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Why Market Groups Want MSRB to Abandon Bank Loan Proposal.

WASHINGTON – Muni market groups are resoundingly saying "no" to the Municipal Securities Rulemaking Board's question of whether it should require municipal advisors to disclose information about their issuer clients' bank loans or privately placed municipal securities.

The MSRB said it asked the question in a March 28 concept release exploring ways to increase the disclosure of bank loans because it worries the current lack of disclosure on EMMA hinders an investor's ability to truly understand the risks of an investment.

Most groups applauded the MSRB's intent to increase disclosure but presented a host of reasons for why the concept of having MAs disclose bank loans is flawed.

Only the National Federation of Municipal Analysts said the concept "is a positive step in improving disclosure of [bank loans]." But that group also proposed other ways to disclose bank loan information.

Terri Heaton, president of the National Association of Municipal Advisors told the board that the "proposal would not get the industry to [the MSRB's] goal line" and would "place an unreasonable burden on municipal advisors."

The MSRB acknowledged in the concept release that there may be impediments to writing such a rule under federal securities laws. The Securities Exchange Act of 1934 contains the Tower Amendment, which bars the MSRB and SEC from requiring information from issuers before offerings. It also bars the MSRB from requesting issuer information after offerings.

But the MSRB said it might be able to write such a rule for MAs along the lines of existing dealer rules like G-32 on primary offering disclosures and G-34 on CUSIPs, new issue, and market information requirements.

Heaton balked at the attempt to justify such a requirement with G-32 and G-34. Unlike dealers, MAs do not have a "customer" relationship with investors or the investing public at large and thus it goes beyond the MSRB's authority to impose such a broad investor delivery requirement on MAs, she wrote.

If the proposal were enacted, it would also threaten the MAs' fiduciary duty to their clients under MSRB Rule G-42, which lays out municipal advisors' core duties, she added.

Ken Artin, president of the National Association of Bond Lawyers, echoed Heaton in a letter for NABL, saying the proposal may present "an unresolvable conflict of interest for the municipal advisor."

He also questioned the MSRB's statutory authority, comparing the possible regulation of MAs to the existing dealer regulation under Securities and Exchange Commission Rule 15c2-12 on disclosure.

Under Rule 15c2-12, the SEC regulates the actions of broker-dealers in primary offerings of municipal securities. Dealers are regulated entities. Primary offerings are regulated transactions and municipal securities are regulated products, Artin wrote. The concept release would have the MSRB regulating disclosure of bank loans or direct purchases, which may or may not be municipal securities, he said.

Many industry groups have asked the SEC whether bank loans and private placements can be considered securities but the commission has not provided any guidance. Officials with George K. Baum & Co. suggested in their letter that the MSRB should delay additional regulation on bank loans until the SEC settles the issue and releases guidance.

Leslie Norwood, managing director, associate general counsel, and co-head of munis for the Securities Industry and Financial Markets Association, wrote: "there is no colorable argument that the MSRB has the statutory authority to require disclosure of bank loans, because they are financial instruments that are not securities."

Bond Dealers of America chief executive officer Mike Nicholas also argued that the idea floated by the MSRB is outside its authority because the board "proposes to require municipal advisors to step into the activities of issuers and issuer responsibilities under the federal securities laws," a power that the exchange act does not give the self-regulator.

Many groups, including the Government Finance Officers Association, NAMA, and BDA, also criticized the proposal for leaving MAs in the position to make a judgement about the materiality and need to disclose a bank loan when that power arguably should be left to the issuer.

Artin said the requirement could make MAs liable for antifraud violations under federal securities law because they could be considered the "makers" of the statement by disclosing, even though the issuer is the one who prepares it. Even if MAs were not considered "makers," Artin argued they could still be subject to aiding and abetting liability.

Issuers' concerns about potential liability as well as their possible desires to avoid bank loan or private placement disclosures may lead some to avoid hiring municipal advisors, several groups argued, which would undermine the purpose of the rule and the benefits of issuers hiring experienced advisors.

Heaton, echoing other comments, said the concept is problematic because there are numerous bank loans and direct purchases that are done without a municipal advisor. Other groups said that MAs who participate in transactions sometimes are not involved in negotiating the loan terms and may lack the required knowledge to make effective disclosures.

The groups offered several proposals of their own to bolster bank loan disclosure, including amending Rule 15c2-12 to include bank loans and private placements as a material event that is required to be disclosed. They also said EMMA should be improved in this area.

SIFMA, BDA, and George K. Baum said the 15c2-12 amendments would be the most comprehensive way to tackle the disclosure problem. Norwood suggested the MSRB could include non-dealer MAs working on direct placements under Rule G-32, which requires dealer MAs that prepare official statements for issuer clients to make electronic versions of the document are promptly made available after issuers approve the distribution of the statements.

Ben Watkins, Florida's director of bond finance, was one of several commenters who said again that the MSRB needs to make it easier for issuers to upload their bank loan disclosures on EMMA. He

suggested the MSRB provide a recommended threshold on the size of bank loans for which disclosures should be made.

The Bond Buyer

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