

CDIAC Webinar
Regulatory Update: The Municipal Advisory Rules
and Their Effect on Public Investments
June 23, 2014

Questions and Answers

Advice

1. Broker-dealers in general either receive "reverse inquiries" or solicit transactions through their salesforce. For example, a salesperson will often solicit a client to purchase or sell security based on a call from the trading desk.

While a reverse inquiry would not be recommendation and, accordingly, would not be advice under the Municipal Advisor Rules, a solicitation could be considered advice under the Rule. Significantly, one is a municipal advisor only if advice relates to investment of bond proceeds or municipal escrow investments.

2. Is it considered "advice" under the Rule for a broker-dealer to select a security from its pool of investments rather than provide the public agency with its complete inventory?

The Municipal Advisor Rules expressly provide that "advice" excludes, among other things, the provision of general information that does not involve a recommendation regarding municipal financial products or the issuance of municipal securities ("general information exclusion"). In the Adopting Release, the Commission provided certain examples of general information, including information of a factual nature without subjective assumptions, opinions, or views, and information that is not particularized to a specific municipal entity or type of municipal entity. FAQ 1.1 provides examples of the general information exclusion from advice, one of which is for

information regarding a financial institution's currently-available investments (e.g., the terms, maturities, and interest rates at which the financial institution offers these investments) or price quotes for investments available for purchase or sale in the market that meet criteria specified by a municipal entity or obligated person

3. Does a broker-dealer provide advice under the Rule if it sells securities to a Registered Investment Advisor ("RIA") firm managing an account for an issuer that includes bond proceeds?

A broker-dealer is considered to be providing advice even when that advice is provided indirectly to a municipal entity. The SEC staff advised in FAQ 1.3 as follows:

[A] market participant who provides advice directly to a municipal entity or obligated person or indirectly to a municipal entity or obligated person through a third-party professional engaged by such municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities would be required to register with the Commission as a municipal advisor.

4. May a county investment portfolio manager ask a broker for advice as to where is the “sweet spot” in the market so that a specific request for an investment may be made by the public agency?

A response that includes only general market information would not be considered “advice” under the Municipal Advisor Rule. The issue is how “objective” is the response – for example, does the response only illustrate a yield curve or does it require analyzing data and making a recommendation? In the latter case, it is more likely that advice is provided.

The RFP/RFQ Exemption

5. May a mini RFP be issued which includes the daily scope of services expected of broker dealers?

A response to a mini-RFP is exempt from the Municipal Advisor Rules under RFP/RFQ exemption.

6. Please explain the limitation on compensation under the RFP exemption.

The RFP exemption prohibits the payment of compensation in connection with or for the response from the broker-dealer. The Municipal Advisor Rules do not prescribe rules for the payment of an underwriter selected pursuant to a RFP for its services in connection with the sale and purchase of the securities.

7. Are there model forms for a RFP and RFQ which would avail a responder to the RFP/RFQ exemption?

There are model forms for RFPs and RFQs posted on the GFOA and SIFMA websites which comport with the RFP/RFQ exemption.

The IRMA Exemption

8. Are Financial Advisors that are affiliated with broker-dealers able to utilize the IRMA exemption?

A Financial Advisor that does not otherwise want to become a Municipal Advisor under the Rules is not precluded from utilizing the IRMA exemption.

9. Must a broker-dealer communicate with the IRMA or may it talk directly with the public agency in order to comply with the IRMA exemption?

The public agency may communicate with either the broker-dealer directly or through the IRMA. Reliance on the IRMA exemption does not require that communication go through the IRMA.

10. Does the Rule or the Release prescribe standards for the IRMA’s scope of services?

The scope of an IRMA’s responsibilities are not prescribed by the Municipal Advisor Rules. The services contract between the public agency and IRMA may establish the scope of the responsibilities of the IRMA.

11. How are IRMAs compensated?

The compensation terms of the IRMA are not proscribed by the Municipal Advisor Rule and may be determined as decided by the public agency.

The Bank Exemption

12. Is a bond trustee holding indenture funds a Municipal Advisor?

No.

Miscellaneous

13. Are trading desks able to provide issuers with a pricing range or spread that a deal should be priced within or will they be limited to providing data from specific comparable financings that have priced recently?

The Underwriter Exclusion will likely apply when pricing advice is related to a financing for which the broker-dealer is the underwriter.

14. Broker-dealers, in their effort to comply with the Municipal Advisor Rules and to avoid being subject to the rules applicable to a municipal advisor, are requesting public agencies to sign letters and certificates. Please describe the scope of these letters and how public agencies should respond to these requests?

In order to avoid being characterized as a Municipal Advisor, broker-dealers have proposed that public agencies execute letters and confirmations from public agencies. Those letters include statements (i) confirmation that a broker-dealer has been engaged as an underwriter and therefore is entitled to the “underwriter exclusion,” (ii) establishing that an Independent Registered Municipal Advisor has been engaged and therefore the “IRMA exemption” may be available, or (iii) confirmation that investments are not being made for accounts that include bond proceeds or that are municipal escrow investments. Some of these proposed letters require the public agency to execute and return the signed letter in order to continue to do business with the broker-dealer, while some letters for bond proceeds that are on deposit prior to July 1 request, but do not require, a reply. Further, in some instances public agencies have delivered a letter to the broker-dealer that set forth facts and information on which the broker-dealer may rely upon to assure itself that it will not be considered a municipal advisor. Useful examples of letters and certificates that can be used as a template (which will need to be customized in each particular case) are posted on the GFOA and SIFMA websites.

15. What is the liability for a public agency if it fails to properly inform a broker-dealer that the investment includes bond proceeds?

There are no penalties proscribed against the public agency under the Municipal Advisor Rule. However, a broker-dealer who is unable to conclude that bond proceeds are not included in the proposed investment may be unable to make a recommendation regarding such investment.

16. Are investments of tax revenues (such as from ad valorem taxes) held as security for and a source of payment for bonds “proceeds” that are subject to the Municipal Advisor Rule?

Yes. “Bond proceeds” are defined to include:

any monies of a municipal entity or obligated person held in funds under legal documents for the municipal securities that are reasonably expected to be used as security or a source of payment for the payment of debt service on the municipal securities, including reserves, sinking funds, and pledged funds created for such purpose.