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MSRB's G-42 Guidance Notes Ambiguities for MAs in Conduit Issues: Burr & Forman

Last week, the MSRB issued "guidance" on the application of Rule G-42 conduct standards for Municipal Advisors in conduit issues. The "guidance" highlights ambiguities from the "for or on behalf" language in the MA Rule when applied to conduit issues (where the MA interacts with both the municipal issuer and the conduit borrower).

Beyond issue-spotting though, the "guidance" merely urges care and defers to the SEC for after-th--fact "facts and circumstances" determinations. In fact, it includes a "don't ask us" disclaimer: These "are interpretive issues that are solely within the jurisdiction of the SEC. Requests for interpretation regarding such issue should be direct to the SEC's Office of Municipal Securities."

Extended to MAs in December 2015, Rule G-42 sets out conduct and disclosure standards following from an MA's statutory fiduciary duty to Municipal Entities ("ME") and duty of care to Obligated Persons. In a conduit borrowing, the governmental issuer is an ME and the conduit borrower is an Obligated Person (but might also be an ME).

There are six take-aways from the guidance:

1. First and always ask "who is the client": The issuer, conduit borrower or both? Who pays your fee isn't dispositive.
2. Next determine if the client is an ME (fiduciary duty) or OP (duty of care). If the conduit borrower also is an ME, then ME status (and your obligations) trump their status as an OP/conduit borrower.
3. Assess actual and potential conflicts of interest now and throughout the representation.
4. Disclose and update those conflicts.
5. Mitigate those conflicts.
6. Withdraw if those conflicts are irreconcilable.

MSRB's guidance discusses potential conflicts and issues in five scenarios involving MAs' involvement in conduit borrowings.

- First, where an Issuer Hires MA for / to Conduit Borrower, consider, disclose and mitigate potential conflicts of interest (arising from the Issuer's payment of the MA's fee).
- Second, where an MA knows (or reasonably should) that an ME client will be seeking and passing along advice to a OP conduit borrower, then the MA should consider, disclose and mitigate potential conflicts arising from an actual or implicit "dual representation." The discussion notes that the MA's fiduciary duty to an ME may mean that the MA cannot "disclose away" actual conflicts. A scope limitation within an engagement may offer appropriate protections, together with thoughtful termination provisions. Clearly, an engagement letter should disclaim any advice to non-clients.

The same considerations apply to explicit dual representations, where:

- Third, the OP conduit borrower hires the MA to provide advice to both borrower and issuer.
- Fourth, dual but "independent" representations in which the OP and ME each hire the same MA.
- Fifth, dual but "independent" representations in which the OP and ME each hire the same MA, but the engagement is staffed by separate MAPs for each client (because the MA enterprise itself owes obligations to each client). So "Chinese Walls" may help mitigate, but won't avoid, conflicts of interest.

The guidance is MSRB Regulatory Notice 2017-13 (July 13, 2017), here.

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