 3(f).

[8] MSRB Response Letter at 14.

[9] *See* MSRB, Policy on the Use of Economic Analysis in MSRB Rulemaking, *available at* www.msrb.org/About-MSRB/Financial-and-Other-Information/Financial-Policies/Economic-Analysis-Policy.aspx (incorporating the SEC's policy that "stresses the need to attempt to quantify anticipated costs and benefits even where the available data is imperfect").

[10] Although the comments provided in Part I, below, represent SIFMA's most pressing concerns in the SIFMA May 2015 Letter, SIFMA wishes to reiterate its other comments from the SIFMA May 2015 Letter, which include: (i) the proposed principal transaction ban should not treat investment funds advised by a municipal advisor (or its affiliates) as being affiliates of the municipal advisor, and therefore subject to Proposed Rule G-42, solely as a result of the investment advisory relationship; (ii) the proposed principal transaction ban should have a clear end date that is defined by or in relation to the termination or completion of the municipal advisory relationship that gave rise to the ban; (iii) the proposed safe harbor for inadvertent advice in Supplementary Material .07 should be expanded to provide an exception from the principal transaction ban and certain other requirements under Proposed Rule G-42 if the proposed conditions are satisfied; (iv) the MSRB should clarify the duties of a municipal advisor to a municipal entity by eliminating the phrases "includes, but is not limited to" and "without regard to the financial or other interests of the municipal advisor" in Supplementary Material .02; and (v) the disclosure and documentation standards in Proposed Rule G-42(b) and (c) should not apply to municipal advisory engagements that are in effect as of the compliance date for Proposed Rule G-42, and municipal advisors should not be obliged to provide new disclosures or additional relationship documentation to supplement or modify the terms of engagements that exist at that time.

applicable requirements for municipal advisors and with FINRA examinations. In Part III below, SIFMA addresses a specific concern with an additional requirement that the MSRB has introduced in Amendment No. 1. In Part IV below, SIFMA reiterates its concern that Proposed Rule G-42 is inconsistent with statutory standards.

I. Critical Issues with Proposed Rule G-42 Still Unresolved

A. Principal Transaction Ban

The proposed principal transaction ban in Proposed Rule G-42(e)(ii) is more restrictive and inflexible than fiduciary obligations under any other financial regulatory regime, seemingly reflecting the MSRB's view of municipal entities as less capable of evaluating and consenting to fully and fairly disclosed conflicts of interest than Congress and the SEC have viewed, by way of example, retail investors under the Investment Advisers Act of 1940 (the "**Advisers Act**").[11] But in the name of protecting municipal entities from self-dealing abuses,[12] the MSRB is setting up an unworkable and inefficient structure, particularly with respect to municipal advisors that also are registered as broker-dealers that provide incidental advice in connection with securities execution services.

The MSRB also has failed to seriously consider various suggested alternatives to temper the negative impact of the proposed ban, including by (i) limiting its scope to principal transactions that are directly related to the *advice* provided by the municipal advisor, and not more broadly to municipal securities *transactions or municipal financial products* as to which the municipal advisor is providing or has provided advice; (ii) limiting the application of the ban on business units and affiliates of a municipal advisor that have no knowledge of the municipal advisory engagement;[13] or (iii) permitting a

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[11] Indeed, in analyzing another potential fiduciary duty that may be imposed under the Dodd-Frank Act, the SEC staff itself recommended permitting broker-dealers subject to a fiduciary duty to engage in principal transactions—subject to conflicts disclosure and consent, along with existing obligations relating to suitability, best execution, and fair and reasonable pricing and compensation—rather than a complete ban on principal dealing. See SEC Staff Study on Investment Advisers and Broker-Dealers (Jan. 2011) at 120 (SEC Staff report pursuant to Section 913 of the Dodd-Frank Act on whether to implement a uniform fiduciary standard for broker-dealers and investment advisers providing personalized investment advice about securities to retail investors).

[12] *See* MSRB Response Letter at 12.

[13] The MSRB again declined to add a knowledge qualifier to the principal transaction ban, on the basis that such a qualifier would be "overly stringent, which could hinder regulatory examinations and enforcement." MSRB Response Letter at 16. SIFMA strongly disagrees; Congress, the SEC and self-regulatory organizations routinely adopt exclusions from substantive requirements for business units of regulated entities or their affiliates that are not involved in, or structurally isolated from, regulated activity. *See, e.g.,* Regulation AC Rule 501(b) (exempting a broker-dealer from the requirements under Regulation AC if it publishes, circulates or provides a research report prepared by a third party research analyst provided that, among other things, the employer of the third party research analyst has no employees in common with the broker-dealer and the broker-dealer maintains and enforces certain policies and (…continued)

principal transaction where the municipal entity is otherwise represented with respect to the principal transaction by another separate registered municipal advisor (an "**SRMA**").

With respect to the SRMA exemption to the principal transaction ban,[14] SIFMA suggested that—consistent with the SEC's view in adopting a parallel exemption from being obliged to register as a municipal advisor where a municipal entity is represented by an independent registered municipal advisor and subject to similar conditions—a municipal entity would be protected from the risk of potential self-dealing where the municipal entity has engaged and will rely on the advice of the SRMA.[15] Nonetheless, the MSRB declined to adopt such an exemption on the basis that such exception likely would be "complex and potentially burdensome to administer" because it would require "a number of conditions" to be imposed, such as "substantial additional relationship documentation."[16] SIFMA strongly disagrees. The SEC did not believe the independent registered municipal advisor exemption would be too "complex and potentially burdensome to administer," and if a municipal advisor believed that exchanging "substantial additional relationship documentation" would outweigh the benefits of the exemption, it could elect to be subject to the principal transaction ban and not rely on the SRMA exemption.

B. Advice Incidental to Brokerage/Securities Execution Services

The MSRB has crafted Proposed Rule G-42 on a "one-size fits all" basis, generally applying the same standards and obligations to all "municipal advisory activities," regardless of the context of the advice. SIFMA acknowledges that a person is a "municipal advisor" whether it advises a municipal entity on a large issuance of municipal securities or it provides brokerage with sporadic incidental advice on the

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procedures to ensure separateness); Regulation M Rule 105(b) (permitting a person under Regulation M to purchase offered securities in an account where there was a short sale in another related account during the restricted period if, among other things, decisions are made separately and without any coordination of trading or cooperation among or between the accounts and there are information barriers separating the accounts); Regulation SHO Rule 200(f) (exempting a broker-dealer from aggregating all of its positions in a security for order marking purposes under Regulation SHO if it qualifies for independent trading unit aggregation based on its separateness from other trading units); NASDAQ Options Market Rules Ch. VII, Sec. 10(b) (permitting market makers to engage in certain other business activities as long as there are information barriers between the market making activities and other business activities and appropriate procedures are in place).

[14] *See* SIFMA May 2015 Letter at 10.

[15] *See* Registration of Municipal Advisors, Exchange Act Release No. 70462 (Sept. 20, 2013) at 15 ("[t]he Commission believes that if a municipal entity or obligated person is represented by a registered municipal advisor, parties to the municipal securities transaction and others who are not registered municipal advisors should be able to provide advice to such municipal entity or obligated person, so long as the responsibilities of each of the parties are clear").

[16] MSRB Response Letter at 20-21.

investment of the proceeds of a previous issuance. However, while the MSRB indicated that it was not persuaded as to "why municipal advisory activities provided in the context of a brokerage relationship differ qualitatively from other municipal advisory activities,"[17] the scope, extent, risks, formalities, and conflicts present in these relationships differ fundamentally. In particular, a municipal entity or obligated person may call upon their broker-dealer for incidental investment advice in connection with the execution of many small investments, with the risk to the municipal entity flowing from any particular piece of advice being significantly less than that arising from advice in the issuance context. The application of the extensive documentation requirements—on a per transaction basis—is entirely impractical in the brokerage context where municipal entities request advice on many small transactions. The effect of requiring it will be that brokers, even those otherwise willing to register as a municipal advisor and be subject to a fiduciary duty, will either (i) decline to offer advice on the investment of municipal bond proceeds because of the practical impossibility of complying with Proposed Rule G-42 or (ii) be unable to provide such advice in a timely manner due to the obligation to prepare significant disclosure and relationship documentation on a per-transaction basis.

Moreover, a number of proposed requirements in Proposed Rule G-42 (such as the extensive documentation requirements) are highly impractical in the context of ordinary securities or brokerage/securities execution services relationships, where a certain amount of discussion takes place between a broker and his or her clients that may amount to "advice." If the principal transaction ban were to extend to this type of informal advice, the ban would potentially exclude or limit the possibility of municipal advisors engaging as principal in securities transactions with municipal entity customers unless the municipal advisor refrained from providing any such informal advice or execution is effected on an agency basis. Since nearly all transactions in fixed-income securities are effected on a principal basis, the problem is particularly acute with respect to that market – a fact explicitly recognized by the SEC when it promulgated a temporary rule to permit broker-dealers that have non-discretionary advisory accounts to engage in principal transactions in certain fixed-income securities,[18] as well as by the Department of Labor ("**DOL**") in its recent proposal of new fiduciary standards for investment advice provided to employee benefit plans or individual retirement accounts.[19]

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[17] MSRB Response Letter at 14.

[18] *See* Advisers Act Rule 206(3)-3T; Temporary Rule Regarding Principal Trades with Certain Advisory Clients, Advisers Act Release No. 2653 (Sept. 24, 2007) (noting, in particular, the fact that fixed-income securities are generally "traded by firms on a principal basis" was one of the factors that led to the promulgation of this rule). *See* Advisers Act Release No. 2653 at 36-38.

[19] *See* DOL, Proposed Class Exemption for Principal Transactions in Certain Debt Securities between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs, 80 Fed. Reg. 21989, 21993 (Apr. 20, 2015) (recognizing that "certain investment advice fiduciaries view the ability to execute principal transactions as integral to the economically efficient distribution of fixed income securities").

Further, while municipal entities often hire third-party advisors in connection with the issuance of municipal securities, many do not do so in connection with their ongoing management of the investment of proceeds. The Government Finance Officers Association ("**GFOA**"), representing the views of municipal entities' finance officers, warned the MSRB that applying the principal transaction ban to the advice incidental to the brokerage context "could force small governments to open a more expensive fee-based arrangement with an investment advisor in order to receive this very limited type of advice on investments that are not risky."[20] Incredibly, without serious analysis or quantification of the costs and benefits, the MSRB responded that although the GFOA may be correct and that municipal entities may be required to bear the cost of additional service providers, the MSRB believes "on balance" the "potential benefits outweigh the potential costs."[21]

Like many other of SIFMA's suggestions, the MSRB does not appear to have seriously considered several suggestions to avoid or limit the significant impairment of the availability of municipal entities to receive full-service brokerage and securities execution services, including (i) temporarily excluding from the principal transaction ban sales of fixed-income securities by a broker-dealer providing incidental advice on the investment of bond proceeds until the SEC and the DOL have concluded their ongoing consideration of the application of a fiduciary duty to principal transactions; and (ii) rationalizing the application of Proposed Rule G-42's documentation, due diligence, risk disclosure and suitability requirements as applied to regular, ongoing incidental advice provided in the brokerage and securities execution services context.

C. Investigating the Accuracy of Client Representations

As described in the SIFMA May 2015 Letter and highlighted by several other commenters,[22] the obligation under Proposed Rule G-42 and Supplementary Material .01 to conduct a reasonable investigation with respect to information provided by the municipal advisor's own client is unnecessary, counterproductive and inefficient. In addition to the obvious absurdity of a municipal advisor not being permitted to rely on its own client's representations in advising that client, the obligation would impose unnecessary costs on municipal entities, who will ultimately be the ones paying for their municipal advisors to investigate facts already known to the municipal entity.

There are numerous examples of SEC, FINRA and other financial regulatory rules where regulated entities can rely upon customer or counterparty representations without needing to conduct any investigation with respect to information provided by the client.

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[20] Letter from Dustin McDonald, GFOA, to Brent J. Fields, SEC (June 15, 2015), *available at* www.sec.gov/comments/sr-msrb-2015-03/msrb201503-17.pdf.

[21] MSRB Response Letter at 14.

[22] *See* OIP at 23.

Most relevant, the SEC in its rules for the registration of municipal advisors permits reasonable reliance on representations from a municipal entity or obligated person without requiring an investigation of the client's representation.[23] Moreover, under FINRA's suitability rule, a broker-dealer must base its suitability analysis upon information obtained from the client, without a duty to investigate any of the information provided by the client.[24] The Commodity Futures Trading Commission ("**CFTC**") also permits swap dealers to obtain representations from counterparties, including from special entity counterparties (e.g., municipalities), where the swap dealer makes a recommendation or acts as an advisor to such counterparties without requiring the swap dealer to conduct any sort of investigation into the representation.[25]

D. Clarifying the Duty of Care for Preparing Official Statements

As described in the SIFMA May 2015 Letter, the duty of care in Proposed Rule G-42 and Supplementary Material .01 should be clarified to squarely place upon a municipal advisor that assists in the preparation of an official statement in connection with a competitive transaction the responsibility to perform reasonable diligence with respect to the accuracy and completeness of any portion of the official statement as to which the municipal advisor assisted in the preparation. The original rule filing of Proposed Rule G-42 with the SEC suggests that this is a component of Proposed Rule G-42,[26] but this obligation should be made explicit in the text of Proposed Rule G-42.

Municipal advisors often are called on to prepare certain sections of an official statement or to review the disclosures prepared by a municipal entity. Because municipal entities are subject to potential liability for material misstatements or omissions in an official statement, both municipal entities and investors expect that material included in the official statement have been prepared with a high degree of care. While a municipal advisor should be permitted to rely on information provided by its municipal entity client for purposes of providing advice to the client, a municipal advisor should be explicitly

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[23] *See* Exchange Act Rule 15Ba1-1(m)(3) (providing that a market participant may rely on representations in writing made by a knowledgeable official of the municipal entity or obligated person regarding whether or not certain funds to be invested constitute proceeds of municipal securities, provided that the market participant seeking to rely on such representation has a reasonable basis for such reliance).

[24] *See* FINRA Rule 2111 (requiring that a broker-dealer rely on its customer to provide information related to the customer's investment profile, such as the customer's investments, financial situations and needs, investment objectives, among others). Moreover, FINRA Rule 2111(b) provides an exemption to customer-specific suitability regarding institutional investors provided that conditions are met.

[25] *See, e.g.*, CFTC Rule 23.434 (when making a recommendation to a counterparty); CFTC Rule 23.440 (when acting as an advisor to a special entity); CFTC Rule 23.450 (when acting as a counterparty to a special entity).

[26] *See* Exchange Act Release No. 74860 (May 4, 2015) at note 9 and accompanying text ("The duty of care … would apply to the provision of comments following the review of any document and the provision of language for use in any document -- including an official statement …").

obligated to undertake a reasonable investigation to confirm that those sections of an official statement that it or the municipal entity prepare do not contain any material misstatements or omissions as part of its fiduciary duty to its client.

II. Additional Comments Based on Members' Experience

A. Need for Clarity Regarding the Definition of "Recommendation"

Proposed Rule G-42(d), as amended by Amendment No. 1, would require, among other things, that (i) a municipal advisor making a "recommendation" must have a "reasonable basis" to believe that its recommendation is suitable; and (ii) a municipal advisor reviewing another party's recommendation must have a reasonable basis to determine whether the other party's recommendation is suitable.

In its original rule filing of Proposed Rule G-42 with the SEC, the MSRB explained that a "recommendation" would be interpreted consistent with how it is interpreted in the context of municipal securities dealers recommending a municipal securities transaction, *i.e.*, where it "could reasonably be viewed as a 'call to action to engage in a municipal securities transaction or enter into a municipal financial product.'"[27] The MSRB further explained that "communications by a municipal advisor to a client that concern minor or ancillary matters that relate to, but are not recommendations of, a municipal securities transaction or municipal financial product might constitute advice (and therefore trigger many other provisions of the proposed rule) but would not trigger the suitability obligation."[28]

SIFMA is concerned, on a practical basis, regarding the ability of municipal advisors to consistently distinguish between recommendations and ancillary advice. While a "suitability" obligation under FINRA rules is also triggered by making a "recommendation," the FINRA rule only applies to the recommendation of a particular purchase or sale of, or investment strategy involving, securities,[29] which are distinct and relatively identifiable events in a brokerage relationship. In the context of an issuance of municipal securities, however, there are likely to be innumerable levels of advice or expressions of opinion as to various matters: whether to engage in an issuance at all, whether to "hold off" until market conditions change, whether to choose an underwriter based on two responses to the issuer's request for proposal ("**RFP**") or to wait for additional responses, whether an offering should be a private placement or a public offering, how to structure the issuance, whether cash should be funded or have a surety, the timing of repayments, amortization schedules, the use of premium or discount bonds,

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[27] Exchange Act Release No. 74860 (May 4, 2015) at 16-17.

[28] *Id.*

[29] *See* FINRA Rule 2111.

what interest rate and whether fixed or floating, when to conduct the issuance—to name a few. It is not clear whether the initial advice to engage in a transaction, each structuring aspect, or only the final "go or no go" advice constitutes a "recommendation" for purposes of Proposed Rule G-42. In order to design effective policies and procedures, and to evidence compliance with this obligation, municipal advisors must be able to know with certainty when a formal suitability obligation is triggered.

Similarly, given the difficulty in this context of attempting to distinguish what is a recommendation versus what is ancillary advice, FINRA and SEC examiners also will need the same guidance in order to know when advice would be considered a recommendation.

This is even more problematic when attempting to determine whether the advice of others would be considered a recommendation that may trigger suitability review and other relevant duties, where the municipal entity or obligated person client has requested that the municipal advisor review a third party recommendation and such review is within the scope of the engagement. For example, if a municipal advisor to a municipal entity client receives numerous responses to an RFP and requests that its municipal advisor review each RFP response (each providing input on multiple issues associated with a proposal), it is unclear whether the municipal advisor would need to comply with the requirements of Proposed Rule G-42(d) when reviewing such third party RFPs, including each element covered by each response, and document its analysis of each, or whether the requirement to review third party recommendations is limited to certain key elements of the responses or not triggered until the transaction or proposal at issue becomes more developed.

B. Need for Clarity Regarding Documentation of Suitability Determinations

As set forth above, a municipal advisor must ensure that a recommended municipal securities transaction or municipal financial product is suitable for its client. MSRB Proposed Rule G-8(h)(iv)(A) would require that a municipal advisor keep "a copy of any document created by a municipal advisor that was material to its review of a recommendation by another party or that memorializes the basis for any determination as to suitability." However, because it is not clear from Proposed Rule G-42(d) when a municipal advisor's communications with a client is a recommendation, it is equally unclear what types of documentation a municipal advisor must retain to comply with MSRB Proposed Rule G-8(h)(iv)(A).

SIFMA requests that the MSRB provide guidance regarding what types of documentation would be required for a municipal advisor to maintain under MSRB Proposed Rule G-8(h)(iv)(A) and Proposed Rule G-42(d) with respect to evidencing support for recommendations and memorializing the basis for any suitability determinations. It is not clear what types of documentation would need to be memorialized that would demonstrate in a regulatory examination what the municipal advisor relied upon when forming the basis for its suitability determination. Requiring

municipal advisors to create and maintain vast amounts of documentation to evidence the basis for the suitability of each recommendation would be vastly more burdensome than under other regulatory structures. For example, under the Advisers Act, an investment adviser has an obligation to provide only suitable investment advice, taking into consideration the client's financial situation, investment experience, and investment objectives. But it need only maintain records of the information it obtained about clients in order to conduct its analysis; it need not memorialize the suitability considerations underlying each recommendation.[30]

C. Align the Requirements of Proposed Rule G-42(d)(i) to those of MSRB Rule G-17

Proposed Rule G-42(d)(i) requires municipal advisors to evaluate the "material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product." A similar requirement applies to underwriters pursuant to MSRB Rule G-17, pursuant to which underwriters must disclose to issuers and obligors financial material risks, only if such risks are "known to the underwriter and reasonably foreseeable at the time of the disclosure."[31]

Municipal advisors, like underwriters, are not in a position to predict with certainty all possible risks. Therefore, the MSRB should amend Proposed Rule G-42(d)(i) to add in the italicized text as follows: "[T]he municipal advisor must inform the client of . . . the municipal advisor's evaluation of the material risks, potential benefits, structure and other characteristics of the recommended municipal securities transaction or municipal financial product *that are known to the municipal advisor and reasonably foreseeable at the time of the disclosure*."

III. Additional Concerns Pertaining to Amendment No. 1

A. Notification Regarding Changes to Forms MA and MA-I

Amendment No. 1 to Proposed Rule G-42(c)(iv) would add a new proposed requirement that a municipal advisor not only provide its clients with the date of the last material change or addition to the legal or disciplinary event disclosures on any Form MA or Form MA-I filed with the SEC, but also provide a "brief explanation of the basis for the materiality of the change or addition."

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[30] *See, e.g.*, Suitability of Investment Advice Provided by Investment Advisers; Custodial Account Statements For Certain Advisory Clients, Advisers Act Release No. 1406 (Mar. 16, 1994) (proposing suitability requirement and recordkeeping rules). *See also* SEC Division of Investment Management, General Information on the Regulation of Investment Advisers, *available at* https://www.sec.gov/divisions/investment/iaregulation/memoia.htm (describing investment adviser suitability obligations).

[31] *See* MSRB Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities (Aug. 2, 2012).

This newly proposed additional requirement is unnecessary and overly burdensome, outweighing any potential benefit. SIFMA agrees that a municipal advisor's clients should have access to information regarding the municipal entity's legal or disciplinary events, and notification regarding material new disclosures. However, requiring municipal advisors to affirmatively consider the materiality to each of its clients of any new disclosure and prepare a written explanation of that materiality determination would simply add additional paperwork burdens without any benefit to the municipal entity's clients. Form MA and MA-I disclosures, like Form BD, Form U-4, and Form ADV disclosures, already tend to be brief descriptions of the legal or disciplinary event. Where a municipal advisor's client is unable to determine the materiality of the disclosure, it can request more information from the municipal advisor.

IV. Proposed Rule G-42 is Inconsistent with Statutory Standards

As noted above, SIFMA continues to believe that certain aspects of Proposed Rule G-42 (i) are more burdensome than they need to be to achieve the rule's stated objective; (ii) are overly broad; (iii) introduce unnecessary costs; and (iv) inappropriately reduce competition in ways that are inconsistent with the standards for MSRB rulemaking under Sections 15B(b)(2)(C) or (L) and fail to meet the standards for SEC approval under Section 3(f) of the Exchange Act.[32]

Specifically, Proposed Rule G-42 will significantly harm competition, as demonstrated by the fact that firms have exited from the municipal advisory business and have stopped providing municipal advisory services in anticipation of the adoption of Proposed Rule G-42. For example, as a result of the fact that neither a municipal advisor nor any of its affiliates is permitted to enter into any principal relationship with a municipal entity client, many multiservice firms, such as firms affiliated with broker-dealers, have determined that the inability to enter into other business with the client makes the cost of providing municipal advisory services too high. As a result, the pool of firms willing to act as municipal advisors may be limited to only a smaller universe of stand-alone monoline firms. Lacking in competition, these remaining municipal advisors will increase their fees, and the quality of their service may decline, harming clients much more than they benefit from increased disclosures.

Moreover, the MSRB's refusal to adopt an exception to the principal transaction ban where a municipal client is represented by an SRMA[33] and refusal to limit the scope of the ban to principal transactions that are directly related to the advice provided by the municipal advisor[34] are examples of how the MSRB is eliminating and burdening competition by making it significantly more difficult for municipal advisors to conduct

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[32] *See supra* note 7 and text accompanying note 7.

[33] *See supra* Part I-A; SIFMA May 2015 Letter at 10.

[34] *See supra* Part I-A; SIFMA May 2015 Letter at 5-6.

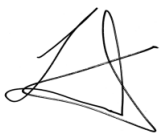
business and for small and mid-size issuers to receive advice on the products and crucial financial services they need. The MSRB could achieve the same objectives without burdening competition by revising Proposed Rule G-42 in a manner consistent with the comments set forth in Part I of this letter.

Finally, certain aspects of Proposed Rule G-42, as described above,[35] are contrary to the MSRB's statutory mandate to protect the interests of municipal entities and obligated persons.[36] As described above, Proposed Rule G-42 would impede on the ability of municipal entities and obligated persons to receive incidental investment advice from their dually-registered broker-municipal advisor, or to receive such advice on a timely basis, and would cause municipal advisors to be subject to new and unnecessary costs and fees to receive advice, or pay for services, such as due diligence on their own representations, that they neither request nor need.

* * *

SIFMA appreciates your consideration of these views. Please do not hesitate to contact me at (212) 313-1130, or our counsel, Lanny A. Schwartz of Davis Polk & Wardwell LLP, at (212) 450-4174 with any questions.

Sincerely yours,



Leslie M. Norwood
Managing Director and
Associate General Counsel

[35] *See, e.g., supra* note 20 and accompanying text.

[36] *See* Exchange Act § 15B(b)(2)(C) (requiring that MSRB rulemaking "be designed to . . . protect investors, municipal entities, obligated persons, and the public interest.")

cc: ***SEC***

Mary Jo White, Chair
Luis A. Aguilar, Commissioner
Daniel M. Gallagher, Commissioner
Michael Piwowar, Commissioner
Kara Stein, Commissioner

Jessica Kane, Director, Office of Municipal Securities
Rebecca Olsen, Deputy Director, Office of Municipal Securities

MSRB

Lynnette Kelly, Executive Director
Robert Fippinger, Chief Legal Officer
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