

MEMO# 19231

October 7, 2005

MSRB ADOPTS RULE AMENDMENTS RELATING TO GIFTS AND OTHER NON- CASH COMPENSATION WITH IMMEDIATE EFFECTIVE DATE

©2005 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [19231] October 7, 2005 TO: 529 PLAN ADVISORY COMMITTEE No. 29-05 529 PLAN MEMBERS No. 16-05 RE: MSRB ADOPTS RULE AMENDMENTS RELATING TO GIFTS AND OTHER NON- CASH COMPENSATION WITH IMMEDIATE EFFECTIVE DATE As we previously informed you, in June, the Municipal Securities Rulemaking Board published for comment proposed amendments to MSRB Rules G-20, relating to gifts and gratuities given by brokers, dealers, or municipal securities dealers (collectively "broker- dealers") and MSRB Rule G-8, relating to recordkeeping.¹ The revisions conform the MSRB's rules to the NASD's rules governing non-cash compensation arrangements.² On October 3, 2005, the Securities and Exchange Commission approved the MSRB's proposed amendments.³ These amendments, which were effective as of their approval by the SEC, are summarized below. RULE G-20(b), THE NORMAL BUSINESS DEALINGS EXCEPTION Rule G-20(a) prohibits a broker-dealer from giving or permitting to be given any thing or service of value in excess of \$100 per year to a person, other than an employee, if such payment or service is in relation to the municipal securities activities of such person. Rule G- 20(b) has always excepted from this general prohibition occasional gifts of meals or sports and entertainment tickets and sponsorship of business functions. The amended rule imposes conditions on these exceptions. In particular, the rule now requires that the occasional gift or meal or ticket that is given or permitted to be given by the broker-dealer be hosted by the broker- dealer, meaning that the broker-dealer's personnel must accompany recipients of the gift. Similarly, for a business function to qualify for the rule's exception, it must now be sponsored by 1 See Memorandum to 529 Plan Advisory Committee No. 23-04 [17679], June 15, 2004. 2 See NASD Rule 2830(I)(5), which governs non-cash compensation arrangements, and Rule 3060, which requires broker-dealers to maintain records of specified gifts and gratuities. 3 See MSRB Notice 2005-52, SEC Approves Amendments to Rule G-20, on Gifts and Gratuities, and Rule G-8, on Books and Records (Oct. 5, 2005) ("MSRB Notice"). A copy of the MSRB Notice is available on the MSRB's website at: <http://www.msrb.org/msrb1/whatsnew/2005-52.asp>. 2 the broker-dealer. This section of the rule has also been revised to provide that such gifts shall not be so frequent or extensive as to raise any question of propriety. RULE G-20(d), NON-CASH COMPENSATION IN CONNECTION WITH PRIMARY OFFERINGS A new subsection (d) has been added to Rule G-20 to govern non-cash compensation in connection with primary offerings.

This new subsection prohibits a broker-dealer or any of its associated persons, directly or indirectly, from accepting or making payments or offers of payments of any non-cash compensation. The following non-cash compensation arrangements are exceptions to this general prohibition:

- Gifts that do not exceed \$100 per individual per year and are not preconditioned on achievement of a sales target;
- Occasional gifts of meals or tickets to theatrical, sporting, and other entertainments, provided that such gifts are not so frequent or so extensive as to raise any question of propriety and are not preconditioned on achievement of a sales target;
- Payment or reimbursement by offerors in connection with meetings held by an offeror or by a broker-dealer for the purpose of training or education of its associated persons provided that:
- Associated persons obtain the prior approval of the broker-dealer to attend the meeting and attendance is not preconditioned by the broker-dealer on achievement of a sales target or any other incentives pursuant to a permitted non-cash compensation arrangement;
- The location is appropriate to the purpose of the meeting, which shall mean an office of the broker-dealer, a facility located in the vicinity of such office, a regional location with respect to regional meetings, or a location at which a significant asset, if any, being financed or refinanced in the primary offering is located; and
- The payment or reimbursement is not preconditioned by the offeror on achievement of a sales target or any other permitted non-cash compensation arrangement;
- Non-cash compensation arrangements between a broker-dealer and its associated persons, or a company that controls the broker dealer and the associated persons of the broker-dealer provided that:
- The non-cash compensation arrangement is based on the total production of associated persons with respect to all municipal securities within respective product types distributed by the broker-dealer;
- The non-cash compensation arrangement requires that the credit received for each municipal security within a municipal security product type is equally weighted; and
- No entity that is not an associated person of the broker-dealer participates directly or indirectly in the organization of a permissible non-cash compensation arrangement; and
- Contributions by any person other than the broker-dealer to a non-cash compensation arrangement between a broker-dealer and its associated persons provided that the arrangement meets the criteria relating to non-cash compensation above.

3 RULE G-20(e), DEFINITIONS Rule G-20 has additionally been revised to add the following definitions for the following terms used in the rule:

- Non-cash compensation – means any form of compensation received in connection with the sale and distribution of municipal securities that is not cash compensation, including but not limited to merchandise, gifts and prizes, travel expenses, meals, and lodging.
- Cash compensation – means any discount, concession, fee, service fee, commission, asset-based sales charge, loan, override or cash employee benefit received in connection with the sale and distribution of municipal securities.
- Offeror – means, with respect to a primary offering of municipal securities, the issuer, any adviser to the issuer (including but not limited to the issuer’s financial adviser, bond or other legal counsel, or investment or program manager in connection with the primary offering), the underwriter of the primary offering, or any persons controlling, controlled by, or under common control with any of the foregoing. With respect to a primary offering of any municipal fund securities, based upon a recommendation made by the Institute, the term also includes any person considered an offeror under NASD Rules 2710, 2820, or 28304 in connection with any securities held as assets of or underlying such municipal fund securities.
- Primary offering – means any primary offering as defined in Securities Exchange Act Rule 15c2-12(f)(7).

5 RULE G-8, RECORDKEEPING Rule G-8 has been amended to require a broker-dealer to maintain records of all non- cash compensation paid under Rule G-20. Such records shall include the name of the person or entity making the payment, the names of the associated persons receiving the payments (if applicable), and the nature (including the location of any training or education meetings, if applicable), and value of the non-cash compensation received.

Tamara K. Salmon Senior Associate Counsel 4 NASD Rules 2710, 2820, and 2830 govern, respectively, Corporate Finance Underwriting Terms and Arrangements, Variable Contracts of an Insurance Company, and Investment Company Securities. 5 SEC Rule 15c2-12(f)(7) under the Securities Exchange Act defines a “primary offering” as: [A]n offering of municipal securities directly or indirectly by or on behalf of an issuer of such securities, including any remarketing of municipal securities (i) that is accompanied by a change in the authorized denomination of such securities from \$100,000 or more to less than \$100,000, or (ii) that is accompanied by a change in the period during which such securities may be tendered to an issuer of such securities or its designated agent for redemption or purchase from a period of nine months or less to a period of more than nine months.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.