American Bankers Association

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[redacted]

VIA ELECTRONIC MAIL

May 29, 2015

Mr. Brent J. Fields, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 10549

Re: File Number SR–MSRB–2015–03
Proposed New Rule G–42 on Duties of Non-Solicitor Municipal Advisors

Dear Mr. Fields:

The American Bankers Association (ABA)[1] is responding to the request for comment by the Securities and Exchange Commission (Commission) on Proposed rule G-42 of the Municipal Securities Rulemaking Board (MSRB) to establish the core standards of conduct and duties of municipal advisors when engaging in municipal advisory activities. Among the proposed core standards there is a treatment of conduct consistent with the fiduciary duty[2] owed by a municipal advisor to its municipal entity clients, which includes, without limitation, a duty of care and of loyalty. Concomitantly, subsection (e)(i) of Proposed Rule G-42 would prohibit specific activities that the MSRB believes could be highly likely to conflict with the duty of loyalty and the duty of care applicable to municipal advisors, including a prohibition on certain transactions by a municipal advisor or its affiliate acting in a principal capacity. ABA is appreciative of the MSRB's efforts to tailor better the scope of the prohibition on principal transactions to the potential for conflict that may arise for different types of municipal advisors. We nonetheless remain concerned about the impact of the prohibition as currently proposed on the ability of commercial banks or their affiliates that are also registered municipal advisors to offer a full range of banking services to their municipal entity clients.

Discussion

Subsection (e)(ii) of Proposed Rule G-42 would prohibit a municipal advisor to a municipal entity, and any affiliate of such municipal advisor, from engaging in a principal transaction directly related to the same municipal securities transaction or municipal financial product as to which the municipal advisor is providing or has provided advice. In subsection (f)(i), the proposed rule further defines the term "engaging in a principal transaction" to mean "when acting as a principal for one's own account, selling to or purchasing from the municipal entity client any security or entering into any derivative, guaranteed investment contract, or other similar financial product with the municipal entity client."

[1] The American Bankers Association is the voice of the nation's $15 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $11 trillion in deposits and extend more than $8 trillion in loans.

[2] The Dodd-Frank Act (Pub. Law No. 111-203, 2010) amended Section 15B of the Securities Exchange Act of 1934 to establish a regulatory regime for municipal advisors and expressly imposes on municipal advisors a statutory fiduciary duty to municipal entity clients. Section 15B(c)(1), 12 U.S.C. § 78*o*-4(c)(1).

The MSRB has proposed this definition to respond to commenters, including ABA, who expressed concern about the impact of a principal transaction prohibition on the ability of banking organizations to conduct normal, day-to-day banking business with municipal entities. Unlike other securities markets firms that provide services primarily in an agency capacity, banking organizations offer traditional banking services, such as deposits and loans, in a principal capacity. In addition banking organizations are required, pursuant to federal banking law, to operate through a variety of affiliates and subsidiaries that would be within the scope of the "common control" definition in the statute. As a result, without such a limitation, a bank or banking organization that includes a municipal advisor would not be able to provide ordinary banking services to a municipal entity advised by the organization's municipal advisor.[3]

However, Proposed Rule G-42 as submitted to the Commission has, for the first time, included within the scope of the term "other similar financial products" (that are within the prohibition on principal transactions), a "bank loan but only if it is in an aggregate principal amount of $1,000,000 or more and is economically equivalent to the purchase of one or more municipal securities." According to the filing, the MSRB's concern is that the provision of a bank loan by a municipal advisor's affiliated bank could present conflicts with the municipal advisor's fiduciary duty to provide only advice that is in the best interest of its municipal entity client.

ABA believes there are circumstances in which that concern is without foundation, and we seek a clarification from the Commission for the following type of situation.

> Assume a bank-affiliated municipal advisor recommends, consistent with its fiduciary duty, that undertaking a bank loan would best serve a municipal entity client's purposes and that the client should solicit bidders for the loan through the use of a Request for Proposals. The municipal entity undertakes the RFP and receives four or five bids, including one from the municipal advisor's bank. To best serve its taxpayers, the municipal entity *itself* chooses which bid to accept, which in this case is from the affiliated bank. *The bank expects and intends to hold the loan on its books until maturity*.

ABA believes that several factors in this scenario substantially mitigate the conflict about which the MSRB is concerned. First, the use of the RFP process provides a neutral process by which the municipal entity client can obtain bids from interested lenders beyond the municipal advisor's affiliated bank. Moreover, where the decision about which bid to select lies with the municipal entity, the municipal entity is free to make its choice based on the factors most appropriate for the municipality and its taxpayers.

Second, when a bank holds the loan on its books until maturity the potential conflict at the heart of the MSRB's concern is substantially mitigated because the interests of both the municipal entity and the bank are in alignment. To offer a loan to a municipal entity that will be kept on its books, a bank must satisfy both its own internal as well as regulatory underwriting standards (for which it will be examined by bank regulators). It must also demonstrate to its own Loan Committee or other approval body that the municipal entity will be a good credit and will be able to repay the loan, because it is retaining 100 percent of the credit risk. In this situation, the bank's interests are wholly aligned with those of the municipal entity – each party wants funding that serves the latter's particular needs *and that can be repaid.*

[3] A banking organization may have a registered municipal advisor within the bank as a separately identifiable department (SID) or it may include a separately registered municipal advisor that would be an affiliate of the bank. In this letter the use of "affiliated bank" is intended to cover both the situation in which (1) the bank SID is the municipal advisor and the bank offers the loan and (2) the municipal advisor is a separate entity and its affiliate bank offers the loan.

The alignment of interests of the bank and the municipal entity differentiates the bank loan situation from that of a broker-dealer underwriting the issuance of municipal bonds, the latter being a context in which the underwriter retains no monetary risk once the transaction is completed. We note that in developing Proposed Rule G-42, the MSRB has drawn primarily on regulatory regimes found in the securities markets, including broker-dealers, municipal securities dealers, and registered investment advisers. By contrast, the bank regulatory and examination regime focuses on safety and soundness issues, including the quality and risk character of loans.

Accordingly, we urge the SEC and the MSRB in a final rule to exclude from the above prohibition on principal transactions bank loans provided in the context described above.[4] If you have any questions about the foregoing, please do not hesitate to contact me.

Sincerely,

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Center for Securities, Trust & Investment

[4] Our request could be effected with language in Paragraph .11 of the Supplementary Material such as: "Such a bank loan is not subject to the prohibition where it has been proffered through a neutral RFP process and the bank intends to hold the loan on its books until maturity."