

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-65749; File No. SR-MSRB-2011-09]

### Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of Proposed Rule Change, as Modified by Amendment No. 2, Consisting of Proposed Interpretive Notice Concerning the Application of MSRB Rule G-17, on Conduct of Municipal Securities and Municipal Advisory Activities, to Underwriters of Municipal Securities

November 15, 2011.

On August 22, 2011, the Municipal Securities Rulemaking Board (“Board” or “MSRB”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) <sup>1</sup> and Rule 19b-4 thereunder, <sup>2</sup> a proposed rule change consisting of a proposed interpretive notice concerning the application of MSRB Rule G-17 (on conduct of municipal securities and municipal advisory activities to underwriters of municipal securities). The proposed rule change was published for comment in the **Federal Register** on September 9, 2011. <sup>3</sup> The Commission received 5 comment letters. <sup>4</sup> On October 11, 2011, the MSRB extended the time period for Commission action to December 7, 2011. On November 3, 2011, MSRB filed Amendment No. 1 to the proposed rule change. On November 10, 2011, MSRB withdrew Amendment No. 1, responded to comments in a letter, <sup>5</sup> and filed Amendment No. 2 to the proposed rule change. The proposed rule change, as modified by Amendment No. 2, is described in Items I and II below, which items have been prepared by MSRB. The Commission is publishing this notice to

solicit comments on the proposed rule change, as modified by Amendment No. 2, from interested persons.

#### I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The MSRB is filing with the SEC the Amendment to File No. SR-MSRB-2011-09, originally filed on August 22, 2011 (the “original proposed rule change”). The Amendment amends and restates the original proposed rule change consisting of a proposed interpretive notice (the “Notice”) concerning the application of MSRB Rule G-17 (on conduct of municipal securities and municipal advisory activities) to underwriters of municipal securities (as amended, the “proposed rule change”). A detailed description of the provisions of the Notice is set forth below. The MSRB has requested that the proposed rule change be made effective 90 days after approval by the Commission.

The text of the proposed rule change is available on the MSRB’s Web site at <http://www.msrb.org/Rules-and-Interpretations/SEC-Filings/2011-Filings.aspx>, at the MSRB’s principal office, and at the Commission’s Public Reference Room.

#### II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the MSRB included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

##### A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) With the passage of the Dodd-Frank Act, the MSRB was expressly directed by Congress to protect municipal entities. Accordingly, the MSRB is proposing to provide additional interpretive guidance that addresses how Rule G-17 applies to dealers in the municipal securities activities described below.

##### Scope of Notice

As clarified by the Amendment, the Notice would concern the duties of underwriters to municipal entity issuers of municipal securities (“issuers”). It

would not address the duties of underwriters to obligated persons. The Notice would not apply to selling group members and, unless otherwise specified, the Notice would apply only to negotiated underwritings and not to competitive underwritings.

##### Role of the Underwriter/Conflicts of Interest

The Amendment would add a new section to the Notice, which would provide for robust disclosure by an underwriter as to its role, its compensation, and actual or potential material conflicts of interest. The disclosure would build on the disclosure already required by the Rule G-23 interpretive notice approved by the Commission in May of this year. <sup>6</sup> Certain of the required disclosures could be made by a syndicate manager on behalf of other syndicate members. The Notice would also prohibit an underwriter from recommending that the issuer not retain a municipal advisor.

The required disclosures would generally be required to be made at the time the underwriter is engaged to provide underwriting services and to be made to an official of the issuer with the power to bind the issuer by contract with the underwriter. The disclosure concerning the arm’s-length nature of the underwriter-issuer relationship would continue to be required to be made at the earliest stages of the underwriter-issuer relationship, as required by the Rule G-23 interpretive notice. In the case of disclosures triggered by recommendations as to particular financings, as under the original proposed rule change, the disclosures would be required to be provided in sufficient time before the execution of a contract with the underwriter to allow the official to evaluate the recommendation. The disclosures required in the Notice under “Role of the Underwriter/Conflicts of Interest/Other Conflicts Disclosures” were included in the original proposed rule change. Pursuant to the Amendment, they would simply be included in the list of required disclosures, so that underwriters reviewing the Notice would only need to look to one place to see all the required conflicts disclosures. The underwriter would be required to attempt to obtain the written acknowledgement of the issuer to the required disclosures and, if the issuer would not provide such

<sup>6</sup> See SEC Release No. 34-64564, File No. SR-MSRB-2011-03 (May 27, 2011).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 65263 (September 6, 2011), 76 FR 55989.

<sup>4</sup> See Letters from Joy A. Howard, Principal, WM Financial Strategies, dated September 30, 2011 (“Howard Letter”); Mike Nicholas, Chief Executive Officer, Bond Dealers of America, dated September 30, 2011 (“BDA Letter”); Colette J. Irwin-Knott, CIPFA, President, National Association of Independent Public Finance Advisors, dated September 30, 2011 (“NAIPFA Letter”); Leslie M. Norwood, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association, dated September 30, 2011 (“SIFMA Letter”); and Susan Gaffney, Director, Federal Liaison Center, Government Finance Officers Association, dated October 3, 2011 (“GFOA Letter”).

<sup>5</sup> See letter from Margaret C. Henry, General Counsel, Market Regulation, MSRB, to Elizabeth M. Murphy, Secretary, Commission, dated November 10, 2011.

acknowledgement, to document that fact.

*Representations to Issuers.* The Notice would provide that all representations made by underwriters to issuers of municipal securities in connection with municipal securities underwritings (e.g., issue price certificates and responses to requests for proposals), whether written or oral, must be truthful and accurate and may not misrepresent or omit material facts.

*Required Disclosures to Issuers.* As clarified by the Amendment, the Notice would provide that an underwriter of a negotiated issue that recommends a complex municipal securities transaction or product (e.g., a variable rate demand obligation with a swap) to an issuer has an obligation under Rule G-17 to disclose all financial material risks (e.g., in the case of a swap, market, credit, operational, and liquidity risks) known to the underwriter and reasonably foreseeable at the time of the disclosure, financial characteristics (e.g., the material economic terms of the swap, the material terms relating to the operation of the swap, and the material rights and obligations of the parties during the term of the swap), incentives, and conflicts of interest (e.g., payments received from a swap provider) regarding the transaction or product. Underwriters would also be required to inform the issuer that there might be accounting, legal, and other risks associated with a swap and that the issuer should consult with other professionals concerning such risks. Such disclosure would be required to be sufficient to allow the issuer to assess the magnitude of its potential exposure as a result of the complex municipal securities financing. Disclosures concerning swaps would also be required to be made only as to the swaps recommended by underwriters. If an issuer decided to accept the recommendation of a swap provider other than the underwriter, the underwriter would have no disclosure obligation with regard to that other provider's swap.

In the case of routine financing structures, underwriters would be required to disclose the material aspects of the structures if the issuer personnel did not otherwise have knowledge or experience with respect to such structures. The Amendment would clarify that any disclosures required to be made with respect to routine financings would be based on the underwriter's "reasonable belief" that issuer personnel lack knowledge or experience with such structures and be linked to whether the underwriter had recommended the routine financing.

The disclosures would be required to be made in writing to an official of the issuer whom the underwriter reasonably believed had the authority to bind the issuer by contract with the underwriter (i) in sufficient time before the execution of a contract with the underwriter to allow the official to evaluate the recommendation and (ii) in a manner designed to make clear to such official the subject matter of such disclosures and their implications for the issuer. If the underwriter did not reasonably believe that the official to whom the disclosures were addressed was capable of independently evaluating the disclosures, the underwriter would be required to make additional efforts reasonably designed to inform the official or its employees or agent.<sup>7</sup>

*Underwriter Duties in Connection with Issuer Disclosure Documents.* The Notice would provide that a dealer's duty to have a reasonable basis for the representations it makes, and other material information it provides, to an issuer and to ensure that such representations and information are accurate and not misleading, as described above, extends to representations and information provided by the underwriter in connection with the preparation by the issuer of its disclosure documents (e.g., cash flows).

*New Issue Pricing and Underwriter Compensation.* The Notice would provide that the duty of fair dealing under Rule G-17 includes an implied representation that the price an underwriter pays to an issuer is fair and reasonable, taking into consideration all relevant factors, including the best judgment of the underwriter as to the fair market value of the issue at the time it is priced. The Notice distinguishes the fair pricing duties of competitive underwriters (submission of *bona fide* bid based on dealer's best judgment of fair market value of securities) and negotiated underwriters (duty to negotiate in good faith). The Notice would provide that, in certain cases and depending upon the specific facts and circumstances of the offering, the underwriter's compensation for the new issue (including both direct compensation paid by the issuer and

other separate payments or credits received by the underwriter from the issuer or any other party in connection with the underwriting) may be so disproportionate to the nature of the underwriting and related services performed, as to constitute an unfair practice that is a violation of Rule G-17.

*Conflicts of Interest.* The Notice would require disclosure by an underwriter of potential conflicts of interest, including the existence of third-party payments, values, or credits made or received, profit-sharing arrangements with investors, and the issuance or purchase of credit default swaps for which the underlying reference is the issuer whose securities the dealer is underwriting or an obligation of that issuer. The Amendment would clarify that the provisions of the Notice concerning disclosures of third-party payments and credit default swaps would require disclosure of the existence of third-party payments, but not the amount, and that particular transactions in credit default swaps would not be required to be disclosed under the Notice. These disclosures would draw the attention of issuers to such payments and credit default swap activity, and the issuers could choose to request more information from the underwriters.

*Retail Order Periods.* The Notice would remind underwriters not to disregard the issuers' rules for retail order periods by, among other things, accepting or placing orders that do not satisfy issuers' definitions of "retail."

*Dealer Payments to Issuers.* Finally, the Notice would remind underwriters that certain lavish gifts and entertainment, such as those made in conjunction with rating agency trips, might be a violation of Rule G-17, as well as Rule G-20.

(b) The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2) of the Securities Exchange Act ("Exchange Act"), which provides that:

The Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

Section 15B(b)(2)(C) of the Exchange Act, provides that the rules of the MSRB shall: be designed to prevent fraudulent and manipulative acts and practices, to promote

<sup>7</sup> Section 4s(h)(5) of the Commodity Exchange Act requires that a swap dealer with a special entity client (including states, local governments, and public pension funds) must have a reasonable basis to believe that the special entity has an independent representative that has sufficient knowledge to evaluate the transaction and its risks, as well as the pricing and appropriateness of the transaction. Section 15F(h)(5) of the Exchange Act imposes the same requirements with respect to security-based swaps.

just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.

The proposed rule change is consistent with Section 15B(b)(2) of the Exchange Act because it will 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 their customers. Rule G-17 has two components, one an anti-fraud prohibition, and the other a fair dealing requirement (which promotes just and equitable principles of trade). The Notice would address both components of the rule. The sections of the Notice entitled "Representations to Issuers," "Underwriter Duties in Connection with Issuer Disclosure Documents," "Excessive Compensation," "Payments to or from Third Parties," "Profit-Sharing with Investors," "Retail Order Periods," and "Dealer Payments to Issuer Personnel" primarily would provide guidance as to conduct required to comply with the anti-fraud component of the rule and, in some cases, conduct that would violate the anti-fraud component of the rule, depending on the facts and circumstances. The sections of the Notice entitled "Role of the Underwriter/Conflicts of Interest," "Required Disclosures to Issuers," "Fair Pricing," and "Credit Default Swaps" primarily would provide guidance as to conduct required to comply with the fair dealing component of the rule.

#### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The MSRB does not believe that the proposed rule change would impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act, since it would apply equally to all underwriters of municipal securities.

#### *C. Self-Regulatory Organization's Statement on Comments Received on the Proposed Rule Change Received From Members, Participants, or Others*

The MSRB has separately filed a comment letter with the Commission in which it discusses the responses to comment letters received by the Commission in response to the notice

for comment on the original proposed rule change published in the **Federal Register**.

#### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

By December 7, 2011 (which is the date that is 90 days after the date the notice of the original proposed rule change was published in the **Federal Register**) the Commission will:

- (A) By order approve or disapprove such proposed rule change, or
- (B) Institute proceedings to determine whether the proposed rule change should be disapproved.

#### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as modified by Amendment No. 2, is consistent with the Act. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-MSRB-2011-09 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-MSRB-2011-09. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing

also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-MSRB-2011-09 and should be submitted on or before December 1, 2011.<sup>8</sup>

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>9</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-65743; File No. SR-ICC-2011-04]

### **Self-Regulatory Organizations; ICE Clear Credit LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Schedule 502 of the ICC Rules To Provide for Clearing of Additional Single Name Investment Grade CDS Contracts**

November 14, 2011.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on November 7, 2011, ICE Clear Credit LLC ("ICC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared primarily by ICC. ICC filed the proposed rule change pursuant to Section 19(b)(3)(A)(iii)<sup>2</sup> of the Act and Rule 19b-4(f)(4)<sup>3</sup> thereunder so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

The purpose of proposed rule change is to provide for the clearance of the following additional investment grade

<sup>8</sup> The Commission believes that a 10-day comment period is reasonable, given the date for Commission action is December 7, 2011. The 10-day comment period will provide adequate time for comment.

<sup>9</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>3</sup> 17 CFR 240.19b-4(f)(4).