

COMMENT LETTER

December 29, 2014

ICI Files Comment Letter with SEC Opposing MSRB's "One-Size-Fits-All" Qualification Examination for Municipal Advisors (pdf)

December 29, 2014 Mr. Brent Fields, Secretary U.S. Securities and Exchange Commission
100 F Street, N.E. Washington, D.C. 20549 Re: MSRB Rule G-3 Relating to Qualification
Requirements For Municipal Advisors; File No. SR-MSRB-2014-08 Dear Mr. Fields: The
Investment Company Institute (ICI)¹ is writing in response to the SEC's request for
comment on amendments proposed to Municipal Securities Rulemaking Board (MSRB) Rule
G-3, which is the MSRB rule governing standards of professional qualification and testing
requirements.² As proposed, the revised rule would require each municipal advisory
principal and representative³ to pass a qualification examination. The Institute fully
supports municipal advisory representatives being required to pass an examination to
demonstrate minimum competency because we believe that such a requirement is in the
best interests of investors. We recommend, however, that the MSRB reconsider utilizing a
single competency examination that is not specifically tailored to the type of advice being
rendered by a representative.

¹ The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$17.4 trillion and serve more than 90 million shareholders. ² See Notice of Filing of a Proposed Rule Change Consisting of Proposed Amendments to MSRB Rule G-1, on Separately Identifiable Department or Division of a Bank; G-2, on Standards of Professional Qualification; G-3, on Professional Qualification Requirements; and D-13, on Municipal Advisory Activities. SEC Release No. 34-73708 (Dec. 1, 2014) ("SEC Release"). ³ As used throughout this letter, the term "municipal advisory representative" is intended to refer to both principals and representatives. Mr. Brent Fields, Secretary December 29, 2014 Page 2 In summary, and as discussed in detail below, consistent with our previous comments to the MSRB on this issue,⁴ we recommend that the MSRB reconsider its current approach to develop only one examination for representatives because, in our view, this approach: will result in use of an examination that does not sufficiently test competencies relevant to the advisory representative's business; and is inconsistent with the approach self-regulatory organizations have long taken to ensure that any examination a representative is required to take is matched to that representative's duties and functions. We are concerned that, by using one examination, the MSRB will be

unable to tailor the examination to the type of advice the representative will render, a result that is not in the interests of municipal advisers' clients. We recommend instead that the MSRB utilize at least two examinations – one for representatives of a municipal advisor whose advisory activities are limited to municipal fund securities and one for representatives whose advice is limited to municipal securities other than municipal fund securities.⁵ TESTING RELEVANT COMPETENCIES Our recommendation that the MSRB tailor the examinations required of municipal fund advisors is intended to address the very significant differences between municipal advice relating to municipal fund securities, such as 529 college savings plans, and those relating to municipal securities other than municipal fund securities.⁶ Indeed, the relevant knowledge and competencies necessary for a municipal advisor representative will vary significantly depending upon the type of advice he or she renders. For example, providing advice on municipal securities likely requires a representative to be knowledgeable about issues such as negotiated prices, debt limits and ratios, underwriting periods, agreements, par values, etc. None of these topics would be relevant for a municipal advisor whose advisory business is limited to providing advice relating to a municipal fund security such as an interest in a 529 education savings plan. Expecting a municipal advisory representative whose work relates exclusively to municipal fund securities to pass an examination that would qualify such persons to advise municipal clients on bond underwritings and the terms and conditions of bonds is the equivalent of requiring a broker-dealer representative whose business is limited to the offer and sale of mutual funds to qualify for that position by passing an examination designed for representatives selling fixed income securities. These are not fungible business lines for broker-dealers and they should not be treated as such in the investment advisory business. As discussed below, the MSRB itself acknowledges through the qualification requirements it currently imposes on representatives of municipal securities

4 See Letter from the undersigned to Ronald W. Smith, Corporate Secretary, MSRB, dated May 9, 2014, which was filed in response to Request for Comment on Establishing Professional Qualification Requirements for Municipal Advisors, MSRB Notice No. 2014-08 (March 17, 2014) ("ICI March Letter"). 5 As discussed in more detail below, in lieu of developing a new, separate examination for the former, the MSRB could recognize the Series 6 examination as the required qualifying examination. 6 For the ease of discussion, as used in this letter subsequently, the term "municipal securities" is intended to mean municipal securities other than municipal fund securities. Mr. Brent Fields, Secretary December 29, 2014 Page 3 dealers the differences in necessary competencies between representatives of those dealers that sell municipal fund securities and those that sell municipal securities.⁷ In the interest of advisory clients, it seems equally important for the MSRB similarly to tailor the examination that a municipal advisor representative must pass to the competency necessary for the type of advice that will be rendered. We strongly believe that the MSRB should create at least two qualification examinations – one for municipal advisors whose business is limited to municipal fund securities and one for advisers whose business involves providing advice on municipal securities.⁸ CONSISTENCY WITH THE SELF-REGULATORY ORGANIZATIONS' APPROACH TO CURRENT EXAMINATION REQUIREMENTS While we recognize that our recommendation of two examinations may impose additional burdens on the MSRB, this approach to competency examinations is wholly consistent with the manner in which self-regulatory organizations, including the MSRB and FINRA, have long implemented examination requirements. For example, MSRB Rule G-3(a)(ii) requires every representative of a municipal securities dealer to pass the "Municipal Securities Representative Examination" (i.e., the Series 52 examination). Importantly, however, the rule provides an exception for any representative whose "activities with respect to municipal securities . . . are limited solely to municipal fund securities." In lieu of the Series 52 examination, such persons may

instead satisfy the qualification requirements by passing the “Limited Representative – Investment Company and Variable Contracts Products Examination” (i.e., the Series 6 examination). This exception was added to MSRB Rule G-3 in 2000. The MSRB explained the rationale for this change as follows: The Board understands that municipal fund securities may not have features typically associated with more traditional municipal securities. Instead, their features are similar to those of investment company securities. Although Board rules generally have been drafted to accommodate the characteristics of debt securities, the Board believes that most current rules can appropriately be applied to municipal fund securities. Nonetheless, the Board feels that certain rules should be amended to recognize the unique characteristics of municipal fund securities.⁹

⁷ As discussed below, municipal securities dealers’ representatives who sell fixed income securities must pass the Series 52 examination, which tests the representative’s knowledge of fixed income securities, fixed income markets, and the MSRB’s rules, while those selling 529 plan securities must pass the Series 6 examination. ⁸ Representatives who provide advice on both municipal fund securities and municipal securities would be required to pass both examinations. ⁹ See Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the MSRB Relating to Municipal Fund Securities, SEC Release No. 34-43066 (July 21, 2000) at p. 46. A footnote to this excerpt provides in relevant part as follows: “Municipal fund securities generally provide investment return and are valued based on the investment performance of an underlying pool of assets having an aggregate value that may increase or decrease from day-to-day, rather than providing interest payments at a stated rate or discount, as is the case for more traditional municipal securities. In addition, unlike Mr. Brent Fields, Secretary December 29, 2014 Page 4 We believe that the Board’s recognition of the need to distinguish the examination requirements imposed on municipal securities dealers based upon whether the product sold is a municipal security or a municipal fund security should also inform the Board’s approach to developing examinations for municipal advisor representatives. FINRA, too, has long required that the examination taken by a representative be tailored to the activities in which the representative will engage. At last count, representatives of FINRA member firms were required to pass one or more of the forty-two examinations that FINRA offers.¹⁰ Each of these examinations has been specifically designed to assess the competency of the test-taker in the areas covered by the examination. We have long supported the efforts of self-regulatory organizations such as the MSRB and FINRA to use multiple examinations, each of which is tailored to the nature of the representative’s business. We encourage the MSRB to adhere to this long-standing practice in developing appropriate examinations to assess the competency of municipal advisor representatives.¹¹ PROTECTING ADVISORY CLIENTS THROUGH TAILORED EXAMINATIONS As noted in the SEC Release, “the qualification examination is intended to determine whether a municipal advisor representative meets a minimum level of competency.”¹² We agree that this should be the regulatory premise underlying a qualification examination. We disagree, however, that one generic examination will be sufficient to assess all representatives’ competency without regard to the nature of the advice they will render. Instead, the required examination should be tailored to the type of advice the representative will provide – i.e., advice relating to municipal fund securities, municipal securities, or both. A government client interested in seeking advice on a bond offering would be ill advised to consult a representative whose knowledge and experience relates to municipal fund securities, just as a state administering a 529 plan likely would be ill served by a municipal advisor representative who is well versed only in bond offerings. We believe that advisory clients would be better served if the representatives they consult have demonstrated competency to render the type of advice sought. This approach is consistent with that of FINRA, which uses forty-two different examinations to better ensure that

representatives only serve in those roles for which they have

traditional municipal securities, these interests do not have stated par values or maturity dates and cannot be priced based on yield or dollar price.” See *id.* at n. 24. 10 A list of these forty-two examinations is available on FINRA’s website at:

<http://www.finra.org/industry/compliance/registration/qualificationsexams/qualifications/p011096>. 11 We additionally note that the idea of multiple examinations tailored to a registrant’s business is wholly consistent with the provisions of Section 15B(b)(2)(A) of the Securities Exchange Act, which expressly authorizes the MSRB to “appropriately classify . . . municipal advisors taking into account relevant matters, including types of business done, nature of securities other than municipal securities sold, and character of business organizations . . .” in developing standards of competence and other qualifications for municipal advisors and their associated persons. 12 SEC Release at p.16. Mr. Brent Fields, Secretary December 29, 2014 Page 5 demonstrated competence. We believe that the MSRB should utilize a similar approach with its required examinations because such an approach would better serve the interests of investors. THE MSRB’S RESPONSE TO THE INSTITUTE’S CONCERNS The SEC Release acknowledges the Institute previously raising the above discussed concerns with the MSRB when it published its proposal for public comment. According to the SEC Release: The [MSRB] appreciates ICI’s contention that the activities of municipal advisors who provide advice to municipal entities regarding municipal fund securities are different than the municipal advisory activities of traditional municipal advisors. The MSRB also acknowledges that some of the content on the examination will not be directly related to municipal fund securities. Nevertheless, the Board believes that individuals who engage in municipal advisory activities regarding municipal fund securities should demonstrate knowledge of the rules and regulations governing municipal advisors by taking the municipal advisor representative qualification examination.¹³ [Emphasis added.] We very much appreciate the MSRB’s previous consideration of our comments. We disagree, however, with the MSRB’s view that it is possible to test municipal advisors’ knowledge of the MSRB’s rules in a manner that is divorced from the nature of the advice (i.e., advice related to municipal bonds vs. 529 plan securities). Indeed, even fundamental concepts addressed by the MSRB’s rules – such as suitability, fair dealing, and disclosure requirements – may differ depending upon the nature of the advice rendered. For all the reasons discussed in this letter, we continue to believe that government clients of municipal advisors would be better served by requiring municipal advisor representatives to pass an examination whose content is “specifically related to the municipal advisory activities or the regulation of such activities.”¹⁴ Requiring all municipal advisor representatives to pass the same examination without regard to the nature of the advice they provide fails to satisfy this standard and fails to serve the best interest of their government clients. ■ ■ ■ ■ Based on the above, we strongly recommend that the MSRB reconsider its plans to develop a single examination to assess the minimum competency of all municipal advisor representatives without regard to the type of advice they render. We instead recommend that the MSRB utilize two examinations – one for those municipal advisors whose business is limited to the business of municipal fund securities and one for all other municipal advisors.¹⁵ As discussed above, this approach: will

13 SEC Release at p. 21. 14 SEC Release at p. 23.

This quote explains the MSRB’s rationale for rejecting commenters’ recommendations that it recognize the Series 7 or 52 examinations in lieu of the proposed new examination for municipal advisor representatives. 15 As discussed in the ICI March Letter, in lieu of developing a separate examination for municipal advisor representatives whose business is limited to providing advice on municipal fund securities, the MSRB could permit such persons to qualify Mr. Brent Fields, Secretary December 29, 2014 Page 6 ensure that the

new examination does, in fact, assess the representative's competency to render the type of advice rendered; is wholly consistent with the current examination requirements imposed by the MSRB and FINRA on municipal securities dealers and broker-dealers, respectively; and would better serve investment advisory clients. We appreciate the opportunity to provide these comments and your consideration of them. If you have any questions, please contact the undersigned at (202) 326-5825. Sincerely, /s/ Tamara K.

Salmon Senior Associate Counsel

by passing the

Series 6 examination. This alternative would avoid much of the regulatory effort and costs associated with developing and maintaining a new, additional examination tailored to this business and would ensure that the qualification requirement imposed on persons who render advice on municipal fund securities is relevant to their advisory activities. According to the SEC Release, the MSRB's response to the Institute's recommendation is that "passing the Series 6 examination would demonstrate only a basic competency in servicing retail customers who purchase mutual funds, interests in 529 college savings plans and variable annuities and, hence, would not establish an individual's competency as a municipal advisor representative." We disagree with this assessment. In our view it fails to recognize that, in order to pass the Series 6 examination, a representative must demonstrate familiarity with applicable regulatory requirements. These are the very same requirements that the MSRB is proposing to impose on municipal advisors either through tailoring its existing rules to include municipal advisory activities within their scope (see, e.g., proposed amendments to Rule G-20, relating to gifts, gratuities, and non-cash compensation to extend its provisions to municipal advisors) or proposing to ensure consistency in the regulatory standards applicable to municipal securities dealers and municipal advisors (see, e.g., MSRB Rule G-44, relating to a municipal advisor's supervisory obligations, which largely tracks MSRB Rule G-27, relating to a municipal securities dealer's supervisory obligations). As a result, the Series 6 will demonstrate basic competency with applicable regulatory requirements. For this reason, we continue to believe that passage of the Series 6, which is specifically tailored to the types of products on which a municipal advisor whose business is limited to municipal fund securities would render advice, should be an acceptable examination for municipal advisor representatives.