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MSRB Discusses Questionable Dealer Contracts, Plans for New Rules.

Some Municipal Securities Rulemaking Board members are concerned about dealer financial advisory contracts with issuers that appear to disclaim away the dealers' legal and regulatory obligations, MSRB chair Jay Goldstone said Friday after the board's meeting at its headquarters in Alexandria. Va.

"There was discussion," Goldstone said in a press call with reporters. "There were certain levels of consternation about this," he said when asked about the contracts.

Goldstone said he knows the issue is on the radar of both the Securities and Exchange Commission and the Financial Industry Regulatory Authority, but that it is "unclear at this point" whether the MSRB needs to tighten its rules.

In some contracts, dealers appear to contract to provide municipal advisory services to issuers, but state they are not financial advisors and have no fiduciary duty to put the issuer's best interest first. The dealers also state they may underwrite any resulting muni bond offering.

The contracts seem to violate Dodd-Frank, which imposes a fiduciary duty on MAs, as well as the MSRB's Rules G-17 on fair dealing and G-23, which bars dealers from serving as both FA and underwriter on the same transaction.

SEC muni chief John Cross recently said at a conference that such language is "a bit too cute."

Enforcement is the SEC's and FINRA's turf, and largely a matter of individual facts and circumstances. The MSRB writes rules. "We are not the enforcement agency," Goldstone said.

But the board decided to streamline its fair-dealing rule by consolidating some of the 32 pages of guidance into two new rules – one on dealers' disclosure obligations to customers at the time of trade and another on sophisticated municipal market professionals – as well as into proposed changes to an existing third rule on suitability, said Goldstone and MSRB executive director Lynnette Kelly.

The board's G-19 on suitability, which requires brokers and dealers to obtain certain customer information prior to completing a muni transaction in a customer's account. The proposed changes to the rule would require additional information, including age, investment time horizon, liquidity needs, investment experience and risk tolerance and bring the rule more in line with FINRA's suitability rule.

Kelly said all these changes are so closely related that it only makes sense to submit them for SEC approval as one package Goldstone said the MSRB will probably file the package with the SEC in the fall.

The board discussed also discussed comments it received on two concept releases, one proposing to

shorten the current 15 minute window for trade reporting and the other proposing underwriters post preliminary official statements on the MSRB's EMMA disclosure website. Goldstone said the MSRB will continue to consider these and that neither is being tabled.

He said many questions remain about whether shortening the 15 minute time window would be productive. "There was discussion about whether there was real value," he said. "Will there be greater transparency?"

He added that some firms already report trades much earlier than required.

Kelly said questions also linger about the POS proposal, including whether issuers are in favor of having their documents posted by their underwriters. "There are lots and lots of questions, which is why we came out with a concept release," she said.

The MSRB also continues to prepare for rules and rule changes for municipal advisors, but is currently waiting for the SEC's final definition of municipal advisor. "We have spent the last few months focusing on the activities of municipal advisors and are prepared to review our draft rules, make changes if necessary and move forward with the rulemaking process," Goldstone said.

Goldstone said the SEC definition has been drafted and circulated to commissioners, but not scheduled for commission consideration. He added it remains a high priority for the commission.

MSRB officials plan to meet with new SEC chair Mary Jo White, Goldstone said, but has not yet had a chance to discuss muni-specific issues with her in person.

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