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SIFMA Weighing Campaign Against Muni Advisor Rule Provisions.

The Securities Industry and Financial Markets Association is considering launching a campaign urging municipal issuers to lobby federal regulators and lawmakers against underwriter restrictions contained in the Securities and Exchange Commission's final municipal advisor registration rule.

SIFMA has circulated a draft letter to member firms entitled "An Open Letter to the U.S. Municipal Community," warning that the SEC's rule, to take effect in mid-January, would "restrict issuers' access to market information and impact their access to the capital markets – delaying financings for schools, hospitals, public housing, and other critical infrastructure projects in communities across America."

The dealer group complains in the draft that the SEC "has done this by issuing the rule in final form with no chance for public review or comment."

The MA rule, slated to take effect by mid-January, would require anyone offering particularized advice about muni bonds, muni derivatives, or the investment of bond proceeds to an issuer or other municipal entity or conduit borrower to register as a municipal advisor. MAs owe a fiduciary duty to put the interests of the issuer or other municipal entity client above their own — something the underwriting community has long maintained is not consistent with the role of an underwriter.

Under the Municipal Securities Rulemaking Board's fair-dealing rule, underwriters are required to disclose to issuers that they do not have any fiduciary duty and that the transaction will be at arm's length, with firms representing their own interests.

The problem is the interplay between the SEC's new MA rule and the MSRB's Rule G-23, which was recast in November 2011 to prohibit dealers from serving as financial advisors and underwriters on the same municipal bond deal.

"It is THE KEY issue for everybody – SIFMA, the National Association of Bond Lawyers, and the Government Finance Officers Association. Everything else is on the periphery," said one non-dealer source familiar with the controversy. "The question is can broker-dealers do what they've done for 30 years and present new financing ideas and refunding plans to issuers and underwrite any deals that result?"

"Dealers have been living with the G-23 prohibition since 2011," the non-dealer source said. But they've always viewed it in the context of a more formal situation, as a prohibition on a dealer trying to be a financial advisor and an underwriter for the same bonds.

The SEC's MA rule are less formal. Under those rules, if a dealer provides targeted advice to an issuer, it becomes an MA with a fiduciary duty to the issuer.

"The concern is that if a dealer gives targeted advice to an issuer, that's going to make the dealer an MA and knock it out of the underwriting box by virtue of treating the MA rule and G-23 as

congruent," the non-dealer source said.

The MA rule allows underwriters to offer limited advice on bonds they have already agreed to underwrite, such as guidance on investor road shows. The rule also contains exemptions designed to allow more extensive communication between prospective underwriters and issuers under certain circumstances. If the municipality retains its own registered MA and certifies in writing that it will rely solely on the advice of that advisor, then underwriters and other professionals could offer advice more freely without fear of becoming MAs. Dealers also would be exempted from the MA rule if they are responding to a Request for Proposals or Quotations that is sent out by an issuer, providing the request is not sent out to only one firm.

But SIFMA does not consider these exemptions to be sufficient enough to avoid "impeding the relationship between underwriters and the issuer clients they serve," its draft letter states.

"Many issuers, large and small, choose not to employ financial advisors for bond transactions for a variety of reasons," the draft says. "Sometimes the issuer has sufficient internal resources to manage the transactions without an advisor. Sometimes the issuer may simply believe the value offered by a financial advisor does not justify the cost."

While the draft is critical of the SEC's decision to adopt the final rule without putting it out for public comment, the commission sifted through more than 1,000 comment letters in developing the final rule, several sources noted.

" If the option of continuing to receive the free flow of information is important to the conduct of your debt program, the SIFMA draft concludes, "we urge you to consult with counsel and let the SEC, and members of Congress, know of your views."

Michael Decker, co-head of municipal securities at SIFMA, confirmed that SIFMA remains concerned about these aspects of the rule. He said SIFMA circulated the draft letter to members in order to get reaction, but has not decided yet how to proceed with it. Decker said the SEC has indicated it will release more guidance and that a dialogue on the issues will continue.

"We're hopeful through that process the rule will become more workable," Decker said.

In fact, sources from several groups said that the SEC's Office of Municipal Securities is currently collecting comments and concerns with the idea of eventually putting out a set of frequently asked questions and answers on the commission's website. There is precedent for this. When the SEC finalized its Rule 15c2-12 on disclosure in late 1994, it worked with the National Association of Bond Lawyers to put out two sets of FAQs on the rule.

NABL , which is currently holding its board meeting in South Carolina, is expected to send the SEC Muni Office some draft FAQs next week, sources said.

Some muni securities experts say they do not understand the controversy, that the MA rule are very different from the MSRB's Rule G-23. When the MSRB issued the final version of Rule G-23, it said: "Rule G-23 is solely a conflicts rule. Accordingly, this notice does not address whether provision of the advice permitted by Rule G-23 would cause the dealer to be considered a "municipal advisor" under the Exchange Act and the rules promulgated thereunder."

Nathan R. Howard, counsel to the National Association of Independent Public Finance Advisors, said the potential SIFMA campaign is clearly more about protecting the interests of dealer firms and not those of issuers. Howard pointed to guidance issued by the GFOA which suggested that underwriter communication with issuers could still occur under the new rule.

“SIFMA’s continued efforts to undermine the MA rule will have a direct negative impact on the very issuers that the rule seeks to protect,” Howard said. “These concerted attempts to undue issuer protections appear to be aimed solely at protecting the interests of SIFMA’s member firms. As the GFOA noted in its release yesterday, underwriters will have ample opportunity to provide ideas to issuers during the course of a transaction.”

Another market participant familiar with the debate also attacked the SIFMA effort.

“The SIFMA letter is purposefully misleading and a great example of how broker-dealers feel they are above the law. If that letter is an example of the type of ‘balanced’ advice they give to issuers then perhaps the rule did not go far enough in constraining them. The municipal advisor rule does not limit the free flow of ideas — it just helps ensure that the ideas presented to issuers (and paid for by taxpayers) are fiscally responsible.”

The MSRB is in the process of crafting rules stemming from the SEC’s work. MSRB executive director Lynnette Kelly said the board may address the issue if appropriate, but is hopeful the SEC will do so in the meantime.

“The MSRB supports the need for clarity on the activities of municipal advisors,” Kelly said. “The SEC is preparing guidance on its registration rule, which should address some of these concerns. The MSRB will evaluate the interplay between the registration rule and existing MSRB rules, and consider issuing guidance as appropriate.”

BY KYLE GLAZIER