SMA
Southern Municipal Advisors, Inc.

August 25, 2014

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, Virginia 22314.

Re: Request for Comment on Revised Draft MSRB Rule 42

Dear Mr. Smith:

Southern Municipal Advisors, Inc. ("SMA") is a woman owned business enterprise specializing exclusively in providing independent financial advisory services to governmental entities. SMA does not participate in the underwriting or selling of municipal securities. SMA serves as an independent financial advisor to governmental entities including municipalities, counties, public authorities and districts. SMA professionals have combined over 60 years experience in public finance throughout the Southeast, in general, and in South Carolina, in particular. It is based upon this experience that the following thoughts regarding Revised Draft MSRB Rule 42 are offered for your consideration.

The Initial and the Revised Draft Rules require in G-42(d) that a municipal advisor must not recommend a municipal securities transaction or financial product unless the advisor "has a reasonable basis for believing that the transaction or product is suitable for the client[.]" (sometimes referred to as the "suitability finding"). We wish to provide two comments regarding this requirement. The first relates to the facts and circumstances the advisor will be permitted to rely upon for having a reasonable basis for believing the transaction or product is reasonable. The second relates to the need to clarify that the suitability finding is based solely upon the facts and circumstances at the time it is made and is limited thereto.

(1) Often it is the client, not the advisor, who initiates a transaction. For instance, the policy making authority (Council or Manager) may determine it is in the municipality's best interest to provide additional administrative or educational facilities. Similarly, a municipality may determine it needs to expand or upgrade its water and or wastewater system either due to population increases or regulatory demands. It may be that as a result of a public referendum, a municipality must proceed with a financing in order to address the will of its citizens. Once these determinations are made, the advisor is then involved to assist in planning for and implementing whatever financing is necessary to accomplish the goals.

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In many cases the financing options are limited by state law, as determined either by the municipality's counsel or bond counsel. In effect, suitability has already been determined by the state legislature and the municipality is merely choosing among the statutorily permitted options.

Further, most municipal policy makers are familiar with all manner of financial instruments permitted by state law – general obligation bonds, revenue bonds, certificates of participation, master leases, and refunding of all of these, as well as bond/tax/grant anticipation notes to name those most often employed. Most, if not all, municipal entities of any size have used all or some of the above listed approaches in the past and will in all likelihood continue to do so to fund their capital and cash flow needs. These are "plain vanilla" transactions familiar to all public officials responsible for capital improvement programs.

Most of the facts or circumstances upon which a suitability determination must be based according to Supplementary Material 09 of the Revised Draft Rules are currently provided for in closing documents prepared by bond counsel. Among material facts provided in closing documents are:

- the issuer's historical financial statements;
- borrowing needs and historical debt;
- issuer's objectives specifically expressed in the resolutions/ordinances publicly voted on by the authorizing policy body;
- the fact all laws and regulations precedent to the issuance of the particular debt have been satisfied;
- projections which demonstrate the associated debt service and coverage requirements, if any, will be satisfied, along with any prior debt; and,
- in the case of general obligation bonds, certification that state requirements limiting the issuance of such debt are satisfied.

Where a transaction (a) is related to a project or event determined by the governing body of the municipal entity or its citizens to be in its interest and consistent with its goals; (b) is permitted by state statute as determined by municipal or bond counsel; and, (c) involves one which the municipality has employed in the past, then it seems suitability has been determined and the advisor ought to be able to rely on these facts and the closing documents as establishing a reasonable basis for suitability. The advisor ought not be put in the position of substituting its judgment as to suitability for that of the municipal policy makers, citizens or state lawmakers.

In contrast to the above, if a municipality were to decide to enter into a swap arrangement for instance in connection with the revenue bond issued to finance a water or wastewater system upgrade, then an investigation into suitability would be in order. This "add on" to a traditional financial arrangement clearly calls for a suitability determination.

(2) The regulations ought to make clear that the suitability finding relates only to the facts and circumstances as they exist at the time the client enters into the transaction. Should those facts and circumstances change over the course of time the advisor should not be subject to censure or criticism if, under future facts and circumstances, the transaction might be seen as unsuitable.

Nor should there be perceived to be a continuing responsibility imposed upon the advisor to update the suitability finding. It is made at a very specific point in time and it would be burdensome to require that the advisor monitor the client's activities with respect to a completed transaction and adjust the suitability finding if necessary. New factors may arise or emerge from time to time and it is not possible for the advisor to predict how such future factors may impact any specific suitability finding. It is the advisor's responsibility to be as informed as possible regarding the client's financial condition in anticipation of future transactions; however, this responsibility does extend to past transactions.

We recognize the difficulties and challenges the MSRB faces in implementing Dodd-Frank Act and appreciate that the MSRB has reached out to municipal advisors as it crafts the regulatory framework. I hope that you will consider these comments.

Sincerely,

Michael C. Cawley

Michael C. Cawley
Senior Consultant

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