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MSRB to Ease Standard of Independence for Board Members.

The Municipal Securities Rulemaking Board has filed rule changes with the Securities and Exchange Commission that would ease the standard of independence for its board.

Some market participants said the MSRB is resisting bringing issuer officials onto the board and wants to keep the board more industry-oriented by choosing retired industry officials as public members. They said the board should not be allowed to loosen or undermine the independence standards. But others claimed the rule changes are needed so that institutional investor representatives can join the board, a current problem because many them have broker-dealer arms to market Section 529 college savings plans, which the SEC has said involves muni securities..

The Dodd-Frank Act mandated the MSRB to have a majority public board. Before the act, the board consisted of 15 members — five from banks, five from securities firms and five from the public, at least one of whom must represent issuers and one of whom must represent institutional investors Members had three-year staggered terms so that five rolled off the board every year.

In Dodd-Frank, Congress said the MSRB must fall in line with other self-regulatory organizations and have more public than industry members, but left it up to the board to determine how to change the board.

The MSRB expanded its board to 21 members, 11 of which are to be independent of any muni broker-dealers, banks or muni advisors, at least of whom represents issuers, one institutional investors, and one who has knowledge or experience in the muni industry. Of the 10 regulated members, at least one must be associated with a non-bank securities broker-dealer, one with a bank. In addition, at least one but not less than 30% of the 10 must be associated with non-dealer or non-bank muni advisors. Board members still serve three-year staggered terms, with seven rolling over every year.

Currently the board defines public members who are “independent of any regulated entities” to mean individuals who have “no material business relationship” with any regulatory entities. The individuals are not, and have not been, associated with a regulated entity for two years and do not have any compensatory or other relationship with a regulated entity that would affect the independence of their decision-making.

But the MSRB told the SEC in its notice, “In practice, this standard has precluded consideration of otherwise viable candidates who are knowledgeable of matters related to the municipal securities market from service as public representatives” because they are associated with regulated entities.

“This standard of independence disqualifies many individuals with expertise and knowledge to represent investors because such persons have a regulated entity within their employer’s corporate structure,” the board said.

The MSRB told the SEC it is proposing “a more function oriented approach to defining

independence” that will specify an individual has “no material business relationship” with a regulated entity such as broker-dealer, bank or muni advisor, if it is not, and within the last two years was not, an officer, director, employee or controlling person of the regulated entity. The term director would not cover independent directors.

“The proposed rule change will … allow the MSRB to consider candidates who are associated with regulated entities solely by virtue of the corporate structure of their employer,” the MSRB said.

But Jeanine Rodgers Caruso, president of the National Association of Independent Public Finance Advisors, said, “NAIPFA is disappointed with the MSRB amendment to MSRB Rule A-3. The MSRB is removing the phrase “associated with” from the language of the rule and is replacing it with the phrase officers, employees, etc. of a broker-dealer. The net effect is that employees of broker-dealer affiliates will be considered to be independent for purposes of the board’s composition regardless of whether they are currently employed by such an affiliate. In other words, if Goldman Sachs had a non-municipal securities dealer affiliate with employees, that individual would be considered to be independent regardless of their current employment state with the affiliate.”

The board told the SEC that all board members, whether public of regulated, “have a fiduciary duty to the MSRB and are bound by a duty of loyalty and duty of care and are obligated to act in the best interests of the organization and to avoid conflicts of interest.”

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