

MEMO# 24897

January 21, 2011

MSRB Proposes Pay-to-Play Rule for Municipal Advisors

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TO: FIXED-INCOME ADVISORY COMMITTEE No. 9-11
MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 3-11
SEC RULES MEMBERS No. 15-11 RE: MSRB PROPOSES PAY-TO-PLAY RULE FOR MUNICIPAL ADVISORS

The Municipal Securities Rulemaking Board (“MSRB”) has issued a proposal, creating Rule G-42, to establish pay-to-play rules for municipal advisors, and to make conforming changes to existing MSRB rules. [\[1\]](#) The proposal is modeled after MSRB Rule G-37, governing municipal dealers, and Securities and Exchange Commission (“SEC”) Rule 406(4)-5, governing investment advisers. [\[2\]](#)

I. Prohibitions

The proposal includes a number of prohibitions designed to prevent the influence of an award of business by government officials by making or soliciting political contributions. These provisions include:

- Prohibiting a municipal advisor from receiving compensation [\[3\]](#) for engaging in municipal advisory business with a municipal entity beginning on the date a covered political contribution is made, and ending two years after all municipal advisory business with the municipal entity has been terminated;
- Prohibiting a municipal advisor from soliciting third-party business from a municipal entity for compensation, or receiving compensation, for two years after the date of a covered political contribution;
- Prohibiting a municipal advisor and municipal advisor professional (“MAP”) from soliciting political contributions, or coordinating political contributions, on behalf of (1) an official of a municipal entity with which the advisor is engaging, or is seeking to engage in, municipal advisory services business, or is seeking business on behalf of a third-party; or (2) a political party of the state or locality of such municipal entity; and
- Prohibiting municipal advisors and MAPs from committing indirect violations of the proposal.

II. Key Terms

Municipal Advisor

A municipal advisor would mean a person who engages in municipal advisory business (i.e., provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities) or solicits a municipal entity on behalf of a third-party broker, dealer, municipal securities dealer, municipal advisor, or investment adviser. [\[4\]](#)

Municipal Advisor Professional

A MAP would mean any associated person of a municipal advisor that is: engaged in municipal advisory business with a municipal entity; solicits municipal advisory business from a municipal entity on its own behalf or solicits third-party business; is a supervisor of any person who is a MAP; is part of the supervisory chain up through and including the Chief Executive Officer or similarly situated official; or is a member of the municipal advisor's executive or management committee or similarly situated officials.

III. Look-back Provision

The proposal would include various look-back periods that would trigger the compensation ban. Generally, there would be a two-year look-back period for MAPs who engage in municipal advisory business. The ban would not apply to contributions made before the effective date of the proposed Rule G-42, with the exception of contributions made by dealer financial advisors already subject to MSRB Rule G-37. A MAP who solicits a municipal entity would only be subject to the two-year look-back if a contribution was made to an official of a municipal entity that the new MAP has solicited. In addition, a person who is a MAP because of his or her supervisory role or because he or she is a member of the municipal advisor's executive or management committee would be subject to a six-month look-back.

IV. Exemptions

The proposal would include several exemptions from the proposed prohibitions. First, it would include an exemption for de minimis contributions of up to \$250 per election to a candidate for which a MAP is entitled to vote. Second, it would include an automatic exemption for when a MAP contributes within the \$250 limit but is not entitled to vote for the candidate. The exemption would become effective if the municipal advisor discovers the contribution within four months and a refund is obtained within sixty days of discovery. Third, the proposal would include a discretionary exemption whereby the MSRB could grant an exemption to a municipal advisor based on a number of factors.

V. Disclosure and Recordkeeping Requirements

The proposal would require quarterly disclosures to the MSRB of certain contributions and related information on proposed Form G-42. Specifically, municipal advisors would be required to publicly disclose all covered contributions to officials of a municipal entity, payments to political parties of states and political subdivisions, and contributions to bond ballot campaigns made by municipal advisors, MAPs, their political action committees, and non-MAP executive officers. [\[5\]](#)

The proposal would require municipal advisors to keep records of the items (discussed above) required to be disclosed to the MSRB for at least six years. In addition, municipal advisors would be required to keep records of:

- Names, titles, and city/county and state of residence of MAP's and non-MAP executive officers;
- States in which the advisor is engaging or is seeking to engage in municipal advisory business, or solicit a municipal entity for a third-party;
- Municipal entities with which the advisor has engaged in municipal advisory business during the current year and the prior two calendar years, and the type of business engaged in; and
- Municipal entities that the advisor solicited on behalf of a third-party during the current year and the prior two calendar years, the nature of the business solicited, and the third-party (including, among others, an affiliate) on whose behalf the solicitation occurred.

VI. Changes to MSRB Rule G-37 and G-38

The proposal would make conforming changes to Rule G-37 including removal of all references to "financial advisory services." It also would specify that MAPs would include associated persons who are "engaged" in municipal advisory business rather than "primarily engaged," as per Rule G-37. In addition, if a MAP engages in municipal advisory business or solicits third-party business, as well as other activities, the individual's supervisors for both types of activities would be considered MAPs.

The proposal seeks comment on whether G-38 should be eliminated. In the alternative, it seeks comment on whether it should be expanded to include a prohibition on payments by non-dealer municipal advisors to other municipal advisors for the solicitation of municipal advisory business.

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endnotes

[1] MSRB Notice 2011-04, Request for Comment on Pay to Play Rule for Municipal Advisors (January 20, 2011) ("Release"), available at <http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2011/2011-04.aspx>. Comments are due to the MSRB by February 25, 2011.

[2] See Political Contributions by Certain Investment Advisers, Release No. IA-2910 (August 7, 2009), available at <http://www.sec.gov/rules/proposed/2009/ia-2910.pdf> and Rules Implementing Amendments to the Investment Advisers Act of 1940, Release No. IA-3110 (November 19, 2010), available at <http://www.sec.gov/rules/proposed/2010/ia-3110.pdf>.

[3] Compensation would mean any economic benefit to the municipal advisor.

[4] In conjunction with proposed amendments to the SEC's pay-to-play rule, the Release notes that persons soliciting advisory business from municipal entities on behalf of their affiliates do not qualify as "municipal advisors," but they would be allowed to voluntarily

register as such.

[\[5\]](#) “Non-MAP executive officer” means an associated person who is in charge of a principal business unit, division or function of the advisor, or who performs a similar policy-making function for the advisor.

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