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September 30, 2011

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: SR-MSRB-2011-09

The National Association of Independent Public Finance Advisors ("NAIPFA") appreciates the opportunity to provide comments on draft Rule G-17 (“G-17”). NAIPFA's comments are provided in the spirit that the rule being established will ensure that issuers can rely on receiving unbiased advice and that the issuer remains in control of their debt issuance process.

The Municipal Securities Rulemaking Board ("MSRB") has made great strides in protecting frequent, sophisticated issuers by setting forth proposed requirements in G-17 for underwriters. NAIPFA is concerned, however, that G-17 may not protect the infrequent and/or small, unsophisticated issuers. There are over 50,000 issuers of municipal bonds and most of these tend to be infrequent issuers from small and unsophisticated municipal entities. NAIPFA believes that additional changes need to be made to G-17 to protect these issuers.

Issuer Confusion

NAIPFA believes that the best protection the MSRB could provide to issuers would be to eliminate an underwriter's ability to provide advice such as is allowed under Rule G-23.[1] NAIPFA reiterates that Rule G-23's allowance of the giving of advice by underwriters is inconsistent with the Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), and, as G-17 illustrates, the fact that underwriters are allowed to do so presents an enormous challenge to the MSRB who is now congressionally mandated to protect the interests of issuers while fairly regulating the activities of underwriters and municipal advisors. NAIPFA believes that most of the disclosures required under G-17 could be eliminated if underwriters were to be prohibited from providing advice.

However, in the absence of such a change, NAIPFA agrees with the assessment made by the Securities Industry Financial Markets Association ("SIFMA") that the requirements of G-17 create a "fiduciary lite" standard.[2] As a result, NAIPFA believes that the appearance of a "fiduciary lite" standard, created by G-17, will confuse municipal issuers as to the role their

[1] NAIPFA acknowledges that a change to G-23 could result from a unilateral action by the MSRB or as the result of further clarification stemming from the release of the SEC's final rule on municipal advisor registration.

[2] *See*, File No. SR-MSRB-2011-09, at 19.

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underwriter is playing.[3] Further, absent a change to Rule G-23, NAIPFA believes that a number of the disclosures are inconsistent with the free market system and undermine the "arm's length" commercial nature of the transaction by confusing the issuer as to the role being played by the underwriter.

NAIPFA is concerned that, rather than giving issuers protection against fraud and manipulation, these disclosures could in fact encourage manipulative practices due to the perceived level of trust that accompanies them.[4] When an issuer is presented with disclosures stating, for example, that the pricing with which they have been given is “fair and reasonable”, this will undoubtedly lead issuers, even sophisticated ones, to conclude that their underwriter is not acting in an arm’s length commercial transaction. Right or wrong, the perception created will cause issuers to unduly trust their underwriter which, in turn, will allow underwriters to influence the issuer’s decision making process. As a result, municipal issuers will be dissuaded from or even unaware they should be engaging in the vigorous negotiation that is required as part of an arm’s length commercial transaction. This undermines the free market system and is inconsistent with any notion of just and equitable principles of trade. Furthermore, this is not the intended result of the Dodd-Frank Act, and is contrary to its purpose as well as the purpose of all of the resulting regulations.

Therefore, NAIPFA requests that in the absence of a change to Rule G-23 eliminating an underwriter’s ability to provide advice, that G-17 be amended to require a disclosure that makes it clear that an underwriter is no replacement for a municipal advisor. As NAIPFA has stated in prior letters regarding underwriter disclosures, any regulatory framework put in place for disclosures should contain certain elements which make it clear that an underwriter (i) is not acting as an advisor but as an underwriter, (ii) is not a fiduciary to the issuer but rather a counterparty dealing at arm's length, (iii) has conflicts with issuers because they represent the interests of the investors or other counterparties, (iv) seek to maximize their profitability, and (v) have no continuing obligation to the issuer following the closing of the transaction. A disclosure taking into account these elements would eliminate any confusion on the part of the issuer and would clearly establish that the issuer should not rely on the advice provided by an underwriter.

Process for Presenting Required Disclosures to Issuers

In the absence of an amendment to Rule G-23 eliminating an underwriter's ability to provide advice to a municipal issuer, NAIPFA requests that the process required to be utilized by an underwriter for presenting disclosures be amended to require no less than what is required of

[3] NAIPFA is concerned that the confusion created by draft Rule G-17 will undermine the purpose of the Dodd-Frank Act, which was enacted to clarify the roles of the various market participants while minimizing the confusion that existed in the market as to the role played by underwriters.

[4] This is potentially even more true and troubling with regard to infrequent, unsophisticated issuers.

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municipal advisors. NAIPFA disagrees with the MSRB's approach with regard to the process by which underwriters must present disclosures to issuers. Unlike municipal advisors who are bound by a fiduciary duty to their issuer clients, underwriters have no such duty, and as a result, in the absence of a clear showing of fraud or manipulation, cannot be held accountable by municipal issuers for their actions or advice.

Consequently, NAIPFA believes that the MSRB has misplaced the regulatory burdens of disclosure onto municipal advisors. Under the municipal advisor portion of proposed Rule G-17 and proposed Rule G-36, municipal advisors are required to undertake a much more rigorous disclosure process than underwriters. NAIPFA believes this is the wrong approach since underwriters, unlike municipal advisors, cannot be held liable for the advice they provide to an issuer with regard to the structure, timing or terms of a securities issuance.[5] However, rather than require underwriters to engage in a rigorous disclosure process, the MSRB has determined to require the opposite, namely, a minimal and blurry disclosure process for underwriters and a rigorous disclosure process for municipal advisors. NAIPFA disagrees with this approach, and requests that in the absence of an amendment to Rule G-23 that underwriters be required to undertake at least as rigorous of a disclosure process as municipal advisors.

To further illustrate NAIPFA's concern, consider the following:

Under G-17, an underwriter is required to make disclosures "in writing to an official of the issuer whom the underwriter reasonably believes had the authority to bind the issuer by contract with the underwriter." This differs significantly from the process that has been proposed for municipal advisors. Under draft Rule G-36 and the draft municipal advisor portion of Rule G-17, a municipal advisor "*must receive written consent to its conflicts* by an official of the municipal entity that the municipal advisor reasonably believes has authority to bind the municipal entity by contract."[6] Under these rules, a municipal advisor must obtain written consent from the issuer, even though the municipal advisor is bound to serve as a fiduciary to the municipal issuer, whereas an underwriter who is not bound to act in the issuer's best interest is only required to present the disclosures. NAIPFA believes that at a minimum, underwriters should be required to obtain informed consent from the issuer.

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5 Under Rule G-23, underwriters are permitted to give advice with regard to the structure, timing, terms and other matters of a municipal issuance so long as they make certain “disclosures” in writing. These “disclosures”, however, will be drafted as disclaimers of liability and will do much more than merely “disclose” that the underwriter is acting in an arm’s length commercial transaction.

6 MSRB Notice 2011-48, *MSRB Files Municipal Advisor Fiduciary Duty Rule and Interpretive Notice*, August 23, 2011 (emphasis added); *See*, MSRB Notice 2011-49, *MSRB Files Interpretive Notice Concerning the Application of MSRB Rule G-17 to Municipal Advisors Advising Obligated Persons or Soliciting Municipal Entities on Behalf of Others*, August 24, 2011.

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Potentially more troubling, however, is the fact that unlike municipal advisors who usually enter into contracts with municipal issuers early on in the financing process, underwriters generally only enter into contracts with municipal issuers at the very end of the transaction. This concerns NAIPFA in two respects. First, NAIPFA is concerned that G-17 creates a situation whereby underwriter disclosures cannot be made to an official of the issuer until the very end of the transaction. Due to the municipal financing process, underwriters typically do not enter into contracts until the end of the transaction; underwriters are aware of this, and underwriters understand that up until the day of sale, the issuer is not bound to them by contract or otherwise. Therefore, it is not until this point that an underwriter will have a reasonable belief that an official has the authority to bind the issuer by contract. Thus, an underwriter will violate G-17 if it provides disclosures prior to an official action being taken by the municipal entity. As a result, NAIPFA's second concern is that it will be impossible for such disclosures to be given "in sufficient time before the execution of a contract [...] to allow the official to evaluate the recommendation." Since it is highly unlikely that an underwriter will have a reasonable belief that an official of the issuer has the authority to bind the issuer by contract prior to an official action by the municipal issuer on the date of sale, it is hard to imagine how disclosures could be made to an official of the issuer in sufficient time before the execution of a contract.

Therefore, NAIPFA respectfully requests that G-17 be amended to require underwriters to obtain informed consent from the municipal issuer's governing body and that any disclosures made pursuant to G-17 be made to the officials of the municipal entity with the power to bind the issuer. For purposes of illustration, in the case of cities, towns, villages, etc. these disclosures would go before the elected board or council, who would then give their consent to the disclosures. Because underwriters, unlike municipal advisors, do not have a fiduciary duty and generally do not enter into contracts until the end of the financing process, NAIPFA believes that this suggested amendment presents a reasonable and superior alternative to what has been presented in G-17 and more effectively protects the interests of municipal issuers by ensuring that disclosures will be made to the appropriate official(s) and by allowing the individuals who receive the disclosures sufficient time to review and evaluate them.

Alternatively, an underwriter should be prohibited from presenting its disclosures to municipal issuer officials based merely on a "reasonable belief". As noted above, NAIPFA is concerned that an underwriter will only have a reasonable basis for believing an official can bind it and the issuer to a contract when an official action is taken by the municipal entity's governing body, such as an action approving the bond purchase agreement. Therefore, NAIPFA believes that G-17 should be amended to prohibit the giving of disclosures based on a "reasonable belief" and should instead require an underwriter to have actual knowledge as to whether an official has the power to bind the issuer by contract. Under this alternative, an underwriter will have actual knowledge or will be able to obtain such knowledge when an official action by the municipal entity is taken with regard to the engagement of the underwriter. NAIPFA believes that this is a better standard than current G-17 because an official action by a municipal entity is a public

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record and, as such, the underwriter will be able to obtain knowledge with relative ease as to whether a particular official has the authority to bind the issuer. This amendment will ensure that disclosures are made to the appropriate official which, ultimately, will better protect the interests of the municipal entity.[7]

Eliminate the "Fair and Reasonable" Pricing Disclosure

NAIPFA requests that the concept put forth regarding the implied representation that the price an underwriter pays in a negotiated sale be "fair and reasonable", be replaced with the concept that the price an underwriter pays be "not unreasonable". NAIPFA agrees with the assessment put forth by the Bond Dealers of America and SIFMA that "the fair pricing obligation in the context of a new issue should employ a good faith standard[,] that there is no prevailing market price for new issues[, and] that an underwriter should only be required to purchase securities at the price that it and the issuer negotiated and agreed to in good faith, without regard to a prevailing market price."[8] In addition, NAIPFA believes that putting in place a fair and reasonable pricing requirement is inconsistent with an arm's length commercial transaction, places an unnecessary burden on the underwriting community, and is unnecessary to "promote just and equitable principles of trade."

Although NAIPFA disagrees with the MSRB's prescription, NAIPFA appreciates the MSRB's attempt to protect issuers of municipal securities from fraudulent and manipulative acts and practices, and promote just and equitable principles of trade, while still emphasizing the duty of fair dealing owed by underwriters to municipal issuers. Further, NAIPFA agrees that "simple principles of fair dealing require that underwriters have more than a *caveat emptor* relationship with their issuer clients."[9] However, NAIPFA believes that the dictates of the rule prohibiting fraud and manipulation are sufficient. What is more, NAIPFA fears that imposing a fair and reasonable fee standard is inconsistent with an arm's length commercial transaction[10] and could have a chilling effect on the market. NAIPFA is concerned that such a requirement could cause underwriting firms to exit the market out of fears of liability from having to affirmatively state that their pricing is fair and reasonable. The recent stimulus bond programs give a perfect illustration of why a fair and reasonable pricing mandate is unmanageable. Under the stimulus bond programs, how could the first underwriter state that their pricing was fair and reasonable when no other comparable issues existed in the market? NAIPFA believes that in situations such as this, the fair and reasonable pricing standard could well have an impact on whether an underwriter brings an issue to market. Conversely, NAIPFA believes that a "not unreasonable" standard strikes the appropriate balance between upholding the MSRB's goal of limiting

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7 Even under this approach, however, NAIPFA is concerned that municipal issuers will not have sufficient time prior to entering into a contract with the underwriter to review and evaluate the G-17 disclosures.

8 *See id.* at 18.

9 *Id.* at 20.

10 Discussed, *supra*, at 1-2.

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manipulative acts and encouraging fair dealing, while allowing underwriters and the free market to function more efficiently.

Notably, however, NAIPFA would not be opposed to eliminating this disclosure altogether if G-23 were to be amended to eliminate an underwriter's ability to provide advice. NAIPFA believes that such a change would clarify the role of an underwriter and would eliminate confusion on the part of the issuer as to the motivations of the underwriter, which would in turn put the issuer on notice that they need to engage in an aggressive arm's length commercial negotiation with their underwriter.

Minimize Disclosures When A Municipal Advisor Is Engaged

The need for numerous disclosures would appear to be minimized when the issuer of municipal securities engages a municipal advisor to act on their behalf. For example, when a municipal advisor is engaged, the requirement that an underwriter provide a disclosure regarding the "fair and reasonable" nature of their fee seems to be unnecessary. In addition, it would also seem unnecessary to require underwriters to provide disclosures on matters such as complex financings, or payments to and from third parties. NAIPFA has not undertaken an exhaustive analysis of what disclosures may be made irrelevant when a municipal advisor is engaged on a transaction, but it is clear to NAIPFA that many of the disclosures could be eliminated or minimized in that situation. Therefore, NAIPFA respectfully requests that the MSRB conduct an analysis of what aspects of a municipal financing are to be the responsibility of the municipal advisor. At the conclusion of this analysis, the MSRB should then amend G-17 to eliminate all underwriter disclosures that overlap areas of the financing covered by the role of the municipal advisor.

Compensation Disclosures

In the absence of an amendment to Rule G-23 that eliminates an underwriter's ability to provide advice, NAIPFA respectfully requests that underwriters be required to provide a disclosure in the same manner and to the same extent as what was put forth in the draft municipal advisor portion of Rule G-17. Underwriter compensation is based primarily on the size and type of an issuance. Therefore, if an underwriter is going to be allowed to provide advice to an issuer of municipal securities regarding matters such as the structure and terms of the securities, there exists at least the appearance of a significant incentive for the underwriter to advise the issuer to either issue a larger amount of securities than they may have otherwise thought necessary, or issue a different kind of security that may not be in the best interest of the municipal entity.[11] Thus, it is

[11] NAIPFA is aware of situations in which certain state and federal loan programs have been available to issuers,

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imperative that the underwriter be required to disclose to an issuer and obtain their informed consent, in writing, that the form of their compensation creates a conflict of interest.[12]

Issuer Protection

The MSRB has gone to great lengths describing the disclosures that are needed to inform municipal issuers as to the various aspects of the municipal financing. This approach is based on the assumption that "the typical fixed rate offering may be presumed to be well understood". NAIPFA believes that for small and/or infrequent issuers this assumption is not necessarily true. It cannot be assumed that small and/or infrequent issuers fully understand such transactions. Therefore, NAIPFA respectfully requests that G-17 be amended to take into consideration the needs of unsophisticated municipal issuers.

To accomplish this, NAIPFA proposes that a less rigid disclosure system be adopted that would require an underwriter to assess the knowledge and understanding of municipal issuers on a case by case basis. To help underwriters determine whether an issuer has the requisite knowledge and understanding required to nullify the need for disclosures, the MSRB could put forth guidance as to the factors an underwriter can look to in making a determination. For example, the conclusion that an issuer is knowledgeable could be justified if the issuer has completed one or more public offerings within the last two years.[13] Another factor could be the amount of outstanding securities that an issuer has. For example, such a factor could be whether the issuer had outstanding within the past five-years more than $100 million of securities.

NAIPFA believes that such an approach strikes an appropriate balance between the needs of infrequent, unsophisticated issuers and underwriters. This approach would ensure that small and/or infrequent municipal issuers are made aware of the nature of the transaction when they do not have the necessary knowledge to make informed decisions. In addition, this approach is flexible enough to give underwriters the ability to avoid making disclosures when such disclosures are unnecessary.

Underwriter Duties in Connection With Issuer Disclosure Documents

NAIPFA has concerns regarding underwriter duties in connection with issuer disclosure documents. NAIPFA agrees with the following MSRB assessment:

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but rather than attempting to access these programs underwriters have advised municipal entities to issue securities. In addition, underwriters often charge different fees based on the type of security issued, which could cause an underwriter to recommend the issuance of one type of security over another.

[12] *See*, MSRB Notice 2011-49.

[13] Given the fluidity within the regulatory landscape, NAIPFA believe a two-year window is appropriate.

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> It would seem a curious result [] for the underwriter not to be required under rule G-17 to have a reasonable basis for its own representations set forth in the official statement, as well as a reasonable basis for the material information it provides to the issuer in connection with the preparation of the official statement, including a reasonable belief in the truthfulness and completeness of any information provided by others that serves as a material basis for such underwriter's information.[14]

However, NAIPFA wishes to point out that there would still exist two different standards of accountability between underwriters and municipal advisors who prepare official statements. Underwriters may only be held accountable if they do not have a reasonable belief as to the truthfulness and completeness of any information provided. However, municipal advisors are likely to be required to "make reasonable inquiries in order to help ensure the appropriate disclosures are made in the official statement" as part of their fiduciary responsibilities.[15] Therefore, NAIPFA respectfully requests that when an underwriter intends to assist in the preparation of an official statement that a disclosure be made to the issuer stating that the underwriter can only be held liable where it can be shown that they did not act with a reasonable belief that the information presented was truthful and complete. Such a disclosure would assist municipal issuers in better understanding the nature of their relationship to the underwriter and would ensure that issuers understand that they may have a difficult time holding their underwriter responsible if their official statement is found to contain material misstatements or omissions.

Disclosure on Reimbursement From Bond Proceeds

Absent a change in Rule G-23 to eliminate an underwriter's ability to provide advice, NAIPFA requests that, in the absence of a disclosure and informed consent, underwriters be prohibited from seeking reimbursements from bond proceeds for expenditures made on behalf of the issuer for any expenses incurred by the underwriter. NAIPFA is concerned that in a situation where the underwriter provides advice to the issuer of municipal securities, the underwriter could, without fraud or manipulation, recommend to the issuer that it be reimbursed for expenses, such as, travel to a rating meeting. In such a case, the underwriter should be required to provide to the issuer a disclosure stating that: "Expenses made in connection with the issuance of securities were incurred by the underwriter on behalf of the issuer, but that the issuer is under no obligation to issue additional bonds to reimburse the underwriter for these expenditures." This disclosure would ensure that issuers are made aware that the expenditures were legitimate expenses made in

[14] *See*, File No. SR-MSRB-2011-09, at 18.
[15] *See*, MSRB Notice 2011-48 (although this rule has been withdrawn from SEC consideration, NAIPFA does not anticipate further changes will be made with respect to a municipal advisor's duty of inquiry or duty of care).

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connection with the issuance of securities, but that the issuer is not obligated to issue additional bonds to reimburse the underwriter for these expenses. This will allow the municipal issuer to fully consider an underwriter's advice with regard to whether they should issue additional bonds for the purpose of reimbursing the underwriter.

Conclusion

NAIPFA hopes these comments provide insight into our concerns with regard to draft Rule G-17 and also its interface with an underwriter's ability to provide advice. We believe a large number of issuers are infrequent and/or small issuers. NAIPFA remains very concerned that these issuers will not be adequately protected and will be confused about the differing roles of underwriters and municipal advisors. Consequently, the suggested amendments detailed in this comment letter would provide much needed additional clarity to these issuers. In addition, NAIPFA hopes that additional clarifications regarding the roles of underwriters and municipal advisors will be forthcoming in the final municipal advisor registration rule due to be released at the end of this year.

NAIPFA believes all issuers should expect to receive and should receive unbiased advice. As such, NAIPFA reiterates its belief that advice should only be provided parties acting as municipal advisors with prescribed fiduciary duties. However, because the current regulatory framework allows for the provision of advice by underwriters, NAIPFA believes that draft Rule G-17 must require comprehensive and timely disclosures with regard to the conflicts that exist when an underwriter provides services to a municipal issuer that go beyond merely buying and selling securities.

Therefore, NAIPFA postulates that small and/or infrequent issuers would benefit from having:

1. All underwriting disclosures presented to the governing body by the underwriter when the underwriter is retained at the onset of the project, and that those disclosures be made to the municipal entity's governing body;
2. The initial underwriting disclosures contain (a) the basis for compensation, (b) a statement to the effect that the basis for compensation is a conflict of interest that could cause the underwriter to recommend that the size of the issuance be larger than is necessary, (c) a statement that sets forth that an underwriter is not a municipal advisor and that the issuer should consult a municipal advisor if they wish to obtain unbiased advice, and (d) a statement, when applicable, that an official statement prepared from the underwriter’s perspective is produced under a different standard than the fiduciary standard of a municipal advisor;

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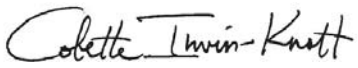
3. A standard for ascertaining the issuer's capacity and knowledge with regard to certain kinds of issuances of securities and, if necessary, ascertain whether a particular security is suitable for that particular issuer;
4. The concept of "fair and reasonable" pricing be modified so that the issuer is not confused as to the arm's length commercial nature of the transaction; and
5. Underwriters be prohibited from being reimbursed for expenses absent their obtaining informed, written consent from the issuer.

Sincerely,



Colette J. Irwin-Knott, CIPFA
President, National Association of Independent Public Finance Advisors

cc: The Honorable Mary L. Schapiro, Chairman
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Troy A. Paredes, Commissioner
Liban Jama, Counsel to Commissioner Aguilar
Lynnette Hotchkiss, Executive Director, Municipal Securities Rulemaking Board