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Dealers Ask SEC Not to Approve Fair Dealing Guidance Changes.

Broker-dealers don't want the Securities and Exchange Commission to approve changes to fair-dealing guidance, saying that a proposed amendment adds complexity and uncertainty to the rule.

Bond Dealers of America made that case to the SEC in a letter dated Oct. 29, asking them not to approve the Municipal Securities Rulemaking Board's amendment to Rule G-17's interpretive guidance.

"Rather than simplify and streamline Rule G-17 compliance, the lengthy amendment would add significant complexity and uncertainty to the G-17 regime," wrote Michael Nicholas, BDA CEO.

BDA is continually opposed to the MSRB's use of a "reasonably foreseeable" standard, saying it would result in inconsistent compliance standards. The standard would provide that an underwriter's potential material conflicts of interest must be disclosed to an issuer only if that potential conflict is reasonably likely to mature into an actual material conflict of interest during the course of that specific transaction.

BDA said that standard is vague and would provide little useful information for issuers as well as inconsistent compliance.

The Securities Industry and Financial Markets Association reiterated that it wants the MSRB to require only disclosures of actual conflicts of interest.

"The MSRB has chosen a standard of 'reasonably forseeable' conflicts, which we feel is not addressing the industry's concerns about a clear standard," said Leslie Norwood, a managing director, associate general counsel and head of municipals at SIFMA. "This is an undefined standard at this point."

BDA also argued that new language in the proposed amended guidance would introduce new disclosures around complex municipal securities financial structures, creating a "compliance gray area."

"The amendment would create a vague and imprecise standard for determining what is a CMSF and what kinds of information related to the transaction would need to be disclosed and under what conditions," Nicholas wrote.

SIFMA wants clarification from the MSRB regarding complex municipal securities disclosures, and confirmation that standardized underwriters' disclosures will still comply with the rule.

In the MSRB's proposed amended interpretive guidance, they ask that transaction-specific disclosures address complex features or products rather than being general in nature.

Underwriters have to adopt policies and procedures that can be implemented in a consistent manner

to satisfy regulatory requirements and examiners, Norwood wrote.

“There have been some small changes in the interpretive guidance that led us to have some concerns regarding the tailoring of complex securities disclosures,” Norwood said. “Specifically, SIFMA wants to ensure that the MSRB, FINRA examiners and underwriters implementing this amended guidance all have the same understanding.”

SIFMA wants to confirm that the way the industry has been complying with the rule through standardized disclosures where appropriate is still a valid way to comply with the rule, given the proposed changes.

SIFMA believes it is reasonable to give any issuer that has been recommended a common complex structure a standard written disclosure that describes the nature and risks, with the understanding that the disclosures would be more tailored if the transaction deviated from the standard, Norwood wrote.

SIFMA also wants to clarify wording in the guidance such as “individualized,” to mean that standard disclosures are designed to be clear, concise and tailored to a specific type of financing such as variable rate demand obligations, not a book of all types of product disclosures.

“Confirmation from the MSRB that this interpretation is reasonable would clear up this confusion from the proposed revised interpretive guidance,” Norwood wrote.

If the SEC approves the MSRB’s proposed changes, SIFMA will review and update its G-17 model documents, Norwood said.

The MSRB’s proposed guidance said that a sole underwriter or lead manager would need to “disclose” to an issuer client that the “issuer may choose to engage the services of an MA with a fiduciary obligation to represent the issuer’s interests in the transaction.”

BDA is opposed to the provision, saying there are no statutory or regulatory requirements that issuers hire an MA and that underwriters should not be required to promote the services of other market participants.

The National Association of Municipal Advisors supports the changes to the interpretive guidance, restating their support on adding underwriter disclosures that issuers may engage the services of MAs who have a fiduciary duty to the issuer, unlike the underwriter.

“Further, we support expanding the language of the interpretative guidance to disallow underwriters from deterring the use of municipal advisors by issuers,” wrote Susan Gaffney, NAMA executive director.

BDA also believes the MSRB missed out on an opportunity to provide compliance on combining and integrating underwriter disclosures required under Rule G-17 and Rule G-23 on activities of financial advisors.

The MSRB is currently reviewing Rule G-23. Some issuers have been concerned that an underwriter firm serving as an issuer’s MA could get insight and leverage a deal, only to then resign as advisor and underwrite a transaction or at least submit a bid on a competitive deal.

However, some municipal market participants say not by allowing that broker-dealer firm to switch roles and underwrite the bonds takes one more firm out of the equation that can actually submit a bid.

The SEC has the final say. They could choose to require changes suggested in comments or by its own staff. The SEC could also choose to approve the proposal as is.

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