

# **Bond Case Briefs**

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## **MA Rule May Change Dealer Practices.**

Broker-dealer practices may change under the Securities and Exchange Commission's new municipal advisor registration rule, as the rule encourages firms to establish underwriting relationships with issuers early in order to be exempt from registration.

SEC muni chief John Cross told participants in a webinar hosted jointly by The Bond Buyer and the Securities Industry and Financial Markets Association that the rule's registration exemption for underwriters will probably result in earlier letters documenting a firm's engagement to underwrite a bond deal.

The rule does not require underwriters to register as municipal advisors and allows them to provide certain advice on a specific issuance of bonds. But it only affords them the underwriter exemption from registration once they have been engaged as underwriter on a specific bond deal.

"That will be a change in focus for the broker-dealer community," Cross said.

The SEC rule says that an MA is someone who provides advice to an issue or other municipal entity or borrower on the issuance of municipal bonds, the investment of bond proceeds or escrow funds, guaranteed investment contracts, and derivatives such as swaps. Advice means recommendations tailored to the municipal entity, and does not include general information or statements of fact.

While the SEC has not taken the position that "engagement" as an underwriter explicitly requires a contractual agreement, Cross said he expects such agreements to be used and to be signed early in the relationship between dealers and issuers. By making clear that they have been engaged on the transaction, dealer firms could rely on that exemption from the registration rule while providing advice on the structure, terms, and timing of the offering.

Dave Sanchez, general counsel at De La Rosa & Co. and former SEC official who also participated in the webinar, said dealer firms are already assuming they are entering a new world under the regulatory regime.

"A majority believe it will have a major effect on their business," he said.

Sanchez asked Cross and SEC attorney-fellow Rebecca Olsen to describe the relationship between the MA rule and Municipal Securities Rulemaking Board Rule G-23 on activities of financial advisors. G-23 prohibits financial advisors from also serving as underwriters on the same transaction. Bond lawyers have questioned whether a municipal advisor under the SEC rule must also be a financial advisor under the MSRB rule. Some have suggested that dealers could offer unsolicited advice to issuers, accept the fiduciary duty that comes with that, and then inform the issuer that they will seek to underwrite at an arm's length later with no fiduciary duty attached at that time.

But the two regulators were quick to discourage that line of thinking.

"Rule G-23 still needs to be complied with," Olsen said.

Cross underscored the intent of G-23, which was designed to prevent dealer-affiliated financial advisors from recommending bond deals that they then underwrite, regardless of whether those deals are in the best interest of the municipality.

“That seems like the classic role-switching that the MSRB rule relates to,” Cross said.

Firms will be required to register as MAs with the SEC under the rule on a staggered basis beginning July 1 2014, though the substantive and interpretative aspects of the rule will take effect 60 days following the publication of the rule in the Federal Register, which has not yet happened.

About 1,150 MAs are currently registered under a temporary registration rule that expires at the end of 2014. Cross said he expects that number to remain about the same once final registration is finished.

But Lanny Schwartz, a lawyer at Davis Polk & Wardwell LLP who also took part in the webinar, said some firms have been “waiting in the weeds” to register under the final rule. Cross said those firms should already be registered under the temporary rule.

The MSRB has the task of creating rules with which registered MAs must comply.

MSRB executive director Lynnette Kelly told webinar participants that while the MSRB board has control over the rulemaking agenda, she expects it may take up a fiduciary duty and fair dealing requirements first and tackle other rules or rule changes over the next 12-18 months. Those are likely to include requirements on supervision, gifts and gratuities, political contributions and professional qualifications. The MSRB also has to develop a professional exam for MAs, who will have to register with the board as well as the SEC.

by: KYLE GLAZIER