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TALKING POINTS FOR PUBLIC FINANCE BANKERS

SEC's New Municipal Advisor Registration Rules

Background

- The SEC's Municipal Advisor Rule was mandated by Section 975 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, passed in July of 2010.
- On September 18, 2013, the SEC approved final rules (the "Rules") governing the definition, registration and regulation of municipal advisors ("MAs").
- The SEC has released FAQs to help interpret provisions of the Rule, most recently revised on January 16, 2013.
- The Rules have the potential to fundamentally alter the way issuers interact with public finance bankers.
- The Rules are effective on July 1, 2014.

The Rules

- A "municipal advisor" is defined in the Rules as a person that provides advice to or on behalf of a municipal entity or obligated person (i.e., conduit borrower) with respect to (i) the issuance of municipal securities or (ii) municipal financial products (which includes derivatives, GICs and investment strategies involving the investment of municipal bond proceeds).
- Whether a communication is deemed to be "advice" is based on all relevant facts and circumstances, including whether the communication is a recommendation that is particularized to the specific needs, objectives, or circumstances of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities. Under this definition, many services currently provided by public finance bankers and many communications between bankers and their issuer or obligated person clients would be treated as "advice" for purposes of the Rules. Providing "advice" as defined in the Rules, and becoming an MA, creates a fundamental problem for public finance bankers. If a banker brings an idea or proposal to a client that is "particularized" to the client's situation and is deemed to be "advice" under the Rules, that banker would be deemed to be an MA (absent an exemption). MA

treatment brings with it a fiduciary duty to municipal entity clients (but not to obligated persons). The FAQ states that providing "advice" and triggering the fiduciary duty is incompatible with serving as an underwriter. Presenting a deal idea to a municipal entity client that triggers MA treatment would, therefore, preclude that firm from serving as an underwriter if the client were to execute a deal based on that idea.

Exemptions from MA Treatment

- The Rules provide for certain exemptions for firms from treatment as MAs, none of which is broad or inclusive.

  - *Underwriting Exemption* - The Rules provide that if a firm is engaged to serve as an underwriter on a specific transaction, activities that are integral to the purchase and distribution of that particular issuance are covered by the underwriting exemption. Serving in an underwriter pool does not permit the firm to rely on the underwriter exemption. In addition, the SEC provides a number of examples of activities that are not within the underwriter exemption, a number of which have historically been requested of underwriters by issuers.
  - *Independent Registered Municipal Advisor ("IRMA")* – Firms are exempt from MA treatment if the issuer has retained and will rely on an IRMA with respect to the same aspects on which the firm is providing ideas, provided the issuer represents in writing it has retained an IRMA and is relying on the IRMA's advice.
  - *Responses to RFPs* – This exemption applies when responding to an RFP, but not when providing unsolicited ideas or even when responding to issuers' informal requests for information or analysis.
  - *Exemptions for Banks* – Banks providing advice with respect to certain bank products would be exempted.

Implications of the Rules for Issuers

- Many issuers depend on deal ideas, analysis, suggestions and related services they receive from bankers outside of an underwriting engagement. The Rules will limit the ability of bankers to provide ideas, suggestions, analysis, assistance or other services to issuer clients in many circumstances outside of an underwriter engagement and may limit certain services normally provided even when engaged as an underwriter pool (without either the IRMA or RFP exemptions).
- There is no way for issuers to simply "opt out" of the Rules outside the narrowly tailored exemptions.