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Client Alert

Current Issues Relevant to Our Clients

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SEC's Municipal Advisor Rules and MSRB Rule G-23

The SEC's final municipal advisor registration rules will become effective on January 13, 2014. The SEC rules have created controversy within the municipal bond community about whether an underwriter will continue to be able to visit clients and pitch ideas without being prohibited from underwriting a resulting bond issue under MSRB Rule G-23.

Various industry groups, such as NABL and SIFMA, are requesting clarification from the SEC on this issue. NABL is reporting that it expects the SEC to issue additional guidance on the municipal advisor rules prior to the January 13, 2014 effective date.

MSRB Rule G-23 is primarily a conflicts of interest rule that prohibits a broker-dealer who is serving as a financial advisor for an issue of municipal securities from switching roles and acting as an underwriter of those securities. MSRB's guidance on Rule G-23 states that a broker-dealer can avoid being deemed to be a financial advisor by clearly disclosing in writing, at the earliest stages of its relationship with the issuer, that it is seeking to act as an underwriter and not as a financial advisor with a fiduciary duty. Once such disclosure is made, Rule G-23 permits an underwriter to make a sales pitch to the issuer without concern of being prohibited from underwriting that issue.

The SEC's municipal advisor rules state that broker-dealers who provide "advice" to municipal issuers and do not have any exemption from the rules (such as a response to an RFP, advice to an issuer who has an independent municipal advisor, or advice given after the broker-dealer has been engaged as an underwriter) are acting as municipal advisors and owe a fiduciary duty to the issuer. In its adopting release for the final rules, the SEC stated that it will broadly construe "advice" to include any communication to a municipal entity or obligated person that includes a recommendation, an expression of opinion or that includes information that is "particularized" to a municipal entity or obligated person. Much of the commentary to date has involved discussions of how a broker-dealer can avoid being considered a municipal advisor in this context.

Many broker-dealer firms will likely register as municipal advisors so, even if they provide pitch books or other pre-engagement information to a municipal entity or obligated person that constitute "advice" under the SEC rules, they will not be in violation of the registration requirements of the SEC rules. Absent an exclusion or exemption, the fiduciary duty will attach to any communication that constitutes "advice." While some broker-dealers may be willing to subject themselves to the fiduciary duty, it is not clear that all broker-dealers will be willing to assume this duty.

The SEC rules do not refer to MSRB Rule G-23 or to the exception that is in MSRB Rule G-23 for broker-dealers who make written disclosures to the issuer that they are acting as underwriters when making sales pitches. As a result, at the present time it is not clear whether a broker-dealer that (a) identifies itself as a prospective underwriter, (b) makes the disclosures required by MSRB Rule G-23 and (c) then provides "advice" within the meaning of the SEC rules will nonetheless be deemed to be a financial advisor for purposes of MSRB Rule G-23 and therefore be prohibited from acting as an underwriter with respect to the securities that are the subject of the advice under MSRB Rule G-23.

Chapman's analysis of the final rules, *U.S. Securities and Exchange Commission Final Municipal Advisor Registration Rules*, is available here. For a copy of the final rules, click here.

For More Information

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