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What Governments Need to Know About the New Municipal Advisor Rule.

A new rule about who can give governments financial advice goes into effect Tuesday, but how to apply it is far from resolved.

It's been a confusing road for the creation of a new category of financial advisors who will be regulated by the federal government. So confusing, in fact that the feds delayed implementating the Municipal Advisor Rule by half a year to July 1.

A municipal advisor is a qualified financial professional (such as a banker or financial consultant) who give municipalities advice on financial deals like bond offerings. That person must be registered through the SEC as a municipal advisor and cannot have any other interest in the deal.

Historically, it was common for those orchestrating the transaction to also dish out advice and counsel to the municipality entering. The problem with this model was that while most underwriters or brokers are fair and reasonable, entrusting a financial professional to give advice to a municipality when that professional could potentially benefit a great deal if the municipality enters into the deal creates an inherent conflict interest.

Reaction from bankers and underwriters on how best to cope with the new restrictions on what they can and can't say to their government clients has been varied. (The rule technically goes into effect this week but many institutions have already been operating under its restrictions ahead of time.) An exception does exist that allows underwriters and bankers on a deal to talk with the government about options so long as the government presents in writing that it already has a municipal advisor and it is relying on its advisor's advice. Still, said Mark-David Adams, a bond counsel at Edwards Wildman law firm, some have effectively instituted a gag order.

"Some banks are telling their officers … to absolutely not give any advice flat-out, whatsoever," he said. "It's just set a term sheet, [that says] 'this is what we want, this is what we'll pay for it, have a nice day and good bye.'"

There are gray areas in which those who conduct financial deals for governments can work and issuers can expect most of the underwriters they deal with to operate in this realm. Some additional key exceptions offered by the Municipal Market Advisors include:

1) Underwriters may include recommendations and advice when responding to an issuer's request for proposal if the RFP is about a specific financing and has been advertised either to three reasonably competitive firms or via posting on the issuer's website. The response timeframe off the RFP must also be less than 6 months.

2) While underwriters and other professionals may not provide recommendations or advice to issuers unless an exemption is met, underwriters may talk with the issuer about "general market information." This does not mean underwriters can "express subjective assumptions, opinions, or views [that] constitute a recommendation." But it does mean they can talk about available products and even "information regarding a municipal entity's particular outstanding bonds, such as current

market prices and yields, without this information constituting a recommendation.”

Adams said many governments are considering whether to retain a municipal advisor on an ongoing basis so as to make it easier for underwriters or bankers to approach a government with a deal that might be good for them (like refinancing debt at a lower interest rate). But that’s not a solution that will work for everyone as many governments are used to seeking advice from different people depending on their expertise and the type of deal.

Adams predicted a 6-month growing pains period before governments and financial institutions settle in to the new routine.

“It’s probably going to be a little clumsy,” he said. “Like someone going out on their first date – it’s going to be awkward for a while.”

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