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Dealer Groups Want the SEC to Approve FIMSAC Recommendation.

Both major securities dealer groups have asked the Securities and Exchange Commission to approve a recommendation to allow investment advisers affiliated with broker-dealers to offer and sell negotiated new issue muni bonds during the order period that the dealer also participates in as a syndicate manager or syndicate member.

The Fixed Income Market Structure Advisory Committee's Municipal Securities Transparency Subcommittee recommended last year to change its rule under section 206(3) of the Investment Advisers Act of 1940, amid what broker-dealers say is a sustained trend toward an increase in advisory accounts.

"The effect of these changed circumstances will be an increased demand for relief from Section 206(3)'s disclosure and consent requirements, particularly during times of market stress," said the Securities Industry and Financial Markets Association in its letter released on Thursday.

FIMSAC is recommending the SEC consider a rule that permits a broker-dealer that negotiates and underwrites a new-issue muni bond or is a co-manager or member of a syndicate to meet the requirements under section 206(3) of the Advisers Act when acting in a principal capacity to sell new-issue muni bonds during the negotiated order period.

Under current rules, a broker-dealer that negotiates and underwrites a new issue muni bond or is a co-manager or member of a selling group can't sell bonds in the offering to its advisory clients without meeting the disclosure and consent requirements of the Advisers Act.

Dealer groups say advisers have to make certain written disclosures and obtain consent from a client each time the adviser and client want to engage in a principal transaction.

"The process of making disclosures and obtaining consent for each covered principal transaction is cumbersome and impractical," Mike Nicholas, Bond Dealers of America CEO, said in his June 2019 letter. "Consequently, many RIAs (registered investment advisers) simply refrain from engaging in covered principal transactions with advisory clients."

Current rules are causing clients to lack access to the bonds that meet their investment criteria or only have access to the bonds in the secondary market at potentially higher prices, FIMSAC said.

According to FIMSAC, this has resulted in few or none of the underwriting dealer's advisory clients buying bonds in initial offerings.

"Advisory clients that wish to buy these bonds will buy them after the deal is closed and the bonds are free to trade — typically at a price higher than the original offer price," FIMSAC wrote.

"The goal here is to provide retail investors with access to as broad a swath of the municipal new issue market as possible," said Michael Decker, consultant to BDA.

Decker said there has been a shortage of bonds available to retail, without much tax-exempt inventory and a portion of the market moving to private placements.

The SEC did have a temporary rule in 2007, Rule 206(3)-3T, that permitted advisers who were also registered as broker-dealers and who offered non-discretionary advisory accounts to engage in certain principal transactions with their advisory customers without requiring transaction-b--transaction, written disclosure and consent.

Clients make trading decisions in a non-discretionary account, while discretionary accounts give dealers freedom to make decisions for their clients.

Rule 206(3)-3T was extended several times before it sunsetted in December 2016.

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