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Invested in America

April 11, 2011

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

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

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

Dear Mr. Smith:

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

I. Executive Summary

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

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA).

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

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

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

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

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

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

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

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

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

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

II. G-36 Proposal – Duties to Municipal Entities

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

1. The MSRB Should Define "Engagement."

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

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

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

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

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

2. Fiduciary Duty Should Apply to Specific Engagements Only.

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

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

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

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

[9] Exchange Act § 15B(e)(7).

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

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

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

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

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

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

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

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

D. Disclosure of Conflicts and Informed Consent.

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

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

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

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

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

2. Non-Individualized Disclosures Should Be Permitted.

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

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

3. Disclosures Need Not be Repeated.

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

4. Official Providing Informed Consent.

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

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

E. Compensation Conflicts and Disclosure.

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

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

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

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

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

F. Unmanageable Conflicts.

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

1. Principal Transactions Should Not be Prohibited.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

G. Prohibition on Excessive Compensation.

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

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

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

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

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[22] Exchange Act § 15B(e)(9).

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

5. Limited Scope Engagements Should Be Limited in Scope.

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

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

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

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

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

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

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

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

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

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

A. Duty of Fair Dealing to Obligated Persons.

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

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

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

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

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

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

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

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[25] *See* Exchange Act § 15B(c)(1).

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

[27] *Id.*

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

6. Misrepresentation Requirements and Disclosures.

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

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

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

1. Disclosures Regarding Solicitation and Offered Products and Services.

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

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

2. Lavish Gifts and Gratuities.

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

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

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

3. Duties Should Not Apply to Affiliated Solicitors.

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

IV. Implementation Period.

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

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

[30] *See* Exchange Act § 15B(e)(9).

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

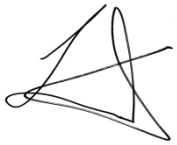
V. Conclusion

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

* * *

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

Sincerely yours,



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cc: ***Securities and Exchange Commission***
The Honorable Mary L. Schapiro, Chairman
The Honorable Kathleen L. Casey, Commissioner
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
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Robert Cook, Director, Division of Trading and Markets
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