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Notice of Filing of a Proposed Rule Change Consisting of Proposed Amendments to Rule G–37, on Political Contributions and Prohibitions on Municipal Securities Business, Rule G–8, on Books and Records, Rule G–9, on Preservation of Records, and Forms G–37 and G–37x; Notices

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–76763; File No. SR–MSRB–2015–14]

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change Consisting of Proposed Amendments to Rule G–37, on Political Contributions and Prohibitions on Municipal Securities Business, Rule G–8, on Books and Records, Rule G–9, on Preservation of Records, and Forms G–37 and G–37x

December 23, 2015.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the ''Act'') [1] and Rule 19b–4 thereunder,[2] notice is hereby given that on December 16, 2015, the Municipal Securities Rulemaking Board (the ''MSRB'' or ''Board'') filed with the Securities and Exchange Commission (the ''SEC'' or ''Commission'') the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the MSRB. 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 MSRB filed with the Commission a proposed rule change consisting of proposed amendments to Rule G–37, on political contributions and prohibitions on municipal securities business, Rule G–8, on books and records to be made by brokers, dealers, municipal securities dealers, and municipal advisors, Rule G–9, on preservation of records, and Forms G–37 and G–37x (the ''proposed rule change''). The MSRB requested that the proposed rule change be approved with an effective date to be announced by the MSRB in a regulatory notice published no later than two months following the Commission approval date, which effective date shall be no sooner than six months following publication of the regulatory notice and no later than one year following the Commission approval date; provided, however, that any prohibition under Rule G–37 already in effect before the effective date of the proposed rule change shall be of the scope, and continue for the length of time, provided under Rule G–37 as in effect at the time of the contribution that resulted in such prohibition.

The text of the proposed rule change is available on the MSRB's Web site at *www.msrb.org/Rules-and-Interpretations/SEC-Filings/2015-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 MSRB 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

1. Purpose

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the ''Dodd-Frank Act'') amended Section 15B of the Exchange Act [3] to provide for the regulation by the Commission and the MSRB of municipal advisors and to grant the MSRB certain authority to protect municipal entities and obligated persons.[4] The Dodd-Frank Act establishes a federal regulatory regime that requires municipal advisors to register with the Commission [5] and prohibits municipal advisors from engaging in any fraudulent, deceptive, or manipulative act or practice.[6] The Dodd-Frank Act also grants the MSRB broad rulemaking authority over municipal advisors and municipal advisory activities.[7]

As charged by Congress, the MSRB is in the process of developing a comprehensive regulatory framework for municipal advisors and their associated persons, including the proposed amendments to Rule G–37.[8] The proposed rule change would extend to municipal advisors through targeted amendments to Rule G–37 the regulatory policies in Rule G–37 that address ''pay to play'' practices and the appearance thereof. ''Pay to play'' practices typically involve a person or an entity making cash or in-kind political contributions (or soliciting or coordinating others to make such contributions) to help finance the election campaigns of state or local officials or bond ballot initiatives as a *quid pro quo* for the receipt of government contracts. The proposed rule change would further the purposes of the Exchange Act, as amended by the Dodd-Frank Act, by addressing an area of potential corruption, or appearance of corruption, in connection with the awarding of municipal advisory business, which impedes a free and open market in municipal securities and may harm investors, issuers, municipal entities and obligated persons.

Such practices among municipal advisors create conflicts of interest and give rise to circumstances suggesting *quid pro quo* corruption involving public officials of municipal entities resulting from such conflicted interests and the receipt of political contributions. In the worst cases, such practices involve the actual corruption of public officials of municipal entities. Even if actual *quid pro quo* corruption does not occur, the appearance of *quid pro quo* corruption in the awarding of municipal advisory business (or municipal securities business or engagements to provide investment advisory services when a municipal advisor solicits on behalf of brokers, dealers or municipal securities dealers (''dealers'') or investment advisers) may be as damaging to the integrity of the

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] 15 U.S.C. 78*o*–4.

[4] Pub. L. 111–203, 124 Stat. 1376 (2010).

[5] *See* Section 15B(a)(1)(B) of the Exchange Act (15 U.S.C. 78*o*–4(a)(1)(B)).

[6] *See* Section 15B(a)(5) of the Exchange Act (15 U.S.C. 78*o*–4(a)(5)).

[7] *See* Section 15B(b)(2) of the Exchange Act (15 U.S.C. 78*o*–4(b)(2)).

[8] In furtherance of this framework, the MSRB adopted Rule G–44 regarding the supervisory and compliance obligations of municipal advisors. *See* Release No. 34–73415 (October 23, 2014), 79 FR 64423 (October 29, 2014) (File No. SR–MSRB–2014–06) (SEC order approving Rule G–44). The MSRB also adopted amendments to Rule G–20, on gifts, gratuities and non-cash compensation, to extend provisions of the rule to municipal advisors and Rule G–3 to establish registration and professional qualification requirements for municipal advisors. *See* Release No. 34–76381 (November 6, 2015), 80 FR 70271 (November 13, 2015) (File No. SR–MSRB–2015–09) (SEC order approving amendments to Rule G–20 on gifts, gratuities and non-cash compensation); and Release No. 34–74384 (February 26, 2015), 80 FR 11706 (March 4, 2015) (File No. SR–MSRB–2014–08) (SEC order approving registration and professional qualification requirements for municipal advisor representatives and municipal advisor principals) (''Order Approving MA Qualification Requirements''). The MSRB also proposed Rule G–42, regarding duties of non-solicitor municipal advisors. *See* Release No. 34–74860 (May 4, 2015), 80 FR 26752 (May 8, 2015) (File No. SR–MSRB–2015–03) (notice of filing and request for comment) (''Proposed Rule G–42 Filing''); Release No. 34–75737 (August 19, 2015), 80 FR 51645 (August 25, 2015) (notice of filing of Amendment No. 1 and request for comment); and Release No. 34–76420 (November 10, 2015) 80 FR 71858 (November 17, 2015) (File No. SR–MSRB–2015–03) (notice of filing of Amendment No. 2 and request for comment).

municipal securities market as actual *quid pro quo* corruption. Further, the appearance may breed actual *quid pro quo* corruption as municipal advisors may feel a need to make *quid pro quo* political contributions in order to be considered a candidate for the award of business that they believe will only be awarded to contributors.[9] Similarly, public officials may feel the need to engage in *quid pro quo* corruption in order to avoid a financial disadvantage to their campaigns as compared to other officials they believe engage in such practices. Even in the absence of actual *quid pro quo* corruption, the mere appearance of such corruption stifles and creates artificial barriers to competition for municipal advisors that believe that ''pay to play'' practices are a prerequisite to being awarded municipal advisory business (or municipal securities business or engagements to provide investment advisory services for broker, dealer, municipal securities dealer or investment adviser clients of a municipal advisor soliciting such business on behalf of clients) but are unwilling or unable to engage in such practices.

''Pay to play'' practices are rarely explicit: Participants typically do not let it be known that contributions or payments are made or accepted for the purpose of influencing the selection of a municipal advisor (or dealer, municipal advisor or investment adviser on behalf of which a municipal advisor acts as a solicitor).[10] Nonetheless, as discussed *infra,*[11] numerous developments in recent years have led the MSRB to conclude that, at least in some instances, the awarding of municipal advisory business (or municipal securities business or engagements to provide investment advisory services when a municipal advisor solicits on behalf of dealers or investment advisers) has been influenced, or has appeared to have been influenced, by ''pay to play'' practices.

In the Board's view, continued ''pay to play'' practices by professionals seeking or engaging in municipal advisory business (including municipal advisors soliciting municipal entities on behalf of dealers, municipal advisors and investment advisers) and the awarding of business by conflicted officials erodes public trust and confidence in the fairness of the municipal securities market, impedes a free and open market in municipal securities, may damage the integrity of the market, and may increase costs borne by municipal entities, issuers, obligated persons and investors. The MSRB believes that extending the policies embodied in Rule G–37 to municipal advisors through targeted amendments to Rule G–37 will help ensure common standards for dealers and municipal advisors, who operate in the same market, and frequently with the same clients.

Rule G–37

In the years preceding the MSRB's adoption of Rule G–37, widespread reports regarding the existence of ''pay to play'' practices had fueled industry, regulatory and public concerns, calling into question the integrity, fairness, and sound operation of the municipal securities market.[12] When proposing Rule G–37 in 1994, the Board believed, based on the Board's review of comment letters and other information, that there were ''numerous instances in which dealers have been awarded municipal securities business based on their political contributions.''[13] Moreover, in the Board's view, even when impropriety had not occurred:

> political contributions create a potential conflict of interest for issuers, or at the very least the appearance of a conflict, when dealers make contributions to officials responsible for, or capable of influencing the outcome of, the awarding of municipal securities business and then are awarded business by issuers associated with these officials.[14]

The problems associated with ''pay to play'' practices undermined investor confidence in the municipal securities market, which was essential to the liquidity and capital-raising ability of the market.[15] Further, such practices stifled and created artificial barriers to competition, thereby harming investors and the public interest and increasing market costs associated with the municipal securities business.[16] In light of these concerns, the Board determined that regulatory action was necessary to protect investors and maintain the integrity of the municipal securities market.[17] In approving Rule G–37 in 1994, the Commission affirmed that the rule was adopted ''to address the real as well as perceived abuses resulting from 'pay to play' practices in the municipal securities market.''[18] The Commission also noted that ''[Rule G–37] represents a balanced response to allegations of corruption in the municipal securities market.''[19]

Current Rule G–37 is a comprehensive regulatory regime composed of several separate and mutually reinforcing requirements for dealers. Chief among them are: Limitations on business activities that are triggered by the making of certain political contributions; limitations on solicitation and coordination of political contributions; and disclosure and recordkeeping regarding political contributions and municipal securities business.

This regime is widely recognized as having significantly curbed ''pay to play'' practices and the appearance of such practices in the municipal securities market.[20] Rule G–37 also has been used as a model by various federal regulators to create ''pay to play'' regulations in other segments of the financial services industry. Pursuant to the Advisers Act,[21] the SEC adopted Rule 206(4)–5 (the ''IA Pay to Play Rule''), which applies to investment advisers and political contributions.[22] The Commodity Futures Trading Commission subsequently adopted Rule 23.451, a rule regarding swap dealers

[9] Rule G–37 was first adopted in the wake of similar dealer concerns in the municipal securities market. *See Blount* v. *SEC,* 61 F.3d 938, 945–946 (D.C. Cir. 1995), *cert. denied,* 517 U.S. 1119 (1996) (''*Blount*'') citing Thomas T. Vogel Jr., *Politicians Are Mobilizing to Derail Ban on Muni Underwriters,* Wall St. J., December 27, 1993, (reporting about some officials rallying support for a boycott of firms that vowed to halt municipal campaign giving); John M. Doyle, *Muni Bond Market Faces Scrutiny Allegations Include Influence Peddling,* Cincinnati Post, March 1, 1994 (''Of primary concern to most reformers is the practice of 'pay to play,' the belief that political contributions by firms are necessary to compete for muni bond underwriting business''); John D. Cummins, *Blount* v. *SEC: An End for Pay-to-Play,* Bond Buyer, August 21, 1995 (noting that support for ''pay to play'' reform ''grew out of a desire to end the perceived abuses'' as well as ''individual bankers who were simply tired of writing checks to politicians'').

[10] *See Blount,* 61 F.3d at 945 (''While the risk of corruption is obvious and substantial, actors in this field are presumably shrewd enough to structure their relations rather indirectly. . . .''); *id.* (''[N]o smoking gun is needed where, as here, the conflict of interest is apparent, the likelihood of stealth great, and the legislative purpose prophylactic.'').

[11] *See infra,* nn. 99–102.

[12] *See* Release No. 34–33868 (April 7, 1994), 59 FR 17621, 17623 (April 13, 1994) (File No. SR–MSRB–94–02) (''Rule G–37 Approval Order'').

[13] *See* Release No. 34–33482 (January 14, 1994), 59 FR 3389, 3390 (January 21, 1994) (File No. SR–MSRB–94–02) (''Notice of Proposed Rule G–37'').

[14] *See id.* at 3390.

[15] *See id.*

[16] *See id.*

[17] *See id.*

[18] *See* Rule G–37 Approval Order, at 17624.

[19] *Id.* at 17628.

[20] *See* Release No. IA–3043 (July 1, 2010), 75 FR 41018, at 41020, 41026–41027 (July 14, 2010) (File No. S7–18–09) (SEC order adopting a rule regarding political contributions made by investment advisers pursuant to the Investment Advisers Act of 1940 (''Advisers Act''), (''Order Adopting IA Pay to Play Rule'')); *id.,* at n. 101 and accompanying text; comment letter from Sanchez, *infra,* n. 113; comment letter from SIFMA, *infra,* n. 113.

[21] *See* 15 U.S.C. 80b–1 *et seq.*

[22] 17 CFR 275.206(4)–5.

and political contributions, (the ''Swap Dealer Rule''),[23] pursuant to the Commodity Exchange Act.[24]

Rule G–37 currently applies to dealers in the following respects. Rule G–37(b) prohibits dealers from engaging in municipal securities business with an issuer within two years after a triggering contribution to an official of such issuer is made by: (i) The dealer; (ii) any person who is a municipal finance professional (''MFP'') of the dealer; or (iii) any political action committee (''PAC'') controlled by either the dealer or any MFP of the dealer (the ''ban on municipal securities business'').[25] Under the principal exclusion to the ban on municipal securities business, provided in Rule G–37(b), a contribution will not trigger a ban on municipal securities business if made by an MFP to an official for whom the MFP is entitled to vote, if such contribution, together with any other contributions made by the MFP to the official, do not exceed $250 per election (a ''*de minimis* contribution''). There is no *de minimis* exclusion for a contribution to an official for whom an MFP is not entitled to vote.

Current Rule G–37(c)(i) prohibits dealers and their MFPs from soliciting or coordinating contributions to an official of an issuer with which the dealer is engaging or seeking to engage in municipal securities business. Rule G–37(c)(ii) prohibits dealers and certain of their MFPs [26] from soliciting or coordinating payments to a political party of a state or locality where the dealer is engaging or seeking to engage in municipal securities business. Rule G–37(d) is an anti-circumvention provision prohibiting dealers and their MFPs from, directly or indirectly, through any person or means, doing any act that would result in a violation of section (b) or (c) of the rule. Rule G–37(e) requires dealers to disclose to the MSRB, for public dissemination, certain information related to their contributions and their municipal securities business.[27]

Currently, Rule G–37 also applies to certain activities of dealers that are now defined as municipal advisory activities under the Exchange Act and Exchange Act Rule 15Ba1–1(e).[28] Specifically, Rule G–37 defines as a type of MFP a person ''primarily engaged in municipal securities representative activities'' other than sales with natural persons.[29] Such municipal securities representative activities may include the provision of ''financial advisory or consultant services for issuers in connection with the issuance of municipal securities.'' [30] Most, and perhaps all, of these financial advisory and consultant services are also municipal advisory activities under Section 15B(e)(4) of the Exchange Act [31] and the SEC Final Rule. Moreover, currently, under Rule G–37, if a ban on municipal securities business is triggered, the ban encompasses the dealer's provision of those same financial advisory and consultant services. Current Rule G–37 applies equally to dealers that are also municipal advisors (''dealer-municipal advisors''). However, Rule G–37 does not currently apply in any respect to any municipal advisor that is not also a dealer (a ''non-dealer municipal advisor.'')

Proposed Amendments to Rule G–37

In summary, the proposed amendments to Rule G–37 would extend the core standards under Rule G–37 to municipal advisors by:

- Subject to exceptions, prohibiting a municipal advisor from engaging in ''municipal advisory business'' [32] with a municipal entity for two years following the making of a contribution to certain officials of the municipal entity by the municipal advisor, a ''municipal advisor professional'' [33] (or ''MAP'') of the municipal advisor, or a PAC controlled by the municipal advisor or an MAP (a ''ban on municipal advisory business'');
- prohibiting municipal advisors and MAPs from soliciting contributions, or coordinating contributions, to certain officials of a municipal entity with which the municipal advisor is engaging or seeking to engage in municipal advisory business;
- requiring a ''nexus'' between a contribution and the ability of the official to influence the awarding of business to the municipal advisor (or the dealer, municipal advisor or investment adviser clients of a defined ''municipal advisor third-party solicitor'');[34]
- prohibiting municipal advisors and certain MAPs from soliciting payments, or coordinating payments, to political parties of states and localities with which the municipal advisor is engaging in, or seeking to engage in, municipal advisory business;
- prohibiting municipal advisors and MAPs from committing indirect violations of proposed amended Rule G–37;
- requiring quarterly disclosures to the MSRB of certain contributions and related information;
- providing for certain exemptions from a ban on municipal advisory business; and
- extending applicable interpretive guidance under Rule G–37 to municipal advisors.

In addition, subject to exceptions, the proposed amendments would prohibit a dealer or municipal advisor from engaging in municipal securities business or municipal advisory business, as applicable, with a municipal entity for two years following the making of a contribution to certain officials of the municipal entity by a municipal advisor third-party solicitor engaged by the dealer or municipal advisor, an MAP of such municipal advisor third-party solicitor, or a PAC controlled by the municipal advisor third-party solicitor or an MAP of the municipal advisor third-party solicitor. The proposed amendments would also subject a dealer-municipal advisor to a ''cross-ban'' on municipal securities business, municipal advisory business,

[23] 17 CFR 23.451.

[24] *See* Commodity Exchange Act (''CEA''), 7 U.S.C. 1 *et seq.*

[25] Hereinafter, a contribution that triggers a ban on municipal securities business, or, as discussed *infra,* municipal advisory business, or both, is a ''triggering contribution.''

[26] MFPs as described in current paragraphs (A) through (C) of current Rule G–37(g)(iv) are subject to the prohibition in Rule G–37(c)(ii). (Paragraph (A) refers to an associated person primarily engaged in municipal securities representative activities, paragraph (B), to an associated person who solicits municipal securities business, and paragraph (C), to an associated person who is both a municipal securities principal or sales principal and a supervisor of the personnel described in paragraph (A) or (B)).

[27] The MSRB makes the information that dealers are required to disclose under Rule G–37(e) available to the public for inspection on the MSRB's Electronic Municipal Market Access (EMMA®) Web site.

[28] 17 CFR 240.15Ba1–1(e). *See generally,* 17 CFR 240.15Ba1–1 to 17 CFR 240.15Ba1–8 and related rules (collectively, ''SEC Final Rule'') (providing for the registration of municipal advisors); Release No. 34–70462 (September 20, 2013), 78 FR 67467, at 67469 (November 12, 2013) (File No. S7–45–10) (''Order Adopting SEC Final Rule'').

[29] *See* Rule G–37(g)(iv)(A).

[30] Rule G–3(a)(i)(A)(2); *see* Rule G–37(g)(iv) (providing that MFP means, under paragraph (A), ''any associated person primarily engaged in municipal securities representative activities, as defined in rule G–3(a)(i), provided, however, that sales activities with natural persons shall not be considered to be municipal securities representative activities for purposes of . . . subparagraph (A)'').

[31] *See* 15 U.S.C. 78*o*–4(e)(4).

[32] The term ''municipal advisory business'' is defined in proposed Rule G–37(g)(ix) and discussed *infra.*

[33] The proposed definition of ''municipal advisor professional'' closely parallels the definition of municipal finance professional in current Rule G–37(g)(iv) and proposed Rule G–37(g)(ii), and is discussed *infra.*

[34] *See* discussion in ''Municipal Advisor Third-Party Solicitors,'' *infra.* The new term ''municipal advisor third-party solicitor'' is defined in proposed Rule G–37(g)(x).

or both municipal securities business and municipal advisory business, consistent with the type of business the award of which can be influenced by the official to whom the contribution was made.

The discussion of the proposed rule change begins with the proposed amendments to expand the purpose and scope of Rule G–37 as set forth in proposed section (a). This is followed by a discussion of the defined terms ''municipal advisor third-party solicitor,'' ''municipal financial professional'' and ''municipal advisor professional'' [35] as an understanding of these defined terms and the treatment under the proposed rule change of persons that fall within these definitions is fundamental to understanding the scope and operation of the subsequent sections of proposed amended Rule G–37. Thereafter, the proposed amendments are discussed in order of the sections of the rule, beginning with a discussion of the proposed amendments to section (b), regarding bans on business.

Purpose Section

Currently, Rule G–37(a) describes the purpose and intent of Rule G–37, which includes the protection of investors and the public interest. It further describes the key mechanisms through which the rule aims to achieve its purposes: (i) A ban on municipal securities business following the making of a triggering contribution to an official of an issuer; and (ii) the public disclosure of information regarding dealers' political contributions and municipal securities business.

The proposed amendments would modify section (a) to include reference to municipal advisory business and reflect that a ban on business and the public disclosure requirements would apply to both dealers and municipal advisors. The proposed amendments also would expand the scope of the purpose to ensure that the high standards and integrity of the ''municipal securities market'' (instead of the ''municipal securities industry'') are maintained. In addition, in section (a) and throughout the rule, the proposed defined term ''municipal entity'' [36] would be used in lieu of the term ''issuer,'' and, the term ''dealer'' would be defined to include collectively, for purposes of the rule, brokers, dealers and municipal securities dealers. With these proposed amendments to section (a), the proposed rule change makes clear that proposed amended Rule G–37 is intended to apply to all dealers and all municipal advisors (collectively ''regulated entities'').

The proposed amendments to section (a) also would add ''municipal entities'' and ''obligated persons'' [37] as parties that the rule would be intended to protect, which reflects the scope of the MSRB's broadened statutory charge under the Dodd-Frank Act.[38] Although, by definition, obligated persons are not in that capacity issuers of municipal securities, at times officials who are the recipients of contributions may have influence in the selection of a dealer, municipal advisor or investment adviser in a matter in which an obligated person has financial obligations.

Municipal Advisor Third-Party Solicitors

Municipal advisors that undertake a solicitation of a municipal entity on behalf of a third-party dealer, municipal advisor or investment adviser engage in a distinct type of municipal advisory business. To extend the policies contained in Rule G–37 to these municipal advisors, the proposed amendments to Rule G–37 would add a new defined term, ''municipal advisor third-party solicitor'' in proposed Rule G–37(g)(x). A municipal advisor third-party solicitor would be defined in proposed Rule G–37(g)(x) as a municipal advisor that:

> Is currently soliciting a municipal entity, is engaged to solicit a municipal entity, or is seeking to be engaged to solicit a municipal entity for direct or indirect compensation, on behalf of a dealer, municipal advisor or investment adviser (as defined in Section 202(a)(11) of the Investment Advisers Act of 1940) that does not control, is not controlled by, or is not under common control with the municipal advisor undertaking such solicitation.

The terms ''solicit'' and ''soliciting'' [39] would be defined in proposed Rule G–37(g)(xix) to mean, except for purposes of Rule G–37(c):

> to make, or making, respectively, a direct or indirect communication with a municipal entity for the purposes of obtaining or retaining an engagement by the municipal entity of a dealer, municipal advisor or investment adviser (as defined in Section 202(a)(11) of the Investment Advisers Act of 1940) for municipal securities business, municipal advisory business or investment advisory services; provided, however, that it does not include advertising by a dealer, municipal advisor or investment adviser.

The terms ''municipal advisor third-party solicitor,'' ''solicit'' and ''soliciting'' would be consistent with the terms ''municipal advisor'' [40] and ''solicitation of a municipal entity or obligated person'' [41] as defined in the Exchange Act and the rules and regulations thereunder.[42] Under the Exchange Act and the SEC Final Rule, the terms ''municipal advisor'' and ''solicitation of a municipal entity or obligated person'' are to be broadly construed, and are reflective of a legislative determination that municipal advisors that act as solicitors on behalf of third-party dealers, municipals advisors or investment advisers should be regulated as such without regard to the extent to which they undertake such

[35] *See* discussion in ''Municipal Finance Professionals and Municipal Advisor Professionals,'' *infra*. The new term ''municipal advisor professional'' is defined in proposed Rule G–37(g)(iii).

[36] In proposed Rule G–37(g)(xi), ''municipal entity'' would have the meaning specified in Section 15B(e)(8) of the Act (15 U.S.C. 78*o*–4(e)(8)), and the rules and regulations thereunder. The proposed rule change would use this term in lieu of the more narrowly defined term ''issuer'' in light of the Dodd-Frank Act's grant of authority to the MSRB to adopt rules with respect to municipal advisors and municipal advisory activities for the protection of municipal entities. *See supra* nn. 3–7 and accompanying text. Exchange Act Rule 15Ba1–1(g) (17 CFR 240.15Ba1–1(g)) defines ''municipal entity'' to mean ''any State, political subdivision of a State, or municipal corporate instrumentality of a State or of a political subdivision of a State, including: (1) Any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (2) Any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (3) Any other issuer of municipal securities.''

''Municipal entity'' includes college savings plans (''529 plans'') that comply with Section 529 of the Internal Revenue Code (26 U.S.C. 529), and certain entities that do not issue municipal securities, including various types of state or local government-sponsored or established plans or pools of assets, such as local government investment pools (''LGIPs''), public employee retirement systems, public employee benefit plans and public pension plans (including participant directed plans and 403(b) and 457 plans). *See* SEC Order Adopting Final Rule, at n. 191 (defining ''public employee retirement system,'' ''public employee benefit plan,'' ''403(b) plan'' and ''457 plan''); *id.,* at 78 FR at 67480–83 (discussing these terms).

[37] ''Obligated person'' is defined in Section 15B(e)(10) of the Exchange Act (15 U.S.C. 78*o*–4(e)(10)) and rules promulgated thereunder. *See* Exchange Act Rule 15Ba1–1(k) (17 CFR 240.15Ba1–1(k)).

[38] *See, e.g.,* 15 U.S.C. 78*o*–4(b)(2)(C).

[39] The proposed definitions of ''solicit'' and ''soliciting'' would be consistent with the term ''solicitation of a municipal entity or obligated person'' as defined in Section 15B(e)(9) of the Exchange Act (15 U.S.C. 78*o*–4(e)(9)) and the rules and regulations thereunder. *See, e.g.,* 17 CFR 240.15Ba1–1(n). In addition, the MSRB proposes to move the definition of ''solicit'' from current Rule G–37(g)(ix) to proposed Rule G–37(g)(xix).

[40] *See* Section 15B(e)(4) of the Exchange Act (15 U.S.C. 78*o*–4(e)(4)).

[41] *See* Section 15B(e)(9) of the Exchange Act (15 U.S.C. 78*o*–4(e)(9)).

[42] *See* Exchange Act Rules 15Ba1–1(d), (e) and (n) (17 CFR 240.15Ba1–1(d), (e) and (n)) (defining the terms ''municipal advisor,'' ''municipal advisory activities'' and ''solicitation of a municipal entity or obligated person,'' respectively).

solicitations.[43] This includes regulation with regards to ''pay to play'' practices.[44] Indeed, Congress determined to grant rulemaking authority over municipal advisors to the MSRB, in part, because it already ''has an existing, comprehensive set of rules on key issues such as pay-to-play. . . .'' [45]

Thus, a municipal advisor that provides advice to or on behalf of a municipal entity or obligated person within the meaning of Section 15B(e)(4) of the Exchange Act [46] and the rules and regulations thereunder may, depending on its other conduct, also be a municipal advisor third-party solicitor within the meaning of proposed Rule G–37(g)(x). Additionally, a municipal advisor may at one point in time also be a municipal advisor third-party solicitor and at another point in time may no longer fall within the proposed definition. For example, in one engagement, a municipal advisor's role may be limited to that of a municipal advisor third-party solicitor and the municipal advisor would solicit a municipal entity on behalf of a third-party dealer, municipal advisor or investment adviser. Contemporaneously, in a second engagement, the municipal advisor may be engaged to provide advice to a municipal entity regarding the issuance of municipal securities. Because, under the above example, the municipal advisor falls within the scope of the municipal advisor third-party solicitor definition in connection with at least one solicitation, engagement to solicit or attempt to seek an engagement to solicit, for purposes of the proposed rule change, the municipal advisor would fall within the definition of a municipal advisor third-party solicitor. Under the proposed rule change, the engagement of a municipal advisor third-party solicitor would have special implications for a dealer or municipal advisor (either a dealer or municipal advisor, a ''regulated entity'') that engages a municipal advisor third-party solicitor (''dealer client'' or ''municipal advisor client,'' respectively) to solicit a municipal entity on its behalf.[47]

Municipal Finance Professionals and Municipal Advisor Professionals

Under current Rule G–37, a contribution by a person who is a municipal finance professional, or MFP, of a dealer may trigger a ban on municipal securities business as to the dealer in certain cases. The proposed amendments would incorporate minor non-substantive amendments to the term MFP, and define as a ''municipal advisor professional,'' or MAP, certain persons who are employed or otherwise affiliated with a municipal advisor. Similarly to an MFP, if an MAP makes a contribution, under the proposed amendments the action may trigger a ban on municipal advisory business as to the municipal advisor in certain cases.

Municipal Finance Professional. An associated person of a dealer is a ''municipal finance professional'' if he or she engages in the functions described in paragraphs (A) through (E) of current Rule G–37(g)(iv). In addition, if designated by a dealer as an MFP in the dealer's records, an associated person is deemed an MFP and retains the designation for one year after the last activity or position that gave rise to the designation.[48]

The MSRB proposes to more specifically identify the persons engaged in the functions described in current paragraphs (A) through (E) of Rule G–37(g)(iv), and to relocate the defined term, municipal finance professional, from subsection (g)(iv) to proposed subsection (g)(ii) of the rule. A person described in current Rule G–37(g)(iv)(A) would be a ''municipal finance representative'' in proposed Rule G–37(g)(ii)(A); a person described in current Rule G–37(g)(iv)(B) would be a ''dealer solicitor'' in proposed Rule G–37(g)(ii)(B); a person described in current Rule G–37(g)(iv)(C) would be a ''municipal finance principal'' in proposed Rule G–37(g)(ii)(C); a person described in current Rule G–37(g)(iv)(D) would be a ''dealer supervisory chain person'' in proposed Rule G–37(g)(ii)(D); and a person described in current Rule G–37(g)(iv)(E) would be a ''dealer executive officer'' in proposed Rule G–37(g)(ii)(E). Additionally, proposed Rule G–37(g)(ii)(B), describing ''dealer solicitors'' (*i.e.,* associated persons of dealers who solicit municipal securities business), would describe this category of MFP by cross-referencing an additional proposed defined term, ''municipal solicitor,'' [49] and would delete as superfluous the parenthetical reference to Rule G–38, on solicitation of municipal securities business. The proposed rule change would use the proposed descriptive defined terms, in both the definition of ''municipal finance professional'' and throughout the rule text.

The MSRB also proposes additional minor technical amendments to the definition of MFP to improve its readability. In paragraph (A), defining the term, ''municipal finance representative,'' the MSRB proposes to substitute the words ''other than'' in place of the more lengthy proviso in the current definition. In paragraph (E), defining the term ''dealer executive officer,'' the MSRB proposes to: (i) Relocate the parenthetical pertaining to bank dealers within the definition; and (ii) reorganize the clause that provides that a dealer shall be deemed to have no MFPs if the only associated persons meeting the MFP definition are those described in paragraph (E) (of current Rule G–37(g)(iv) or proposed Rule G–37(g)(ii)). Also, the MSRB proposes minor, non-substantive amendments to shorten the final paragraph of the definition of municipal finance professional, which provides that a person designated by the dealer as an MFP in the dealer's records under Rule G–8(a)(xvi) would be deemed to be an MFP and would retain the designation for one year after the last activity or position which gave rise to the designation. The amendments to the defined term are not intended to, and would not be interpreted to, substantively modify the scope of the current definition of municipal finance professional, except to the extent the defined term ''municipal solicitor'' used within the ''dealer solicitor'' definition applies to the solicitation of a

[43] *See* Order Adopting SEC Final Rule, 78 at 67477 (noting that ''the statutory definition of municipal advisor is broad and includes persons that traditionally have not been considered to be municipal financial advisors'' and that the definition includes ''solicitors'' that engage in municipal advisory activities). *See also id.* at n. 411 and accompanying text (''As discussed in the Proposal, a solicitation of a single investment of any amount from a municipal entity would require the person soliciting the municipal entity to register as a municipal advisor.'').

[44] As the Commission has recognized, the regulation of municipal advisors and their advisory activities is generally intended to address problems observed with the unregulated conduct of some municipal advisors, including ''pay to play'' practices. *See* Order Adopting SEC Final Rule, 78 FR at 67469.

[45] S. Report 111–176, at 149 (2010) (''Senate Report'').

[46] 15 U.S.C. 78*o*–4(e)(4).

[47] Hereinafter, a ''dealer client'' or a ''municipal advisor client'' may also be referred to as a ''regulated entity client.''

[48] *See* Rule G–8(a)(xvi) (Records Concerning Political Contributions and Prohibitions on Municipal Securities Business Pursuant to Rule G–37).

[49] In proposed Rule G–37(g)(xiii), ''municipal solicitor,'' would mean: (A) An associated person of a dealer who solicits a municipal entity for municipal securities business on behalf of the dealer; (B) an associated person of a municipal advisor who solicits a municipal entity for municipal advisory business on behalf of the municipal advisor; or (C) an associated person of a municipal advisor third-party solicitor who solicits a municipal entity on behalf of a dealer, municipal advisor or investment adviser (as defined in Section 202(a)(11) of the Investment Advisers Act of 1940) that does not control, is not controlled by, or is not under common control with such municipal advisor third-party solicitor.

''municipal entity,'' rather than an ''issuer.''

Municipal Advisor Professionals. The associated persons of a municipal advisor that would be subject to the rule would be defined as ''municipal advisor professionals'' in proposed Rule G–37(g)(iii). ''Municipal advisor professional'' would be analogous to the amended defined term, ''municipal finance professional.'' As in the definition of ''municipal finance professional,'' proposed Rule G–37(g)(iii) identifies five types of MAPs, in proposed paragraphs (A) through (E), respectively, as: ''municipal advisor representative,'' ''municipal advisor solicitor,'' ''municipal advisor principal,'' ''municipal advisor supervisory chain person,'' and ''municipal advisor executive officer.''

Under proposed Rule G–37(g)(iii), an MAP would be any associated person of a municipal advisor engaged in the following activities:

(A) Any ''municipal advisor representative''—any associated person engaged in municipal advisor representative activities, as defined in Rule G–3(d)(i)(A); [50]

(B) any ''municipal advisor solicitor''—any associated person who is a municipal solicitor (as defined in paragraph (g)(xiii)(B) of this rule) (or in the case of an associated person of a municipal advisor third-party solicitor, paragraph (g)(xiii)(C) of this rule);

(C) any ''municipal advisor principal''—any associated person who is both: (1) A municipal advisor principal (as defined in Rule G–3(e)(i)); [51] and (2) a supervisor of any municipal advisor representative (as defined in paragraph (g)(iii)(A) of this rule) or municipal advisor solicitor (as defined in paragraph (g)(iii)(B) of this rule);

(D) any ''municipal advisor supervisory chain person''—any associated person who is a supervisor of any municipal advisor principal up through and including, in the case of a municipal advisor other than a bank municipal advisor, the Chief Executive Officer or similarly situated official, and, in the case of a bank municipal advisor, the officer or officers designated by the board of directors of the bank as responsible for the day-to-day conduct of the bank's municipal advisory activities, as required by 17 CFR 240.15Ba1–1(d)(4)(i); or

(E) any ''municipal advisor executive officer''—any associated person who is a member of the executive or management committee (or similarly situated official) of a municipal advisor (or, in the case of a bank municipal advisor, the separately identifiable department or division of the bank as defined in Section 15B(e)(4) of the Act and 17 CFR 240.15Ba1–1(d)(4)(i) thereunder); provided, however, that if the persons described in this paragraph are the only associated persons of the municipal advisor meeting the definition of municipal advisor professional, the municipal advisor shall be deemed to have no municipal advisor professionals.

As in the definition of MFP, proposed Rule G–37(g)(iii) defining MAP would provide that a person designated by a municipal advisor as an MAP in the municipal advisor's records would be deemed an MAP and would retain the designation for one year after the last activity or position which gave rise to the designation.

The chart below illustrates the similarities between the defined term, ''municipal finance professional,'' as revised by the proposed amendments, and the new proposed defined term, ''municipal advisor professional.''

Types of municipal finance professional	Types of municipal advisor professional
''municipal finance representative''	''municipal advisor representative.''
''dealer solicitor''	''municipal advisor solicitor.''
''municipal finance principal''	''municipal advisor principal.''
''dealer supervisory chain person''	''municipal advisor supervisory chain person.''
''dealer executive officer''	''municipal advisor executive officer.''

Ban on Business

Currently, Rule G–37(b) sets forth a ban on municipal securities business that might have otherwise been awarded as a *quid pro quo* for a contribution, or at least as to which the appearance of a *quid pro quo* might have arisen. It prohibits a dealer from engaging in municipal securities business with an issuer within two years after a triggering contribution is made to an issuer official by the dealer, an MFP of the dealer or a PAC controlled by either the dealer or an MFP of the dealer. Proposed Rule G–37(b)(i)(A) would retain this ban on municipal securities business for dealers. Proposed Rule G–37(b)(i)(B) would create an analogous two-year ban on municipal advisory business applicable to municipal advisors that are not, at the time of the triggering contribution, municipal advisor third-party solicitors. Proposed Rule G–37(b)(i)(C)(1) would create, for municipal advisor third-party solicitors, a two-year ban on municipal advisory business analogous to the ban in proposed Rule G–37(b)(i)(B).

Under the proposed amendments, as discussed *infra,* [52] whether a contribution would trigger a ban on municipal securities business, a ban on municipal advisory business, or a ban on both types of business (any such ban, a ''ban on applicable business'') for a dealer, municipal advisor or dealer-municipal advisor generally would depend on the identity of the person who made the contribution, the type of influence that can be exercised by the official to whom the contribution was made and whether an exclusion from the ban would apply.

Persons From Whom Contributions Could Trigger a Ban on Business

Dealers. Under current Rule G–37(b)(i), contributions by three types of contributors—a dealer, [53] an MFP of the dealer [54] or a PAC controlled by either the dealer or an MFP of the dealer [55]—

[50] Rule G–3(d)(i)(A), defines a ''municipal advisor representative'' as ''a natural person associated with a municipal advisor who engages in municipal advisory activities on the municipal advisor's behalf, other than a person performing only clerical, administrative, support or similar functions.''

[51] Rule G–3(e)(i) defines the term ''municipal advisor principal'' to mean ''a natural person associated with a municipal advisor who is qualified as a municipal advisor representative and is directly engaged in the management, direction or supervision of the municipal advisory activities of the municipal advisor and its associated persons.'' *See* Order Approving MA Qualification Requirements. The term ''municipal advisory activities'' (which is used within the ''municipal advisor principal'' definition) is defined in Rule D–13 to mean, except as otherwise specifically provided by rule of the Board, ''the activities described in Section 15B(e)(4)(A)(i) and (ii) of the Act and the rules and regulations promulgated thereunder.''

[52] *See* discussion in ''Persons from Whom Contributions Could Trigger a Ban on Business,'' ''Official of a Municipal Entity,'' ''Ban on Business for Dealers; Ban on Business for Municipal Advisors,'' ''Ban on Business for Dealer-Municipal Advisors'' and ''Excluded Contributions,'' *infra.*

[53] *See* Rule G–37(b)(i)(A).

[54] *See* Rule G–37(b)(i)(B).

[55] *See* Rule G–37(b)(i)(C).

may trigger a ban on municipal securities business for the dealer. The proposed amendments to Rule G–37 would provide that this same set of persons may trigger a ban on business for the dealer, and would renumber this provision as proposed subsection (b)(i)(A).

Municipal Advisors that are not Municipal Advisor Third-Party Solicitors. Proposed Rule G–37(b)(i)(B) would set forth, for municipal advisors that are not municipal advisor third-party solicitors at the time of a contribution, a provision that parallels proposed Rule G–37(b)(i)(A) for dealers. Under proposed Rule G–37(b)(i)(B), contributions by three types of contributors—a municipal advisor, an MAP of the municipal advisor or a PAC controlled by either the municipal advisor or an MAP of the municipal advisor—may trigger a ban on municipal advisory business for the municipal advisor.

Municipal Advisor Third-Party Solicitors. Proposed Rule G–37(b)(i)(C)(1) would set forth, for municipal advisor third-party solicitors, a provision that parallels proposed Rule G–37(b)(i)(A) for dealers and proposed Rule G–37(b)(i)(B) for municipal advisors that are not municipal advisor third-party solicitors. Under proposed Rule G–37(b)(i)(C)(1), contributions by three types of contributors—the municipal advisor third-party solicitor, an MAP of the municipal advisor third-party solicitor or a PAC controlled by either the municipal advisor third-party solicitor or an MAP of the municipal advisor third-party solicitor—may trigger a ban on municipal advisory business for the municipal advisor third-party solicitor.

Clients of a Municipal Advisor Third-Party Solicitor that are Dealers or Municipal Advisors. Under proposed Rule G–37(b)(i)(C)(2), the engagement of a municipal advisor third-party solicitor would have special implications for a dealer client or municipal advisor client. If a dealer or municipal advisor engages a municipal advisor third-party solicitor to solicit a municipal entity on its behalf, three additional types of contributors may trigger a ban on municipal securities business as to a dealer client, or a ban on municipal advisory business as to a municipal advisor client. Clause (b)(i)(C)(2)(a) would apply to dealer clients of a municipal advisor third-party solicitor [56] and clause (b)(i)(C)(2)(b) would apply to municipal advisor clients (including municipal advisor third-party solicitor clients) of a municipal advisor third-party solicitor.[57] Under each of the proposed provisions, the additional types of contributors that may trigger a ban for the regulated entity are the same. They are: The engaged municipal advisor third-party solicitor; an MAP of the engaged municipal advisor third-party solicitor; and a PAC controlled by either the engaged municipal advisor third-party solicitor or an MAP of the engaged municipal advisor third-party solicitor. The MSRB believes the risk of actual or apparent *quid pro quo* corruption is obvious and substantial when a municipal advisor third-party solicitor who is engaged to solicit a municipal entity for business on behalf of a regulated entity client makes a triggering contribution to an official of that municipal entity with the ability to influence the awarding of business to the municipal advisor third-party solicitor's client. For such instances, clauses (b)(i)(C)(2)(a) and (b) are designed to curb actual and apparent *quid pro quo* corruption involving the regulated entity client and the official to whom the contribution is made and to prevent such a regulated entity client from obtaining the benefit of any actual *quid pro quo* corruption.

The determination of whether a municipal advisor was engaged as a municipal advisor third-party solicitor by a regulated entity client would be determined based on the facts and circumstances.[58] The MSRB would not consider the absence of a writing evidencing the relationship, or the absence of particular terms in a writing evidencing the relationship, to preclude a finding that a municipal advisor third-party solicitor was engaged by a regulated entity to solicit a municipal entity on its behalf within the meaning of proposed Rule G–37(b)(i).[59]

Investment Adviser Clients of a Municipal Advisor Third-Party Solicitor. Because Rule G–37 does not apply to investment advisers in their capacity as such, if an investment adviser engages a municipal advisor third-party solicitor to solicit on its behalf for an engagement to provide investment advisory services, the actions of the municipal advisor third-party solicitor would not trigger a ban on business for the investment adviser.[60]

Official of a Municipal Entity

Under current Rule G–37, for any contribution to trigger a ban on applicable business, an additional element—selection influence—must be present. A contribution by a dealer, MFP or PAC controlled by either the dealer or an MFP of the dealer can only trigger a ban on municipal securities business for the dealer if the official to whom the contribution was made is an ''official of an issuer.'' As discussed

[56] Currently, a dealer is generally prohibited under Rule G–38 from making payments to a third-party solicitor to solicit municipal securities business on behalf of the dealer. However, proposed Rule G–37(b)(i)(C)(2)(a) would apply in the limited cases where payments to a third-party solicitor are permitted under Rule G–38 as well as in cases where a dealer engaged a municipal advisor third-party solicitor in violation of Rule G–38.

[57] Although municipal advisors that are not dealers are not subject to Rule G–38, municipal advisors that are not municipal advisor third-party solicitors would be subject to proposed Rule G–42, if approved by the Commission. In relevant part, proposed Rule G–42 provides that non-solicitor municipal advisors are prohibited from making payments for the purpose of obtaining or retaining an engagement to perform municipal advisory activities subject to limited exceptions, which include reasonable fees paid to another municipal advisor registered as such with the Commission and the Board for making such a direct or indirect communication with a municipal entity or obligated person on behalf of the municipal advisor where such communication is made for the purpose of obtaining or retaining an engagement to perform municipal advisory activities. *See* Proposed Rule G–42 Filing.

[58] For example, if the facts and circumstances suggest that On-Site MA, a municipal advisor third-party solicitor, and Best Dealer, a dealer, orally agreed that On-Site MA would solicit Municipal Entity to retain Best Dealer to underwrite municipal securities for Municipal Entity, On-Site MA would be deemed to have been engaged as a municipal advisor third-party solicitor on behalf of Best Dealer with respect to Municipal Entity, even in the absence of a written engagement letter. Similarly, if there was a written engagement letter between On-Site MA and Best Dealer that was limited to soliciting municipal securities business in a major metropolitan city located in a tri-state area, but the facts and circumstances show that Best Dealer actually agreed to engage On-Site MA to solicit municipal securities business from any and all municipal entities in the metropolitan tri-state area, On-Site MA would be deemed to have been engaged as a municipal advisor third-party solicitor on behalf of Best Dealer with respect to the entire metropolitan tri-state area.

[59] *But see* discussion in ''Persons from Whom Contributions Could Trigger a Ban on Business—Municipal Advisor Third-Party Solicitors,'' *supra,* and ''Municipal Securities Business and Municipal Advisory Business,'' *infra.* Under proposed Rule G–37(b)(i)(C)(1), to impose a ban on municipal advisory business for a municipal advisor third-party solicitor, the municipal advisor third-party solicitor does not need to be specifically engaged, at the time of the contribution, to solicit the type of work over which the official to whom the contribution is made has selection influence. Because a municipal advisor third-party solicitor, by definition, may solicit for several different types of business (*i.e.,* municipal securities business, municipal advisory business and investment advisory services), a contribution to any official with the ability to influence the awarding of business to the solicitor's *current or prospective* dealer, municipal advisor or investment adviser clients could trigger a ban for the municipal advisor third-party solicitor since there is at least an appearance of *quid pro quo* corruption when it makes a contribution to such an official. *See infra,* n. 62.

[60] However, investment advisers are subject to the requirements and prohibitions provided in the IA Pay to Play Rule. 17 CFR 275.206(4)–5; *see generally,* Order Adopting IA Pay to Play Rule.

infra, an ''official of an issuer'' must, in relevant part, have the ability to influence ''the hiring of a broker, dealer or municipal securities dealer for municipal securities business by an issuer.'' [61] Proposed amended Rule G–37 would, as explained below, extend this selection influence element to municipal advisors (and the dealer, municipal advisor and investment adviser clients of municipal advisor third-party solicitors), requiring a nexus between the influence that can be exercised by the ''official of a municipal entity'' (''ME official'') who receives a potentially ban-triggering contribution and the type of business in which the regulated entity is engaged or is seeking to engage.[62]

The term ''official of a municipal entity'' would be substituted for the current term ''official of an issuer'' in Rule G–37. The definition of ''official of an issuer'' (or ''official of such issuer'') in current Rule G–37(g)(vi) includes any person who, at the time of the contribution, was an incumbent, candidate or successful candidate: (A) For elective office of the issuer which office is directly or indirectly responsible for, or can influence the outcome of, the hiring of a dealer for municipal securities business by the issuer; or (B) for any elective office of a state or of any political subdivision, which office has authority to appoint any person who is directly or indirectly responsible for, or can influence the outcome of, the hiring of a dealer for municipal securities business by an issuer.

The proposed amendments would delete the term ''official of an issuer'' from Rule G–37(g)(vi) and substitute the term ''official of a municipal entity'' as set forth in proposed Rule G–37(g)(xvi). To take into account the possibility that an ME official may have the ability to influence the hiring of a dealer, municipal advisor or investment adviser, or the hiring of two or more of such professionals, three categories of ME officials would be identified in proposed Rule G–37(g)(xvi): An official of a municipal entity with dealer selection influence, as described in proposed paragraph (A), an official of a municipal entity with municipal advisor selection influence, as described in proposed paragraph (B), and an official of a municipal entity with investment adviser selection influence, as described in proposed paragraph (C).

The term ''official of a municipal entity with dealer selection influence'' would be substantively similar to the ''official of an issuer'' definition in current Rule G–37(g)(vi), with the exception of the substitution of the term ''municipal entity'' in place of the term ''issuer.'' [63] However, because the term ''municipal entity'' used in the ''official of a municipal entity with dealer selection influence'' definition includes entities beyond those defined as ''issuers,'' the official of a municipal entity with dealer selection influence definition is more expansive than the ''official of an issuer'' definition it replaces.[64] The term ''official of a municipal entity with municipal advisor selection influence'' would be analogous to the ''official of a municipal entity with dealer selection influence'' definition. In connection with municipal advisor third-party solicitors that solicit on behalf of an investment adviser, the term ''official of a municipal entity with investment adviser selection influence'' would be analogous to the ''official of a municipal entity with dealer selection influence'' definition for dealers (and municipal advisor third-party solicitors on behalf of a dealer) and the ''official of a municipal entity with municipal advisor selection influence'' definition for all municipal advisors. The proposed definition's structure, which includes the three categories of ME officials, provides the flexibility to establish, in the case of a contribution to an ME official, whether there is the required nexus between the ME official who received the contribution (based upon his or her scope of influence) and the awarding of business that gives rise to a sufficient risk of *quid pro quo* corruption or the appearance of such corruption to warrant a two-year ban.

Municipal Securities Business and Municipal Advisory Business

Currently, under Rule G–37, a dealer subject to a ban is generally prohibited from engaging in ''municipal securities business'' with the relevant issuer. ''Municipal securities business'' is currently defined in Rule G–37(g)(vii) as the purchase of a primary offering on other than a competitive bid basis, the offer or sale of a primary offering of municipal securities, providing financial advisory or consultant services to or on behalf of an issuer with respect to a primary offering on other than a competitive bid basis, and providing remarketing agent services with respect to a primary offering on other than a competitive bid basis. Under interpretive guidance issued in 1997 (the ''1997 Guidance''), the municipal securities business from which a dealer subject to a ban is prohibited from engaging in is ''new'' municipal securities business. The MSRB has interpreted ''new'' municipal securities business as contractual obligations with an issuer entered into after the date of the triggering contribution to an official of the issuer and contractual obligations that were entered into prior to the date of the triggering contribution but which

[61] *See* Rule G–37(g)(vi).

[62] Dealers and municipal advisors that are not municipal advisor third-party solicitors are typically compensated by the municipal entity or obligated person to whom they are providing advice or municipal securities business. Thus, when a *quid pro quo* contribution is made by a dealer or such a municipal advisor, the *quid* is the contribution and the *quo* is the awarding of business to the dealer or municipal advisor in exchange for the contribution. However, municipal advisor third-party solicitors (in their capacity as such) are typically compensated not by the municipal entity or obligated person they solicit, but by a third-party dealer, municipal advisor or investment adviser for whom they are attempting to secure municipal securities business, municipal advisory business or engagements to provide investment advisory services. When a *quid pro quo* contribution is made by a municipal advisor third-party solicitor, the *quid* is the contribution and the *quo* is typically the awarding of business to the current or prospective clients of the municipal advisor third-party solicitor. Of course, the *quo* for a municipal advisor third-party solicitor (a type of municipal advisor) could also be the awarding of municipal advisory business to the municipal advisor itself, as a municipal advisor third-party solicitor may simultaneously undertake a solicitation of a municipal entity or obligated person and provide, or seek to provide, to another municipal entity or obligated person certain advice. Thus, for municipal advisor third-party solicitors, the appearance of *quid pro quo* corruption may arise with respect to a wider range of contributions, as compared to dealers and municipal advisors that are not municipal advisor third-party solicitors. Because municipal advisor third-party solicitors are in the business of attempting to secure business for third-party dealers, municipal advisors and investment advisers, the fact that a municipal advisor third-party solicitor is not, at the time of a contribution, actually engaged to solicit a municipal entity for a particular type of business does not avoid the appearance of *quid pro quo* corruption. As discussed *supra,* a municipal advisor third-party solicitor is a municipal advisor that, in relevant part, is currently soliciting, is engaged to solicit, or is seeking to be engaged to solicit a municipal entity for business on behalf of a third-party dealer, municipal advisor or investment adviser. Thus, a municipal advisor third-party solicitor will always stand to gain from a *quid pro quo* contribution as such a contribution may assist the municipal advisor third-party solicitor in obtaining new business from a prospective dealer, municipal advisor or investment adviser client seeking to curry favor with the ME official to whom the municipal advisor third-party solicitor made the contribution.

[63] In addition, the proposed definition of ''official of a municipal entity with dealer selection influence'' would include minor technical amendments to the current definition of ''official of an issuer'' to improve its readability.

[64] For example, the term ''municipal entity'' includes certain entities that do not issue municipal securities, including various types of state or local government-sponsored or established plans or pools of assets, such as LGIPs, public employee retirement systems, public employee benefit plans and public pension plans (including participant directed plans and 403(b) and 457 plans). *See supra,* n. 36.

are not specific to a particular issue of a security.[65] The latter category that is subject to the ban is referred to as ''pre-existing but non-issue specific contractual undertakings.''[66] In contrast, pre-existing issue-specific contractual undertakings are generally not deemed ''new'' municipal securities business, and are not subject to the ban.[67] Interpretive guidance issued in 2002 (the ''2002 Guidance'') modified the 1997 Guidance in a limited respect to expand the scope of municipal securities business that is not ''new'' for dealers that serve as primary distributors of municipal fund securities, in light of the unique aspects of municipal fund securities programs and the role that primary distributors play with respect to such programs.

Under the proposed rule change, the definition of municipal securities business would not be amended, except to renumber the definition as proposed subsection (g)(xii) and incorporate conforming changes. Additionally, the 1997 Guidance and the 2002 Guidance would remain unchanged for dealers.

Under proposed Rule G–37(b)(i)(B) and proposed Rule G–37(b)(i)(C)(1), a municipal advisor (including a municipal advisor third-party solicitor) subject to a ban would generally be prohibited from engaging in ''municipal advisory business'' with the relevant municipal entity. Proposed Rule G–37(g)(ix) would define ''municipal advisory business'' to mean those activities that would cause a person to be a municipal advisor as defined in Section 15B(e)(4) of the Act, 17 CFR 240.15Ba1–1(d)(1)–(4) and other rules and regulations thereunder.[68]

Notably, if a municipal advisor third-party solicitor is subject to a ban under proposed Rule G–37(b)(i)(C), it would be prohibited from engaging in all types of municipal advisory business with the relevant municipal entity, including providing certain advice to the municipal entity and soliciting the municipal entity on behalf of *any* third-party dealer, municipal advisor or investment adviser.

For municipal advisors, the MSRB intends that all existing interpretive guidance regarding the municipal securities business of dealers under Rule G–37 would apply to the analogous interpretive issues regarding the municipal advisory business of municipal advisors. However, because the ''new'' versus non-''new'' business distinction in the 1997 Guidance only applies to pre-existing issue-specific contractual obligations *with an issuer,* such guidance would not apply to municipal advisor third-party solicitors as their contractual obligations are not owed to an issuer but to third parties that are regulated entity clients or investment adviser clients. Further, the 2002 Guidance would not be extended to any municipal advisors to municipal fund securities programs because the 2002 Guidance addressed a non-analogous interpretive issue for dealers.[69] Multiple factors supported the 2002 Guidance regarding primary distributors of municipal fund securities, but the essential factor was the magnitude of the possible repercussions to an issuer of municipal fund securities or investors in municipal fund securities resulting from a sudden change in the primary distributor. For example, issuers would typically not be faced with redesigning existing programs in light of the exit of a municipal advisor to such a plan. Further, the MSRB believes that the exit of a municipal advisor would typically have little or no direct impact on investors, and would not force investors to restructure or establish new relationships with different dealers in order to maintain their investments. The Board does not believe that the disruption of services provided by a municipal advisor to a municipal fund securities plan would result in repercussions of comparable scope or severity to issuers and investors.

Ban on Business for Dealers; Ban on Business for Municipal Advisors

Under the proposed rule change, a dealer or municipal advisor that is not a municipal advisor third-party solicitor could be subject to a ban on applicable business only when a triggering contribution is made to an ME official who can influence the awarding of the type of business in which that regulated entity engages.

A dealer that engages in municipal securities business, but not municipal advisory business, would be subject to a ban on municipal securities business only when a triggering contribution is made by any of the persons described in proposed Rule G–37(b)(i)(A) or proposed Rule G–37(b)(i)(C)(2) to an official of a municipal entity with dealer selection influence, as described in proposed Rule G–37(g)(xvi)(A). (Although the ME official may also have influence as described in proposed Rule G–37(g)(xvi)(B) and (C), regarding the selection of municipal advisors and investment advisers, the broader scope of influence would be irrelevant in determining whether a dealer would be subject to a ban on municipal securities business.)[70] Conversely, a contribution made by any of the persons described in proposed Rule G–37(b)(i)(A) or proposed Rule G–37(b)(i)(C)(2) to an ME official that does not have dealer selection influence (such as an official with only municipal advisor selection influence, or only municipal advisor and investment adviser selection influence) would not trigger a ban for the dealer.

Similarly, a non-dealer municipal advisor that is not a municipal advisor

[65] *See* 1997 Guidance.

[66] *See id.* Pre-existing but non-issue-specific contractual undertakings are subject to the ban on municipal securities business, subject to an orderly transition to another entity that is not subject to a ban to perform such business. *Id.*

[67] *See id.* For example, if a bond purchase agreement was signed prior to the date of a contribution triggering a ban on municipal securities business, a dealer may continue to perform its services as an underwriter on the issue. Significantly, however, new or different services provided under provisions in existing issue-specific contracts that allow for changes in the services provided by the dealer or the compensation paid by the issuer are deemed new municipal securities business. *Id.* Thus, Rule G–37 precludes a dealer subject to a ban from performing such additional functions or receiving additional compensation.

[68] *See* proposed Rule G–37(g)(ix).

[69] Because the 1997 Guidance would not apply to municipal advisor third-party solicitors, the 2002 Guidance (which modifies the 1997 Guidance) would also have no application to municipal advisor third-party solicitors. Thus, municipal advisor third-party solicitors on behalf of third-party dealers, municipal advisors and investment advisers would be prohibited, based on a triggering contribution, from continuing to perform under any pre-existing contract to solicit the relevant municipal entity (whether an issuer of municipal fund securities or any other type of municipal entity).

[70] The following example illustrates the impact of a triggering contribution made by an MAP of a municipal advisor third-party solicitor when the municipal advisor third-party solicitor was engaged by a dealer client as set forth in proposed Rule G–37(b)(i)(C)(2).

Best Dealer is a dealer located in a Midwestern state. On-Site MA is a municipal advisor third-party solicitor located in a western coastal state, State A. Best Dealer engages On-Site MA to solicit three major municipal entities in State A to hire Best Dealer to underwrite municipal bonds, including North City and South City of State A. Dan is an employee and an MAP of On-Site MA. Dan resides in North City. Dan makes a contribution of $240 to an ME official of South City, for whom Dan is not entitled to vote. The ME official exercises influence in the selection of dealers, municipal advisors and investment advisers for South City matters. As a result of Dan's $240 contribution to the ME official, Best Dealer, the dealer client of On-Site MA, becomes subject to a ban on engaging in municipal securities business with South City, because Dan's contribution is a triggering contribution and Best Dealer engaged On-Site MA to solicit South City on behalf of Best Dealer. In addition, as discussed *infra,* On-Site MA would also become subject to a ban on engaging in municipal advisory business with South City.

Although the ME official exercises influence in the selection of municipal advisors and investment advisers, because Best Dealer does not engage in municipal advisory business, a ban on applicable business would subject Best Dealer only to a ban on municipal securities business.

third-party solicitor would be subject to a ban on municipal advisory business only when a triggering contribution is made by any of the persons described in proposed Rule G–37(b)(i)(B) or proposed Rule G–37(b)(i)(C)(2) to an ME official that is at least an official of a municipal entity with municipal advisor selection influence.[71]

A non-dealer municipal advisor third-party solicitor would be subject to a ban on municipal advisory business, including advising and soliciting, when a triggering contribution is made by any of the persons described in proposed Rule G–37(b)(i)(C)(1) to any ME official,[72] if investment adviser selection influence.[73]

If a municipal advisor does not also engage in municipal securities business, a ban on applicable business under the proposed rule change would subject the municipal advisor only to a ban on municipal advisory business.

Ban on Business for Dealer-Municipal Advisors

The proposed rule change would treat dealer-municipal advisors as a single economic unit and would subject such firms to an appropriately scoped ban on business. The scope of the ban on business would not be dependent on the particular line of business within the dealer-municipal advisor with which the person or PAC that is the contributor may be associated. Instead, the scope of the ban on business would depend on the type of influence that can be exercised by the ME official to whom the triggering contribution is made. As a result, a dealer-municipal advisor could be subject, based on a single contribution, to a ban on municipal securities business, a ban on municipal advisory business, or both. Further, any of the following entities or persons might trigger a ban on business for a dealer-municipal advisor if the entity or person makes a contribution that is a triggering contribution in the particular facts and circumstances: The dealer-municipal advisor; an MFP or MAP of the dealer-municipal advisor; a PAC controlled by the dealer-municipal advisor or an MFP or an MAP of the dealer-municipal advisor; a municipal advisor third-party solicitor engaged on behalf of the dealer-municipal advisor; an MAP of such municipal advisor third-party solicitor; or a PAC controlled by either such municipal advisor third-party solicitor or an MAP of such municipal advisor third-party solicitor.

Ban on Applicable Business for Dealer-Municipal Advisors. A dealer-municipal advisor could be subject to a ban on municipal securities business, in its capacity as a dealer, under proposed Rule G–37(b)(i)(A) or proposed Rule G–37(b)(i)(C)(2)(a), under the same terms that apply to other dealers. Similarly, a dealer-municipal advisor that is not a municipal advisor third-party solicitor could, under proposed Rule G–37(b)(i)(B) or proposed Rule G–37(b)(i)(C)(2)(b), be subject to a ban on municipal advisory business under the same terms that apply to non-dealer municipal advisors that are not municipal advisor third-party solicitors. In addition, if a dealer-municipal advisor is a municipal advisor third-party solicitor, under proposed Rule G–37(b)(i)(C), the dealer-municipal advisor could be subject to a ban on municipal advisory business under the same terms that apply to other municipal advisor third-party solicitors.

Cross-Ban. In addition to paragraphs (b)(i)(A), (b)(i)(B) and (b)(i)(C) potentially having application to dealer-municipal advisors, proposed Rule G–37(b)(i)(D) would provide for the imposition of a ''cross-ban'' for dealer-municipal advisors to address *quid pro quo* corruption, or the appearance thereof, in two scenarios that arise only for dealer-municipal advisors. The proposed cross-ban would be a ban on business applicable to a line of business within a dealer-municipal advisor as a result of a triggering contribution that emanated from a person or entity associated with the other line of business within the same dealer-municipal advisor. With the provision for a cross-ban, the scope of a ban on business for a dealer-municipal advisor would not be dependent on the particular line of business within the dealer-municipal advisor with which the person or PAC that is the contributor may be associated. Instead, the scope of

[71] The following example illustrates the impact of a triggering contribution made by an MAP of a municipal advisor third-party solicitor when engaged by a municipal advisor client that is not a municipal advisor third-party solicitor as set forth in proposed Rule G–37(b)(i)(C)(2).

Best MA is a municipal advisor located in a Midwestern state, and is not a municipal advisor third-party solicitor. On-Site MA is a municipal advisor third-party solicitor located in a western coastal state, State A. Best MA engages On-Site MA to solicit the city school districts of three major municipalities in State A to hire Best MA to provide municipal advisory services for such school districts, including North City School District and South City School District. Dan is an employee and an MAP of On-Site MA. Dan resides in North City. Dan makes a contribution of $240 to an official running for re-election to the school board of South City School District. Dan is not entitled to vote for the candidate. The ME official exercises influence in the selection of dealers, municipal advisors and investment advisers for South City School District matters. As a result of Dan's $240 contribution to the ME official, Best MA, the client of On-Site MA, becomes subject to a ban on engaging in municipal advisory business with South City School District, because Dan's contribution is a triggering contribution and Best MA engaged On-Site MA to solicit South City School District on behalf of Best MA. Because Best MA does not engage in municipal securities business, a ban on applicable business would subject Best MA only to a ban on municipal advisory business.

In addition, as discussed *infra,* On-Site MA would also become subject to a ban on engaging in municipal advisory business with South City.

[72] The impact of a triggering contribution made by a municipal advisor third-party solicitor (or one of its MAPs, or a PAC controlled by the municipal advisor third-party solicitor or an MAP thereof) to an ME official is illustrated as follows:

Best Dealer is a dealer located in a Midwestern state. Best MA is a municipal advisor located in a Midwestern state, and is not a municipal advisor third-party solicitor. Best IA third-party solicitor located in a western coastal state, State A. Best Dealer engages On-Site MA to solicit three major municipal entities in State A, including North City and South City, to hire Best Dealer to underwrite municipal bonds. Best MA engages On-Site MA to solicit the five largest municipal entities in State A, including North City and South City, to hire Best MA to provide municipal advisory services for such entities. Best IA engages On-Site MA to solicit, in State A, all municipalities with populations over 150,000 people, to retain Best IA for investment advice. Dan is an employee and an MAP of On-Site MA, and resides in North City. Dan makes a contribution of $240 to an ME official of South City, for whom Dan is not entitled to vote. The ME official exercises influence in the selection of dealers, municipal advisors and investment advisers, for South City matters.

The consequences for On-Site MA would be as follows: On-Site MA would be banned from the following business with South City: engaging in any form of municipal advisory business with South City (because municipal advisory business is defined to include solicitation on behalf of dealers, municipal advisors and investment advisers AND other municipal advisory functions), including soliciting South City on behalf of any dealer, including Best Dealer, any third-party municipal advisor, including Best MA, and any investment adviser.

The additional consequences of such contribution would be as follows: The dealer client, Best Dealer, would become subject to a ban on engaging in municipal securities business with South City, because Best Dealer engaged On-Site MA to solicit South City on behalf of Best Dealer (and the ME official receiving the contribution had dealer selection influence); and the municipal advisor client, Best MA, would become subject to a ban on engaging in municipal advisory business (of any type) with South City, because Best MA engaged On-Site MA to solicit South City on behalf of Best MA (and the ME official receiving the contribution had municipal advisor selection influence). However, Best IA, who also engaged On-Site MA to solicit South City (a municipality with a population of over 150,000 people), would not be subject to a ban under proposed amended Rule G–37, because although the ME official receiving the contribution had investment adviser selection influence, the proposed rule change does not extend to investment advisers that are not also dealers or municipal advisors. However, as noted *supra,* Best IA would be subject to the requirements and prohibitions provided in the IA Pay to Play Rule. *See* discussion in ''Investment Adviser Clients of a Municipal Advisor Third-Party Solicitor'' and n. 60, *supra.*

[73] Additionally, a contribution made by any of the persons described in proposed Rule G–37(b)(i)(C)(2) to an official of a municipal entity with municipal advisor selection influence could also trigger a ban for the engaging municipal advisor third-party solicitor if the engaging municipal advisor third-party solicitor engaged another municipal advisor third-party solicitor under proposed Rule G–37(b)(i)(C)(2)(b).

the ban on business will depend on the type of influence that can be exercised by the ME official to whom the triggering contribution is made.

In the first scenario, a contribution is made to an ME official with *both* dealer and municipal advisor selection influence by a person or entity associated with *only one* line of business within the dealer-municipal advisor. For example, assume an MFP of the dealer-municipal advisor who is not also an MAP makes a triggering contribution to an ME official with both dealer and municipal advisor selection influence. Proposed paragraph (b)(i)(D) would subject the dealer-municipal advisor to a ban not only on municipal securities business but also to a cross-ban on municipal advisory business because the contribution is to an ME official who can exercise influence as to the selection of the dealer-municipal advisor in both a dealer and municipal advisor capacity.

In the second scenario, a contribution is made to an ME official with *only one* type of influence (either dealer selection influence or municipal advisor selection influence, but not both) from a person or entity associated only with the line of business as to which the ME official *does not* have influence. For example, assume a triggering contribution is made to an official of a municipal entity with only dealer selection influence by an MAP of the dealer-municipal advisor who is not also an MFP. Proposed paragraph (b)(i)(D) would subject the dealer-municipal advisor to a cross-ban on municipal securities business, but not to a ban on municipal advisory business because the ME official is not an official with municipal advisor selection influence.[74] Similarly, if a triggering contribution were made to an official of a municipal entity with only municipal advisor selection influence by an MFP of the dealer-municipal advisor who is not an MAP, the dealer-municipal advisor would be subject to only a ban on municipal advisory business.

The table below shows the most common persons from whom a contribution could trigger a ban on municipal securities business, a ban on municipal advisory business, or both under proposed amended Rule G–37.

PERSONS FROM WHOM A CONTRIBUTION COULD TRIGGER A BAN ON MUNICIPAL SECURITIES BUSINESS, MUNICIPAL ADVISORY BUSINESS, OR BOTH[75]

Regulated Entity Subject to a Ban	I. Dealer	II. Municipal Advisor That Is Not a Municipal Advisor Third-Party Solicitor	III. Municipal Advisor Third-Party Solicitor (for purposes of this table, "MATP solicitor")	IV. Dealer-Municipal Advisor (for purposes of this table, "the firm")	
Contributor	the dealer	the municipal advisor	the MATP solicitor	the firm.	
	an MFP of the dealer	an MAP of the municipal advisor.	an MAP of the MATP solicitor.	an MFP of the firm	an MAP of the firm.
	a PAC controlled by the dealer.	a PAC controlled by the municipal advisor.	a PAC controlled by the MATP solicitor.	a PAC controlled by the firm.	
	a PAC controlled by an MFP of the dealer.	a PAC controlled by an MAP of the municipal advisor.	a PAC controlled by an MAP of the MATP solicitor.	a PAC controlled by an MFP of the firm.	a PAC controlled by an MAP of the firm.
	If an MATP solicitor is engaged to solicit a municipal entity on behalf of the dealer, the entities and persons in column III.	If an MATP solicitor is engaged to solicit a municipal entity on behalf of the municipal advisor, the entities and persons in column III.	If an MATP solicitor is engaged to solicit a municipal entity on behalf of the MATP solicitor, the entities and persons in this column above.	If an MATP solicitor is engaged to solicit a municipal entity on behalf of the firm, the entities and persons in column III.	

Orderly Transition Period

As discussed above, under the 1997 Guidance, a dealer that is subject to a ban on municipal securities business with an issuer is prohibited from engaging in new municipal securities business with that issuer, which includes pre-existing but non-issue-specific contractual undertakings. In such cases, to give the issuer the opportunity to receive the benefit of the work already provided and to find a replacement to complete the work performed by the dealer, as needed, the dealer may—notwithstanding the ban on business—continue to perform its pre-existing but non-issue-specific contractual undertakings subject to an orderly transition to another entity to perform such business.[76] The interpretive guidance provides that this transition period should be as short a period of time as possible.[77]

Proposed Rule G–37(b)(i)(E) would essentially codify this guidance for dealers and extend it to municipal advisors that are not soliciting the municipal entity with which they become subject to a ban on applicable business. Under this provision, a dealer or municipal advisor that is engaging in municipal securities business or municipal advisory business with a municipal entity and, during the period of the engagement, becomes subject to a ban on applicable business, may continue to engage in the otherwise prohibited municipal securities business and/or municipal advisory business solely to allow for an orderly transition to another entity and, where

[74] Consistently, if a contribution is made by an MAP of a dealer-municipal advisor that is also a municipal advisor third-party solicitor to an ME official with only investment adviser selection influence, the dealer-municipal advisor would be subject to a ban on municipal advisory business, but it would not be subject to a cross-ban on municipal securities business.

[75] This table is for illustrative purposes only. Reference should be made to the proposed amended rule text for complete details.

[76] *See* 1997 Guidance.

[77] *Id.*

applicable, to allow a municipal advisor to act consistently with its fiduciary duty to its client. This provision, however, would not permit a municipal advisor third-party solicitor to continue soliciting a municipal entity with which it becomes prohibited from engaging in municipal advisory business.[78] Consistent with the 1997 Guidance, the proposed rule change would specifically provide that the transition period must be as short a period of time as possible. In addition, in the event that a dealer or municipal advisor avails itself of the orderly transition period, proposed Rule G–37(b)(i)(E) would extend the ban on business with the municipal entity for which the dealer or municipal advisor utilized the orderly transition period by the duration of the orderly transition period.

For municipal advisors, consistent with the existing interpretive guidance applicable to dealers, the orderly transition period would apply only with respect to pre-existing but non-issue-specific contractual undertakings owed to municipal entities, which, as discussed above, are included in ''new'' municipal advisory business and are subject to a ban. For example, if a municipal advisor enters into a long-term contract with a municipal entity for municipal advisory business (*e.g.,* a five-year agreement in which the municipal advisor agrees to provide to the municipal entity advice on a range of matters, including with respect to its reserve policy and the issuance of municipal securities) and a contribution that results in a ban on municipal advisory business is given after such a non-issue-specific contract is entered into, the municipal advisor would be permitted to continue to perform under the contract for as short a period of time as possible to allow for an orderly transition to another municipal advisor. Also, in this example, the ban on municipal advisory business with the municipal entity would be extended by the length of the orderly transition period.

After carefully considering whether to extend the orderly transition period under the interpretive guidance to municipal advisors, the MSRB determined that it is a necessary and appropriate aspect of the regulatory framework governing the municipal market. Significantly, the MSRB believes that certain aspects of proposed amended Rule G–37 would serve as important bulwarks against potential abuse of the orderly transition period. Public disclosure is a critical aspect of Rule G–37 and under the proposed rule change, municipal advisors would be required to disclose (comparable to the current requirements for dealers) to the MSRB information about their political contributions and the municipal advisory business in which they have engaged.[79] The MSRB then would make such disclosures available to the public as well as fellow regulators charged with examining for compliance with and enforcing Rule G–37. In addition, under proposed Rule G–37(d), municipal advisors and their MAPs would (comparable to the current requirements for dealers) be prohibited from doing, directly or indirectly, through or by any other person or means, any act which would result in a violation of a ban on business. This anti-circumvention provision, together with the required disclosures, would act to deter and promote detection of potential abuses of the orderly transition period. The MSRB believes that this overall approach strikes the appropriate balance between accommodating the need for municipal advisors to act consistently with their fiduciary duties and the need to address the appearance of, or actual, *quid pro quo* corruption involving municipal advisors.

Excluded Contributions

Proposed amendments to Rule G–37(b)(ii) would consolidate in one provision the types of contributions that do not currently subject a dealer to a ban on applicable business, and would extend the same exclusions to municipal advisors. The first exclusion is for *de minimis* contributions, and the second and third exclusions are modifications of the two-year look-back provision that would otherwise apply, as explained below.

De Minimis Contributions. Under current Rule G–37(b)(i), contributions made by an MFP to an issuer official for whom the MFP is entitled to vote will not trigger a ban on municipal securities business if such contributions do not, in total, exceed $250 per election.[80] The proposed amendments to Rule G–37 would retain this exclusion for MFPs of dealers in proposed Rule G–37(b)(ii)(A). Proposed Rule G–37(b)(ii)(A) also would extend this exclusion to the MAPs of all municipal advisors, including the MAPs of municipal advisor third-party solicitors. If a contribution by an MAP of a municipal advisor third-party solicitor would meet the *de minimis* exclusion, neither the municipal advisor third-party solicitor nor the dealer client or municipal advisor client for which it was engaged to solicit business would be subject to a ban. In addition, proposed Rule G–37(b)(ii)(A) would incorporate non-substantive changes to the *de minimis* exclusion in current Rule G–37 to improve the readability of the provision.

Other Excluded Contributions. Currently, under Rule G–37, according to what is known as the ''two-year look-back,'' a dealer is generally subject to a ban on municipal securities business for a period of two years from the making of a triggering contribution, even if such contributions were made by a person, who, although now an MFP of a dealer, was not an MFP of the dealer at the time he or she made the contribution. The proposed rule change would retain the two-year look-back for MFPs[81] and would extend it to the MAPs of municipal advisors that are not municipal advisor third-party solicitors[82] as well as municipal advisors that are municipal advisor third-party solicitors.[83]

Currently, the two-year look-back is modified under Rule G–37 in two situations. Under Rule G–37(b)(ii), contributions to an issuer official by an individual that is an MFP solely based on his or her solicitation activities for the dealer are excluded and do not trigger a ban on municipal securities business for the dealer, *unless* such MFP (who is so characterized solely based on his or her solicitation activities for the dealer) subsequently solicits municipal securities business from the same issuer. The proposed amendments to Rule G–37 would relocate to proposed paragraph (b)(ii)(B) this exclusion applicable to such MFPs (''dealer solicitors'' as defined in proposed Rule G–37(g)(ii)(B)) and would extend it to MAPs that perform a similar solicitation function within a municipal advisory firm (''municipal advisor solicitors'' as

[78] Because any relevant contractual obligations of a municipal advisor third-party solicitor in its capacity as such are owed not to a municipal entity but to third-party regulated entities or investment advisers, the rationale for the orderly transition period would not apply.

[79] *See* discussion in ''Public Disclosure of Contributions and Other Information,'' *infra.*

[80] For purposes of the *de minimis* exclusion, primary elections and general elections are separate elections. Therefore if an official is involved in a primary election prior to the general election, an MFP who is entitled to vote for such official may, within the scope of the *de minimis* exclusion, contribute up to $250 to the official in a primary election and again contribute a separate $250 to the same official in a general election. *See* MSRB Rule G–37 Interpretive Notice—Application of Rule G–37 to Presidential Campaigns of Issuer Officials (March 23, 1999).

[81] *See* proposed Rule G–37(b)(i)(A).

[82] *See* proposed Rule G–37(b)(i)(B).

[83] *See* proposed Rule G–37(b)(i)(C). The ban on business for the dealer or municipal advisor, like the current treatment under Rule G–37, would only begin when such individual becomes an MFP or MAP of the dealer or municipal advisor, as applicable.

defined in proposed Rule G–37(g)(iii)(B)). To improve the readability of this provision, Rule G–37(b)(ii), as proposed to be amended, would refer to the relevant MFPs and MAPs by the proposed descriptive terms (discussed above) rather than by cross-reference to the relevant definitions. Lastly, a technical amendment would be incorporated in proposed Rule G–37(b)(ii)(B) to clarify that the non-solicitation condition would not be required to be met for the contribution to be excluded after two years have elapsed since the making of the contribution.

Currently, under Rule G–37(b)(iii), contributions by MFPs who have that status solely by virtue of their supervisory or management-level activities, including persons serving on an executive or management committee (*i.e.,* those persons described in paragraphs (C), (D) and (E) of current Rule G–37(g)(iv), the definition of municipal finance professional) are excluded and do not trigger a ban on municipal securities business if such contributions were made more than six months before the contributor obtained (including by designation) his or her MFP status. The proposed amendments to Rule G–37 would relocate to paragraph (b)(ii)(C) this exclusion applicable to such MFPs (*i.e.,* ''municipal finance principals,'' ''dealer supervisory chain persons,'' and ''dealer executive officers'' as defined in proposed Rule G–37(g)(ii)(C), (D) and (E)) and, similarly, would treat contributions made, under the same circumstances, by the analogous categories of MAPs as excluded contributions. The analogous categories of MAPs would be those MAPs that have MAP status solely by virtue of their supervisory or management-level activities, including persons serving on an executive or management committee (*i.e.,* ''municipal advisor principals,'' ''municipal advisor supervisory chain persons,'' and ''municipal advisor executive officers'' as defined in proposed Rule G–37(g)(iii)(C), (D) and (E)). To improve the readability of this provision, proposed Rule G–37(b)(ii), as proposed to be amended, would refer to the relevant MFPs and MAPs by the proposed descriptive terms rather than by cross-references to the relevant definitions.

Prohibition on Soliciting and Coordinating Contributions

Currently, Rule G–37(c)(i) prohibits a dealer and an MFP of the dealer from soliciting any person or PAC to make any contribution or coordinating any contributions to an issuer official with which the dealer is engaging or is seeking to engage in municipal securities business. The proposed amendments to this subsection would retain this prohibition with respect to dealers and their MFPs and would extend the prohibition to municipal advisors and their MAPs. Further, to ensure a relevant nexus exists between the type of business in which a regulated entity engages or seeks to engage and its solicitation or coordination of any contributions to an ME official with the influence to award such business, proposed subsection (c)(i) would be amended to distinguish contributions based on the type of influence held by the ME official.

Thus, under proposed subsection (c)(i), a dealer and an MFP of the dealer would be prohibited from soliciting any person or PAC to make any contribution, or from coordinating any contributions, to an official of a municipal entity with dealer selection influence with which municipal entity the dealer is engaging, or is seeking to engage, in municipal securities business. Similarly, a municipal advisor and an MAP of the municipal advisor would be prohibited from soliciting any person or PAC to make any contribution, or from coordinating any contributions, to an official of a municipal entity with municipal advisor selection influence with which municipal entity the municipal advisor is engaging, or is seeking to engage, in municipal advisory business. In addition, in light of the nexus that exists between a municipal advisor third-party solicitor's business (to solicit business on behalf of dealers, municipal advisors and investment advisers) and ME officials of every type, the prohibition on soliciting and coordinating contributions would apply, for municipal advisor third-party solicitors, to the solicitation or coordination of contributions to any ME official, if the ME official has municipal advisor selection influence, dealer selection influence or investment adviser selection influence.

Because dealer-municipal advisors engage in both municipal securities business and municipal advisory business, and consistent with the principle that dealer-municipal advisors should be treated as a single economic unit, proposed subsection (c)(i) would not, for dealer-municipal advisors, distinguish a contribution given to an official of a municipal entity with dealer selection influence from one given to an official of a municipal entity with municipal advisor selection influence. Thus, a dealer-municipal advisor, its MFPs, and its MAPs would be prohibited from soliciting any person or PAC to make any contribution or coordinating any contributions to an official of a municipal entity with dealer selection influence or municipal advisor selection influence with which municipal entity the dealer-municipal advisor is engaging or is seeking to engage in municipal securities business or municipal advisory business. If the dealer-municipal advisor is a municipal advisor third-party solicitor, the dealer-municipal advisor and its MAPs would also be prohibited from soliciting or coordinating contributions to an official with investment adviser selection influence.

Currently, Rule G–37(c)(ii) prohibits a dealer and three of the five categories of MFPs as defined, respectively, in current Rule G–37(g)(iv)(A), (B) and (C), from soliciting any person or PAC to make any payment or coordinate any payments to a political party of a state or locality where the dealer is engaging or seeking to engage in municipal securities business. Proposed amendments to this subsection would retain this prohibition with respect to dealers and these categories of MFPs and would extend the prohibitions to municipal advisors and the three analogous categories of MAPs (''municipal advisor representatives,'' ''municipal advisor solicitors,'' and ''municipal advisor principals,'' as defined, respectively, in proposed Rule G–37(g)(iii)(A), (B) and (C)). To improve the readability of this provision, Rule G–37(c)(ii), as proposed to be amended, would refer to the relevant MFPs and MAPs by their proposed descriptive terms, rather than by cross-references to the relevant definitions.

Prohibition on Circumvention of Rule

Rule G–37(d) currently prohibits a dealer and any MFP of the dealer from doing, directly or indirectly, through or by any other person or means, any act which would result in a violation of the ban on municipal securities business or the prohibition on soliciting or coordinating contributions. Proposed amendments to this section would retain this prohibition with respect to dealers and their MFPs and would extend it to municipal advisors and their MAPs.

Public Disclosure of Contributions and Other Information

Currently, Rule G–37(e) contains broad public disclosure requirements to facilitate enforcement of Rule G–37 and to promote public scrutiny of dealers' political contributions and municipal securities business. Under the provision, dealers are required to

disclose publicly on Form G–37 information about certain: (i) Contributions to issuer officials; (ii) payments to political parties of states or political subdivisions; (iii) contributions to bond ballot campaigns; and (iv) information regarding municipal securities business with issuers. Currently, Form G–37 may be provided to the Board in paper or electronic form.

The proposed amendments to Rule G–37(e) would retain these disclosure requirements for dealers, except such requirements would apply to contributions to ''officials of municipal entities,'' which is a potentially broader group of recipients than ''officials of an issuer.'' [84] The disclosure requirements would also apply to municipal securities business with ''municipal entities'' rather than ''issuers.'' Proposed amendments to Rule G–37(e)(iv), however, would remove the option of making paper, rather than electronic, submissions to the Board.

For municipal advisors, the disclosure requirements of proposed amended Rule G–37(e), would be substantially similar to those for dealers, with one exception for municipal advisor third-party solicitors. The proposed amendments to Rule G–37(e)(i)(C) would require municipal advisor third-party solicitors to list on Form G–37 the names of the third parties on behalf of which they solicited business as well as the nature of the business solicited. The proposed amendments to Rule G–37(e)(iv) would require municipal advisors, like dealers, to submit the required disclosures to the Board in electronic form. The MSRB also proposes to incorporate minor, non-substantive changes to section (e) to improve the readability of the section.

Currently, Rule G–37(f) permits dealers to submit additional voluntary disclosures to the Board. The proposed amendments to Rule G–37(f) would make no change in this respect for dealers and would permit municipal advisors also to make voluntary disclosures.

Definitions

Current Rule G–37(g) sets forth definitions for several terms used in Rule G–37. Proposed amendments to this section (which are not addressed in detail elsewhere in this filing) would add to Rule G–37 new defined terms and would modify existing defined terms in large part to make the appropriate provisions of Rule G–37 applicable to municipal advisors and their associated persons. The first new defined term, ''regulated entity,'' in proposed Rule G–37(g)(i), would mean ''a dealer or municipal advisor,'' and the terms ''regulated entity,'' ''dealer'' and ''municipal advisor'' would exclude the entity's associated persons. With the addition of the defined term ''regulated entity'' current Rule G–37(g)(iii), which distinguishes dealers from their associated persons, would be deleted as unnecessary. The definition of ''reportable date of selection'' would be amended to apply it to municipal advisors, to slightly reorganize the definition and to relocate it from Rule G–37(g)(xi) to proposed Rule G–37(g)(xviii).

Several of the proposed new defined terms for municipal advisors would be analogous to the defined terms applicable to dealers in current Rule G–37. Proposed Rule G–37(g)(xiv) would define the new term ''non-MAP executive officer'' regarding the executive officers of a municipal advisor in a manner analogous to the term ''non-MFP executive officer'' applicable to executive officers of dealers under proposed Rule G–37(g)(xv).[85] Also, proposed Rule G–37(g)(iv) would define the new term ''bank municipal advisor'' in a manner analogous to the current definition of the term ''bank dealer'' under Rule D–8.[86] The term ''municipal advisor'' would be defined based on the definition of the term in the Exchange Act and Commission rules.[87]

The proposed amendments would renumber and relocate a number of definitions in Rule G–37(g) as follows: ''bond ballot campaign'' would be relocated from subsection (g)(x) to proposed subsection (g)(v); ''issuer'' would be relocated from subsection (g)(ii) to proposed subsection (g)(vii); ''payment'' would be relocated from subsection (g)(viii) to proposed subsection (g)(xvii); ''municipal securities business'' would be relocated from subsection (g)(vii) to proposed subsection (g)(xii); and ''contribution'' would be relocated from subsection (g)(i) to proposed subsection (g)(vi). With the exception of substituting the term ''municipal entity'' in place of ''issuer'' in the definition of the terms ''contribution'' and ''municipal securities business,'' the proposed amendments to Rule G–37(g) would not substantively amend the definitions of these terms.

Operative Date

Current Rule G–37(h) provides that a ban on business under the rule arises only from contributions made on or after April 25, 1994 (the original effective date of Rule G–37). Proposed amendments to section (h) would provide that a ban on applicable business under the rule would arise only from contributions made on or after an effective date to be announced by the MSRB in a regulatory notice published no later than two months following SEC approval, which effective date shall be no sooner than six months following publication of the regulatory notice and no later than one year following SEC approval. However, with respect to dealers and dealer-municipal advisors that are currently subject to the requirements of Rule G–37, any ban on municipal securities business that was already triggered before the effective date of the proposed rule change would remain in effect and end according to the provisions of Rule G–37 as in effect at the time of the contribution that triggered the ban.

Exemptions

Rule G–37 currently provides two mechanisms through which a dealer may be exempted from a ban on municipal securities business. First, under current Rule G–37(i), a registered securities association of which a dealer is a member, or another appropriate regulatory agency [88] (collectively, ''agency'') may, upon application, exempt a dealer from a ban on municipal securities business. In determining whether to grant the exemption, the agency must consider, among other factors:

- Whether the exemption is consistent with the public interest, the protection of investors and the purposes of the rule;

[84] The MSRB does not propose to amend the existing disclosure requirements to limit the disclosure of contributions based on the relevant ME official's type of influence. Rather, to further the purposes of the proposed rule change, including permitting the public to scrutinize the political contributions of regulated entities and to address the appearance of *quid pro quo* corruption, the applicable disclosures would be required for contributions to any type of ME official.

[85] The current definition of ''Non-MFP executive officer'' would be relocated from Rule G–37(g)(v) to proposed Rule G–37(g)(xv) and incorporate minor, technical changes to the term (*e.g.,* to update a cross-reference and to replace the phrase ''broker, dealer or municipal securities dealer,'' with ''dealer'').

[86] ''Bank municipal advisor'' is defined in proposed Rule G–37(g)(iv) to mean: ''a municipal advisor that is a bank or a separately identifiable department or division of the bank as defined in Section 15B(e)(4) of the Act and 17 CFR 240.15Ba1–1(d)(4)(i) thereunder.''

Rule D–8 defines the term ''bank dealer'' to mean ''a municipal securities dealer which is a bank or a separately identifiable department or division of a bank as defined in rule G–1 of the Board.''

[87] ''Municipal advisor'' is defined in proposed Rule G–37(g)(viii) to mean: ''a municipal advisor that is registered or required to be registered under Section 15B of the Act and the rules and regulations thereunder.''

[88] Under MSRB Rule D–14, ''[w]ith respect to a broker, dealer, or municipal securities dealer, 'appropriate regulatory agency' has the meaning set forth in Section 3(a)(34) of the Act.''

• whether, prior to the time a triggering contribution was made, the dealer had developed and instituted procedures reasonably designed to ensure compliance with the rule, and had no actual knowledge of the triggering contribution;

• whether the dealer has taken all available steps to cause the contributor to obtain a return of the triggering contribution(s), and has taken other remedial or preventive measures as appropriate under the circumstances, and the nature of such other remedial or preventive measures directed specifically toward the contributor who made the triggering contribution and all employees of the dealer;

• whether, at the time of the triggering contribution, the contributor was an MFP or otherwise an employee of the dealer, or was seeking such employment;

• the timing and amount of the triggering contribution;

• the nature of the election (*e.g.,* federal, state or local); and

• the contributor's apparent intent or motive in making the triggering contribution, as evidenced by the facts and circumstances surrounding the triggering contribution.[89]

The proposed amendments to section (i) would extend its provisions to municipal advisors, including municipal advisor third-party solicitors, and bans on municipal advisory business, on generally analogous terms. The proposed amendments would provide a process for municipal advisors subject to a ban on municipal advisory business to request exemptive relief from such ban on business from a registered securities association of which is it a member or the Commission, or its designee, for all other municipal advisors. Dealer-municipal advisors seeking exemptive relief from a ban on municipal securities business and a ban on municipal advisory business must, for each type of ban, seek relief from the applicable agency or agencies. With respect to dealers, the proposed amendments to section (i) would also make minor, non-substantive changes to improve its readability.

Under the proposed amendments, in determining whether to grant the requested exemptive relief from a ban on municipal advisory business, the relevant agency would be required to consider the factors, with limited modifications, that currently apply when a request for exemptive relief is made by a dealer. The proposed modifications to the factors are limited to those necessary to reflect their application to both dealers and municipal advisors[90] and to make them otherwise consistent with previously discussed proposed amendments to Rule G–37. Specifically, subsection (i)(i), which currently requires an agency to consider whether the requested exemptive relief would be ''consistent with the public interest, the protection of investors and the purposes of'' Rule G–37, would be amended to require consideration also of whether such exemptive relief would be consistent with the protection of municipal entities and obligated persons. In addition, as incorporated throughout the proposed amended rule, the term ''regulated entity'' would be substituted for the deleted phrase, ''broker, dealer or municipal securities dealer.''

As previously discussed, under the proposed amendments to Rule G–37(b), a contribution made by an MAP of a municipal advisor third-party solicitor soliciting business for a dealer client or a municipal advisor client would subject both the municipal advisor third-party solicitor and the regulated entity client to a ban on applicable business. Under the proposed amendments to section (i), if either the municipal advisor third-party solicitor or the regulated entity client desired exemptive relief from the applicable ban on business, the entity that desired relief would be required to separately apply for the exemptive relief and independently satisfy the relevant agency that the application should be granted.

Second, under Rule G–37(j)(i), a dealer currently may avail itself of an automatic exemption (*i.e.,* without the need to apply to an agency) from a ban triggered by its MFP if the dealer: Discovered the contribution within four months of the date of contribution; the contribution did not exceed $250; and the MFP obtained a return of the contribution within sixty days of the dealer's discovery of the contribution. Rule G–37(j)(ii) currently limits the number of automatic exemptions available to a dealer to no more than two automatic exemptions per twelve-month period. Rule G–37(j)(iii) currently further limits the use of the automatic exemption, providing that a dealer may not execute more than one automatic exemption relating to contributions made by the same person (*i.e.,* an individual MFP) regardless of the time period.

The proposed amendments to section (j) would extend its provisions to all municipal advisors and bans on municipal advisory business. A municipal advisor could avail itself of an automatic exemption from a ban triggered by an MAP of the municipal advisor upon satisfaction of conditions that are the same or analogous[91] to those currently applicable to dealers. Similarly, a dealer-municipal advisor subject to a cross-ban could avail itself of an automatic exemption from a ban on applicable business upon satisfaction of the applicable conditions.[92] In addition, when a contribution made by an MAP of the municipal advisor third-party solicitor soliciting business for a regulated entity client would subject both the municipal advisor third-party solicitor and the regulated entity client to a ban on applicable business, each would be allowed to avail itself of an automatic exemption if it separately met the specified conditions. The use of an automatic exemption would count against a regulated entity's allotment (of no more than two automatic exemptions) per twelve-month period, regardless of whether the contribution that triggered the ban was made by an MFP or an MAP of that regulated entity or by an MAP of an engaged municipal advisor third-party solicitor.

Proposed Amendments to Rules G–8 and G–9 and Forms G–37 and G–37x

The proposed amendments to Rule G–8 (books and records) and Rule G–9 (preservation of records) would make related changes to those rules based on the proposed amendments to Rule G–37. The proposed amendments to Rule G–8 would add a new paragraph (h)(iii) to impose the same recordkeeping requirements related to political contributions by municipal advisors and their associated persons as currently exist for dealers and their associated persons. With respect to dealers, minor conforming proposed amendments to Rule G–8(a)(xvi) would be incorporated to conform the recordkeeping requirements of the rule to the proposed

[89] *See* Rule G–37(i).

[90] For example, in the case of a municipal advisor, the proposed amendments to Rule G–37(i)(iii) would require an agency to consider whether, at the time of the triggering contribution, the contributor was an MAP, otherwise an employee of the municipal advisor, or was seeking such employment, or was an MAP or otherwise an employee of a municipal advisor third-party solicitor engaged by the municipal advisor, or was seeking such employment.

[91] For example, in the case of a municipal advisor pursuing an automatic exemption, the proposed amendments to Rule G–37(j)(i)(C) would require the MAP-contributor to obtain the return of the triggering contribution.

[92] A cross-ban would be considered one ban on business. Thus, under section (j)(ii), as proposed to be amended, the execution by a dealer-municipal advisor of the automatic exemptive relief provision to address a cross-ban would be the execution of one exemption.

amendments to Rule G–37 regarding dealers. For example, the proposed rule change would incorporate in Rule G–8(a)(xvi) certain terms added to the definition of municipal finance professional, and the obligation to submit Forms G–37 and G–37x to the Board in electronic form.

The proposed amendments to Rule G–9(h) would generally require municipal advisors to preserve for six years the records required to be made in proposed amended Rule G–8(h)(iii), consistent with the analogous retention requirement in Rule G–9(a) for dealers.

The proposed amendments to Forms G–37 and G–37x would permit the forms to be used by both dealers and municipal advisors to make the disclosures that would be required by proposed amended Rule G–37(e). Dealer-municipal advisors could make all required disclosures on a single Form G–37.

2. Statutory Basis

Section 15B(b)(2) of the Exchange Act [93] provides that

[t]he 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 [94] provides that the MSRB's rules shall

be designed to prevent fraudulent and manipulative acts and practices, to promote 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 MSRB believes that the proposed rule change is consistent with the Act. It would address potential ''pay to play'' practices by municipal advisors involving corruption or the appearance of corruption. Doing so is consistent with the intent of Congress in granting rulemaking jurisdiction over municipal advisors to the MSRB. As the Commission has recognized, the regulation of municipal advisors and their advisory activities is generally intended to address problems observed with the unregulated conduct of some municipal advisors, including ''pay to play'' practices.[95] Indeed, the relevant legislative history indicates that Congress determined to grant rulemaking authority over municipal advisors to the MSRB, in part, because it already ''has an existing, comprehensive set of rules on key issues such as pay-to-play and . . . that consistency would be important to ensure common standards.'' [96]

The proposed amendments to Rule G–37 would subject all municipal advisors, including municipal advisor third-party solicitors, to ''pay to play'' regulation that is consistent with the MSRB's regulation of dealers.[97] Like dealers, municipal advisors that seek to influence the award of business by government officials by making, soliciting or coordinating political contributions to officials can distort and undermine the fairness of the process by which government business is awarded, creating artificial impediments to a free and open market in municipal securities and municipal financial products. These practices can harm obligated persons, municipal entities and their citizens by resulting in inferior services and higher fees, as well as contributing to the violation of the public trust of elected officials who might allow political contributions to influence their decisions regarding public contracting. ''Pay to play'' practices are rarely explicit: Participants do not typically let it be known that contributions or payments are made or accepted for the purpose of influencing the selection of a municipal advisor (or dealer, municipal advisor or investment adviser on behalf of which a municipal advisor acts as a solicitor).[98] Nonetheless, numerous developments in recent years have led the MSRB to conclude that the selection of market participants that may now be defined as municipal advisors has been influenced by ''pay to play'' practices and that political contributions as the *quid pro quo* for the award of valuable financial services contracts have been funneled through third parties that may now be municipal advisor third-party solicitors as defined in the proposed rule change. These include public reports of ''pay to play'' practices involving the use of persons that may now be defined as municipal advisors,[99] legislative and regulatory statements regarding the activity engaged in by some persons that may now be defined as municipal advisors,[100] market participant

[93] 15 U.S.C. 78*o*–4(b)(2).

[94] 15 U.S.C. 78*o*–4(b)(2)(C).

[95] *See* Order Adopting SEC Final Rule, 78 FR at 67469, 67475 nn.104–6 and accompanying text (discussing relevant enforcement actions); Senate Report, at 38.

[96] Senate Report, at 149.

[97] Some financial advisory firms that may now be defined as municipal advisory firms are registered as dealers and therefore subject to current Rule G–37. With respect to municipal advisors that are not dealers, as of 2009, approximately fifteen states had some form of ''pay to play'' prohibition, some of which were broad enough to apply to financial advisory services. Some municipalities also have such rules. In many cases, the limited and patchwork nature of these state and local laws has not been effective in addressing in a comprehensive way the possibility and appearance of ''pay to play'' practices in the municipal securities market. *See* Statement of Ronald A. Stack, Chair, MSRB, Before the Senate Committee on Banking, Housing and Urban Affairs (Mar. 26, 2009).

[98] *See Blount,* 61 F.3d at 945 (''While the risk of corruption is obvious and substantial, actors in this field are presumably shrewd enough to structure their relations rather indirectly. . . .''); *id.* (''[N]o smoking gun is needed where, as here, the conflict of interest is apparent, the likelihood of stealth great, and the legislative purpose prophylactic.'').

[99] *See, e.g.,* Randall Jensen, *Some California FAs Use Pay-to-Play Tactics, Critics Say,* Bond Buyer, May 24, 2012 (suggesting that some financial advisors may engage in ''pay to play'' practices in the municipal market and noting that they are not currently subject to ''pay to play'' regulation); Randall Jensen, *Brokers' Gifts That Keep Giving,* Bond Buyer, January 13, 2012 (suggesting that the selection of dealers, financial advisors and other professionals in connection with bond ballot initiatives is motivated by ''pay to play'' practices and noting that financial advisors generally donate more than dealers but are not required to disclose contributions to the MSRB); Mary Williams Walsh, *Nationwide Inquiry on Bids for Municipal Bonds,* N.Y. Times, January 8, 2009, at A1 (reporting that ''pay to play'' in the municipal bond market was widespread, and specifically referencing ''independent specialists who are supposed to help local governments''); Sarah McBride and Leslie Eaton, *Legal Run-Ins Dog the Firm in New Mexico Probe,* Wall St. J., January 7, 2009 and Mary Williams Walsh, *Bond Advice Leaves Pain in Its Wake,* N.Y. Times, February 16, 2009 (both describing potential ''pay to play'' activity in the municipal securities market engaged in by an ''unregulated'' adviser); Brad Bumsted, *Firm in ''Pay to Play'' Probe Got $770,000 From State,* Pittsburgh Trib. Rev., January 6, 2009 (reporting on the political contributions made by the head of a financial advisory firm and the awarding of a financial advisory contract to that firm in the context of a nationwide inquiry into ''pay to play'' practices in the municipal bond market); and Lynn Hume, *SEC Doing Pay-to-Play Examinations,* Bond Buyer, July 1, 2004 (reporting SEC plans to examine a number of financial advisors and broker-dealers to determine if they have engaged in ''pay to play'' activities in the municipal market).

[100] *See* nn. 95 and 97 and accompanying text. *See also Bond Regulators Eye Campaign Contribution Abuses,* Reuters, April 10, 2003, available at Westlaw, 4/10/03 Reuters News 20:14:27 (citing Commission, MSRB, and NASD (now FINRA) concerns of continued ''pay to play'' activity in the market, based on reports involving suspicious conduct engaged in by some market participants, including financial advisors); and SEC Report, at 102 (''[O]ther forms of potentially problematic pay-to-play activities involving commodity trading

Continued

comments submitted to the MSRB regarding ''pay to play'' regulation,[101] and a number of enforcement actions involving potential ''pay to play'' practices and financial advisors or third-party intermediaries that may now be defined as municipal advisors.[102]

The proposed rule change is expected to aid municipal entities that choose to engage municipal advisors in connection with their issuance of municipal securities as well as transactions in municipal financial products by promoting higher ethical and professional standards of such advisors and helping to ensure that the selection of such municipal advisors is based on merit and not tainted by *quid pro quo* corruption or the appearance thereof. The MSRB also believes that, by applying the proposed rule change to municipal advisor third-party solicitors, the proposed rule change will level the playing field upon which dealers and municipal advisors (and the third-party dealer, municipal advisor and investment adviser clients of such solicitors) compete because all such persons would be subject to the same or similar requirements.

These parties play a valuable role in the municipal securities market, in the course of providing financial and related advice or in underwriting the securities. The mere perception of *quid pro quo* corruption among such professionals may breed actual *quid pro quo* corruption as municipal advisors, dealers, investment advisers and ME officials alike may feel compelled to take part in ''pay to play'' practices in order to avoid a competitive disadvantage as compared to similarly situated parties they believe do engage in such practices. The appearance of *quid pro quo* corruption in the selection of municipal securities professionals also diminishes investor confidence in the ability or willingness of a dealer, municipal advisor or investment adviser to faithfully fulfill its obligations to municipal entities and the investing public. Such apparent *quid pro quo* corruption also creates artificial impediments to a free and open market as professionals that believe that ''pay to play'' practices are a prerequisite to the receipt of government business but are unwilling or unable to engage in such practices may be reluctant to enter the market and provide to issuers and investors their honest, and potentially more qualified, services. The proposed rule change is expected to curb such *quid pro quo* corruption and the appearance thereof.

Further, the disclosure requirements contained in the proposed rule change will serve to give regulators and the market, including investors, transparency regarding the political contributions of municipal advisors and thereby promote market integrity. The combined effect of the ban on business provisions and the disclosure provisions will serve to reduce the appearance of *quid pro quo* corruption in the municipal market and enhance the ability of the MSRB and other regulators to detect and deter fraudulent or manipulative acts and practices in connection with the awarding of municipal securities business and municipal advisory business (and engagements to provide investment advisory services to the extent a municipal advisor third-party solicitor is used to obtain or retain such business).

Additionally, upon a finding by the Commission that the proposed rule change imposes at least substantially equivalent restrictions on municipal advisors as the IA Pay to Play Rule imposes on investment advisers and that the proposed rule change is consistent with the objectives of the IA Pay to Play Rule, the proposed rule change would serve as a means to permit investment advisers to continue to pay municipal advisors for the solicitation of investment advisory

advisors, municipal advisors, or other municipal securities market participants are not yet directly regulated but raise disclosure issues for investors and the market.'').

[101] Notice of Filing of Proposed Rule Change Relating to Solicitation of Municipal Securities Business Under MSRB Rule G–38, Release No. 34–51561 (April 15, 2005), 70 FR 20782, at 20785–20786 (April 21, 2005) (File No. SR–MSRB–2005–04) (citing comment letters from Jerry L. Chapman, First Southwest Company, Kirkpatrick, Pettis, Smith, Polian Inc., Merrill Lynch and Morgan Keegan & Company, Inc. and stating ''[m]any commentators are concerned that, although the problems associated with pay-to-play in the municipal securities industry are not limited to dealers, only dealers are subject to regulation in this area . . . They urge the MSRB to coordinate efforts with the Commission, NASD and others to apply pay-to-play limits to financial advisors, derivatives advisors, bond lawyers and other market participants'') (internal citations omitted); Notice of Filing of a Proposed Rule Change Relating to Amendments to MSRB Rules G–37 and G–8 and Form G–37, Release No. 34–68872 (February 8, 2013), 78 FR 10656, 10663 (February 14, 2013) (File No. SR–MSRB–2013–01) (summarizing comments from market participants that recommend extending the proposed amendments to Rule G–37 regarding increased disclosure of bond ballot contribution information to municipal advisors); Notice of Filing of Proposed New Rule G–42, on Political Contributions and Prohibitions on Municipal Advisory Activities; Proposed Amendments to Rules G–8, on Books and Records, G–9, on Preservation of Records, and G–37, on Political Contributions and Prohibitions on Municipal Securities Business; Proposed Form G–37/G–42 and Form G–37x/G–42x; and a Proposed Restatement of a Rule G–37 Interpretive Notice, Release No. 34–65255 (September 2, 2011), 76 FR 55976 at 55983 (September 9, 2011) (File No. SR–MSRB–2011–12) (withdrawn) (quoting commenter NAIPFA) (''All too often, we see funds and/or campaign services being contributed to bond campaigns by underwriters [and] financial advisors . . . who end up providing services for the bond transaction work once the election is successful.''). From the time that the MSRB first proposed ''pay to play'' regulation for the municipal securities market, it has received comments from market participants requesting the extension of such regulation to persons that may now be deemed municipal advisors. *See* Notice of Filing of Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Political Contributions and Prohibitions on Municipal Securities Business, Release No. 34–33482 (January 14, 1994), 59 FR 3389, 3402–03 (January 21, 1994) (File No. SR–MSRB–94–02) (summarizing concerns from several commenters that Rule G–37, as initially proposed in 1994, did not apply to certain market participants including third-party solicitors and independent financial advisors).

[102] Financial regulators have brought enforcement actions charging financial advisors with violations of various MSRB fair practice rules in connection with alleged activities that follow or include ''pay to play'' practices and *quid pro quo* exchanges. Other enforcement actions are in response to a specific violation of Rule G–37. *See, e.g., In re Wheat, First Securities, Inc.,* SEC Initial Dec. Rel. No. 155 (December 17, 1999) (finding violation of Rule G–17 and Florida fiduciary duty law for financial advisor's false disclosures to municipal entity regarding the use of a third party—who had ''[o]ver the years, . . . made hundreds, if not thousands, of political contributions'' that ''secure[d]'' his access to officials—to secure its advisory contract with the county); *In re RBC Capital Markets Corp.,* SEC Release No. 59439 (February 24, 2009) (finding that a financial advisor made advances in violation of Rule G–20 on behalf of a municipal entity client to pay for travel and entertainment expenses unrelated to the bond offering); FINRA Letter of Acceptance, Waiver and Consent No. 2009016275601 (February 8, 2011) (finding that dealer that also engaged in financial advisory activities violated a number of MSRB rules, including engaging in municipal securities business notwithstanding a triggering contribution under Rule G–37, and making payments to unaffiliated individuals for the solicitation of municipal securities business under Rule G–38). Criminal authorities have also brought actions against a former Philadelphia treasurer, municipal securities professionals and a third-party intermediary seeking business on behalf of such municipal securities professionals for their participation in a complex scheme involving ''pay to play'' practices. *See, e.g.,* Indictment *U.S.* v. *White, et al.,* No. 04–370 (E.D. Pa. June 29, 2004). In addition, the Commission brought and settled charges against the former treasurer of the State of Connecticut and other parties alleging that engagements to provide investment advisory services were awarded as the *quid pro quo* for payments made to officials that were funneled through third-party intermediaries. *See, e.g., SEC* v. *Paul J. Silvester, et al.,* Litigation Release No. 16759 (October 10, 2000); Litigation Release No. 20027 (March 2, 2007); Litigation Release No. 19583 (March 1, 2006); Litigation Release No. 16834 (December 19, 2000). Similar activity in connection with investment advisers seeking to manage the assets of the New York State Common Retirement Fund resulted in guilty pleas to criminal charges and remedial sanctions in parallel administrative orders. *See, e.g., SEC* v. *Henry Morris, et al.,* Litigation Release No. 22938 (March 10, 2014). For further instances of ''pay to play'' activity involving third-party intermediaries and solicitors that may now be defined as municipal advisors, *see* Order Adopting IA Pay to Play Rule, 75 FR at 41019–20.

services on behalf of the investment adviser.[103]

Section 15B(b)(2)(L)(iv) of the Act [104] requires that rules adopted by the Board

not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.

The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2)(L)(iv) of the Exchange Act. While the proposed rule change would affect all municipal advisors, including small municipal advisors, the MSRB believes it is necessary and appropriate to address ''pay to play'' practices in the municipal market. The MSRB believes that the approach taken under the proposed rule change (which has for more than two decades applied to dealers of diverse sizes) would appropriately accommodate the diversity of the municipal advisor population, including small municipal advisors and sole proprietorships.

The MSRB recognizes that municipal advisors would incur costs to meet the requirements set forth in the proposed rule change. These costs may include additional compliance and recordkeeping costs associated with initially establishing compliance regimes and ongoing compliance, as well as separate legal and compliance fees associated with the triggering of a ban on applicable business or an application for relief from such a ban. Small municipal advisors, however, will necessarily have fewer personnel whose contributions may trigger disclosure obligations or subject the municipal advisory firm to a ban on applicable business under the proposed rule change. Small municipal advisors can also reasonably be expected to have relatively fewer municipal advisory engagements than larger firms and fewer municipal entities with whom they engage in municipal advisory business. Thus, their compliance costs are likely to be significantly lower than relatively larger municipal advisors.

The MSRB also believes that the proposed amendments to Rule G–37(i) regarding application for an exemption from a ban on applicable business and proposed amendments to Rule G–37(j) regarding the automatic exemption from a ban on applicable business provide significant relief to all municipal advisors, including small municipal advisors, from the consequences of an inadvertent triggering contribution. In particular, the automatic exemption provision would provide a regulated entity relief from a ban on applicable business without the need to resort to a formal application for an exemption, which may involve the use of outside legal counsel or compliance professionals.

Additionally, because small municipal advisors can be reasonably expected to employ fewer personnel and/or have fewer engagements, they are likely to have less information to report to the MSRB under the proposed rule change. Further, municipal advisors that meet the standards to file a Form G–37x in lieu of a Form G–37 may avail themselves of relief from all other reporting obligations as long as they continue to meet those standards. Thus, the MSRB believes that the proposed rule change is consistent with the Dodd-Frank Act's provision with respect to burdens that may be imposed on small municipal advisors.

Finally, the MSRB believes that the proposed rule change will allow small municipal advisors to compete based on merit rather than their ability or willingness to make political contributions, which may be a significant benefit relative to the status quo.

The MSRB also believes that the proposed rule change is consistent with Section 15B(b)(2)(G) of the Exchange Act,[105] which provides that the MSRB's rules shall prescribe records to be made and kept by municipal securities brokers, municipal securities dealers, and municipal advisors and the periods for which such records shall be preserved.

The proposed rule change would require, under proposed amendments to Rule G–8, that a municipal advisor make and keep certain records concerning political contributions and the municipal advisory business in which the municipal advisor engages. Proposed amendments to Rule G–9 would require that these records be preserved for a period of at least six years. The MSRB believes that the proposed amendments to Rules G–8 and G–9 related to recordkeeping and records preservation will promote compliance and facilitate enforcement of the proposed amendments to Rule G–37.

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

Section 15B(b)(2)(C) of the Exchange Act [106] requires that MSRB rules not be designed to impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. In addition, Section 15B(b)(2)(L)(iv) of the Exchange Act provides that MSRB rules may

not impose a regulatory burden on small municipal advisors that is not necessary or appropriate in the public interest and for the protection of investors, municipal entities, and obligated persons, provided that there is robust protection of investors against fraud.[107]

The Board's Policy on the Use of Economic Analysis in Rulemaking, according to its transitional terms, does not apply to the Board's consideration of the proposed rule change, as the rulemaking process for the proposed rule change began prior to the adoption of the policy. However, the policy can still be used to guide the consideration of the proposed rule change's burden on competition. The MSRB also considered other economic impacts of the proposed rule change and has addressed any comments relevant to these impacts in other sections of this filing.

The Board has evaluated the potential impacts of the proposed rule change, including in comparison to reasonable alternative regulatory approaches, relative to the baseline. The MSRB does not believe that the proposed rule change will impose any additional burdens, relative to the baseline, that are not necessary or appropriate in

[103] The IA Pay to Play Rule prohibits an investment adviser and its covered associates from providing or agreeing to provide payment to any person to solicit a government entity for investment advisory services unless the person is, in relevant part, a ''regulated person.'' *See* 17 CFR 275.206(4)–5(a)(2)(i)(A). A ''regulated person'' includes a municipal advisor, provided that MSRB rules prohibit such municipal advisors from engaging in distribution or solicitation activities if certain political contributions have been made; and the Commission finds that such rules impose substantially equivalent or more stringent restrictions on municipal advisors as the IA Pay to Play Rule imposes on investment advisers and that such rules are consistent with the objectives of the IA Pay to Play Rule (the ''SEC finding of substantial equivalence''). *See* 17 CFR 275.206(4)–5(f)(9)(iii). The compliance date for the IA Pay to Play Rule's ban on third-party solicitation is July 31, 2015. *See* Investment Advisers Act Release No. 4129 (June 25, 2015), 80 FR 37538 (July 1, 2015). However, the staff of the SEC's Division of Investment Management has indicated that until the later of (i) the effective date of a FINRA ''pay to play'' rule that obtains the SEC finding of substantial equivalence or (ii) the effective date of an MSRB ''pay to play'' rule that obtains the SEC finding of substantial equivalence, it would not recommend enforcement action to the Commission against an investment adviser or its covered associates for violation of the IA Pay to Play Rule's ban on third-party solicitation. *See* SEC, Staff Responses to Questions About the Pay to Play Rule, at Question I.4, available at *https://www.sec.gov/divisions/investment/pay-to-play-faq.htm.* The proposed rule change is intended to impose at least substantially equivalent standards on municipal advisors to the standards imposed on investment advisers under the IA Pay to Play Rule for purposes of the SEC finding of substantial equivalence, however, such a finding may be made only by the Commission.

[104] 15 U.S.C. 78*o*–4(b)(2)(L)(iv).

[105] 15 U.S.C. 78*o*–4(b)(2)(G).

[106] 15 U.S.C. 78*o*–4(b)(2)(C).

[107] 15 U.S.C. 78*o*–4(b)(2)(L)(iv).

furtherance of the purposes of the Act. To the contrary, the MSRB believes that the proposed rule change is likely to increase fair competition.

''Pay to play'' practices may interfere with the process by which municipal advisors or the third-party clients of a municipal advisor third-party solicitor are chosen since the receipt of contributions made by such persons might influence an ME official to award business based, not on merit, but on the contributions received. ''Pay to play'' practices may also raise artificial barriers to entry and detract from fair competition among municipal advisors and the third-party clients of municipal advisor third-party solicitors.[108]

The MSRB believes that the proposed rule change will make it more likely that municipal advisors (and the third-party clients of a municipal advisor third-party solicitor) will be selected based on merit and cost, rather than on contributions to political officials. By serving to level the playing field upon which municipal advisors compete for business and solicit business for others, the proposed rule change will help curb manipulation of the market for municipal advisory services (and municipal securities business and investment advisory services, to the extent a municipal advisor third-party solicitor is used to obtain or retain such business). Municipal entities are, in turn, more likely to receive higher-quality advice and lower costs in procuring such business and services.

As noted by the SEC in the IA Pay to Play Approval Order, the efficient allocation of advisory business may be enhanced when it is awarded to investment advisers that compete on the basis of price, quality of performance and service and not on the influence of political contributions.[109] It is a similar case with the awarding of municipal advisory business to municipal advisors and municipal securities business to dealers. The SEC also noted in the same approval order that investment advisory firms, and particularly smaller investment advisory firms, will be able to compete based on merit rather than their ability or willingness to make political contributions.[110] The SEC's reasoning is equally applicable to the potential impact on municipal advisors and dealers of the proposed rule change. A merit-based process is likely to result in a more efficient allocation of professional engagements, compared to the baseline state.

In addition, the proposed rule change subjects municipal advisory activities to a regulatory regime comparable to the regulatory regimes for other entities and persons in the financial services industry, in particular those such as dealers or investment advisers who provide services to municipal entities and are subject to existing ''pay to play'' rules including Rule G–37 and the IA Pay to Play Rule, respectively.

The MSRB considered whether costs associated with the proposed rule change, relative to the baseline, could affect the competitive landscape. The MSRB recognizes that the compliance, supervisory and recordkeeping requirements associated with the proposed rule change may impose costs and that those costs may disproportionately affect municipal advisors that are not also broker-dealers or that have not otherwise previously been regulated in this area. During the comment period, the MSRB sought information that would support quantitative estimates of these costs, but did not receive any relevant data.

The MSRB believes that the SEC estimates of the costs associated with implementing the IA Pay to Play Rule may provide a guide to the initial, one-time costs that previously unregulated municipal advisors might incur under the proposed rule change. Because even the largest municipal advisory firms are generally smaller than large investment advisory firms, however, the MSRB believes the costs of compliance associated with the proposed rule change will be lower than those associated with the IA Pay to Play Rule.

The MSRB also recognizes that the proposed rule change may cause some firms—either because they have engaged in competition primarily on the basis of political contributions or because of the costs of compliance—to exit the market. Some municipal advisors may consolidate with other municipal advisors in order to benefit from economies of scale (*e.g.,* by leveraging existing compliance resources of a larger firm) rather than to incur separately the costs associated with the proposed rule change. While this might reduce the number of firms competing for business, consolidated firms might compete more effectively on price, which would offer benefits to municipal entities. Some firms wishing to enter the market may find the costs of compliance create barriers to entry. Finally, some dealer-municipal advisors may separate and form dealer-only and municipal advisor-only firms to avoid the ''cross-ban.'' If separations result in lost efficiencies of scope, such firms may compete less effectively on price—potentially raising issuance costs, but the presence of such firms also may potentially foster greater competition, particularly among smaller firms.

The MSRB recognizes that small municipal advisors and sole proprietors may not employ full-time compliance staff and that the cost of ensuring compliance with the requirements of the proposed rule change may be proportionally higher for these smaller firms, potentially leading to exit from the industry or consolidation. However, as the SEC recognized in its Order Adopting SEC Final Rule, the market for municipal advisory services is likely to remain competitive despite the potential exit of some municipal advisors (including small entity municipal advisors) or the consolidation of municipal advisors.[111]

The MSRB also believes that the proposed amendments to Rule G–37(i) regarding application for an exemption from a ban on applicable business and proposed amendments to Rule G–37(j) regarding the automatic exemption from a ban on applicable business provide significant relief to all municipal advisors, including small municipal advisors, from the consequences of an inadvertent triggering contribution. In particular, the automatic exemption provision would provide a regulated entity relief from a ban on applicable business without the need to resort to a formal application for an exemption, which may involve the use of outside legal counsel or compliance professionals.

Overall, the MSRB believes that the proposed rule will not, on its own, significantly change the number or concentration of firms offering municipal advisory services and that the increased focus on merit and cost will result in a more competitive market.

The MSRB solicited comment on the potential burdens of the draft amendments to Rules G–37, G–8 and G–9 in a notice requesting comment, which notice incorporated the MSRB's preliminary economic analysis.[112] The specific comments and the MSRB's responses thereto are discussed in Section C.

[108] Because of the illicit nature of the activity, quantifying the extent of *quid pro quo* corruption is difficult. In its order providing for the registration of municipal advisors, however, the Commission noted that the new municipal advisor registration and regulatory regime is intended to mitigate some of the problems observed with the conduct of some municipal advisors, *including ''pay to play'' practices. See* Order Adopting SEC Final Rule, 78 FR at 67469.

[109] *See* Order Adopting IA Pay to Play Rule, at 41053.

[110] *See id.*

[111] *See* Order Adopting SEC Final Rule, at 67608.

[112] MSRB Notice 2014–15, Request for Comment on Draft Amendments to MSRB Rule G–37 to Extend its Provisions to Municipal Advisors (August 18, 2014) (''Request for Comment'').

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

The MSRB received thirteen comment letters in response to the Request for Comment.[113] The comment letters are summarized below by topic and the MSRB's responses are provided.

Support for the Proposed Rule Change

Most commenters supported to some degree the initiative to extend the policies contained in Rule G–37 to municipal advisors. The Public Interest Groups stated that, by recognizing that municipal advisors may play a key role in underwriting and other municipal funding decisions, the MSRB's expansion of the scope of the rule will help promote the integrity of the contracting process. BDA supported the objective of the draft amendments on the grounds that it would create a level playing field between dealers and municipal advisors. SIFMA maintained that it is important that all market participants are subject to the same rules applicable to political activity, and that the draft amendments significantly advance that interest. NAIPFA supported the draft amendments without qualification. Sanchez noted the draft amendments would address practices that create artificial barriers to competition.

Several commenters expressed support for specific provisions in the draft amendments. The Public Interest Groups and CCP supported replacing the term ''official of an issuer'' with the new defined term ''official of a municipal entity.'' CCP further supported the draft amendments' creation of different categories of ''officials of a municipal entity.'' SIFMA and CCP both expressed support for the purpose for which these categories were created—namely, to ensure that there is a nexus between a contribution and the awarding of business that gives rise to a sufficient risk of corruption, or the appearance thereof, to warrant a ban on applicable business.

De Minimis Contributions

Under draft amended Rule G–37(b)(ii)(A), contributions made by an MFP or MAP to an ME official for whom the MFP or MAP is entitled to vote would be *de minimis* and would not trigger a ban on municipal securities business or municipal advisory business if such contributions made by such MFP or MAP do not, in total, exceed $250 per election. Five commenters said that the MSRB should harmonize this *de minimis* exclusion with those set forth for investment advisers under the IA Pay to Play Rule,[114] and two of these five commenters said that the *de minimis* exclusion should be harmonized with those set forth for swap dealers under the Swap Dealer Rule.[115] As described below, however, the comments differed with regard to the extent of harmonization suggested and the offered rationale for harmonization. Two additional commenters opposed any modification to the *de minimis* exclusion.[116]

Raising the Threshold for the Existing De Minimis Exclusion

The five commenters that supported greater harmonization agreed that Rule G–37 should be modified to raise the threshold from $250 to $350 for the existing *de minimis* exclusion under draft amended Rule G–37(b)(ii).

SIFMA, BDA and C&D supported a $350 *de minimis* threshold principally on the basis of promoting more efficient administration of federal ''pay to play'' programs and reducing the compliance burdens on those regulated entities that are also subject to the IA Pay to Play Rule and the Swap Dealer Rule[117]—both of which have a *de minimis* threshold of $350 for a contribution to an official for whom the contributor is entitled to vote.[118] SIFMA expressed the view that both the $250 *de minimis* threshold in Rule G–37 as well as the $350 *de minimis* threshold utilized in the IA Pay to Play Rule[119] appear to be somewhat arbitrary. However, it argued, to the extent a *de minimis* amount is exempted, it should be uniform across the federal ''pay to play'' regimes. In contrast, NAIPFA expressed unqualified support for the draft amendments and specifically opposed any increase in the *de minimis* threshold of $250. Sanchez also opposed any change to the *de minimis* threshold, commenting that Rule G–37 has been an important tool in enhancing free and fair competition and that a change in the *de minimis* threshold would provide a distinct and unfair advantage to large financial services firms over smaller firms.

CCP and Callcott framed their arguments for a $350 *de minimis* threshold based on First Amendment concerns. Because the IA Pay to Play Rule[120] appeared to embody a determination that a *de minimis* threshold of $350 was sufficient to prevent *quid pro quo* corruption, or the appearance thereof, they suggested the MSRB's proposed $250 *de minimis* threshold could not be ''narrowly tailored to achieve a compelling government interest.'' While CCP was skeptical as to whether the *de minimis* thresholds under the IA Pay to Play Rule are consistent with constitutional requirements, it expressed concern that the MSRB did not articulate why these thresholds are not sufficient for purposes of Rule G–37. Callcott argued that, although Rule G–37's $250 *de minimis* threshold was upheld by the DC Circuit in *Blount*[121] in 1995, the rule cannot continue to withstand constitutional scrutiny in the wake of the IA Pay to Play Rule[122] and Supreme Court cases decided since *Blount,* including *McCutcheon* v. *FEC.*[123] In contrast, Sanchez stated that unlike some of the recent Supreme Court rulings on political contributions, Rule G–37 is narrowly tailored to only affect persons who seek specific types of business with municipal entities and not citizens at large.

The MSRB is sensitive to the effect of differing ''pay to play'' *de minimis* thresholds for dealers and municipal advisors that also operate in the

[113] Comments were received from American Council of Engineering Companies: Letter from David A. Raymond, President & CEO, dated October 1, 2014 (''ACEC''); Anonymous Attorney: Email from Anonymous, dated October 1, 2014 (''Anonymous''); Bond Dealers of America: Letters from Michael Nicholas, Chief Executive Officer, dated October 1, 2014 (''First BDA'') and October 8, 2014 (''Second BDA'') (together, ''BDA''); Caplin & Drysdale, Chtd.: Letter from Trevor Potter and Matthew T. Sanderson, dated September 30, 2014 (''C&D''); Castle Advisory Company LLC: Email from Stephen Schulz, dated August 18, 2014 (''Castle''); Center for Competitive Politics: Letter from Allen Dickerson, Legal Director, dated October 1, 2014 (''CCP''); Dave A. Sanchez: Letter from Dave A. Sanchez, dated November 5, 2014 (''Sanchez''); Hardy Callcott: Email from Hardy Callcott, dated September 9, 2014 (''Callcott''); National Association of Independent Public Finance Advisors: Letter from Jeanine Rodgers Caruso, President, dated October 1, 2014 (''NAIPFA''); Public Citizen, et al.: Letter from Bartlett Naylor, Financial Policy Advocate, et al., dated October 1, 2014 (''The Public Interest Groups''); Securities Industry and Financial Markets Association: Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, dated September 30, 2014 (''SIFMA''); and WM Financial Strategies: Letter from Joy A. Howard, Principal, dated October 1, 2014 (''WMFS'').

[114] *See* 17 CFR 275.206(4)–5.

[115] *See* 17 CFR 23.451. BDA, C&D, CCP, Callcott and SIFMA proposed harmonization with the IA Pay to Play Rule. BDA and SIFMA also proposed harmonization with the Swap Dealer Rule.

[116] NAIPFA and Sanchez opposed modification to the *de minimis* exclusion.

[117] C&D also noted that a $350 threshold would partly account for the effects of inflation since the Board first established $250 as the threshold in 1994.

[118] *See* 17 CFR 275.206(4)–5(b)(1); *see also* 17 CFR 23.451(b)(2)(i)(A).

[119] *See id.*

[120] *Id.*

[121] *Blount* v. *SEC,* 61 F.3d 938 (D.C. Cir. 1995), *cert. denied,* 517 U.S. 1119 (1996).

[122] *See* 17 CFR 275.206(4)–5.

[123] *McCutcheon* v. *FEC,* 572 U.S. ____, 134 S. Ct. 1434 (2014) (''*McCutcheon*'').

investment advisory market or the swap market. However, the Board believes that, to the extent possible and appropriate, consistency between the regulatory treatment of dealers and municipal advisors, who operate in the same market and typically with the same clients, is vital to curb *quid pro quo* corruption or the appearance thereof in the municipal market. Dealers have been subject to the requirements of Rule G–37 for more than two decades, and as commenters have noted, its terms, including its *de minimis* threshold, have been effective in combating corruption or the appearance of corruption in connection with the awarding of municipal securities business to dealers.[124]

Moreover, as acknowledged by several of the commenters, in *Blount,* the D.C. Circuit previously determined that Rule G–37 was constitutional on the ground that the rule was narrowly tailored to serve a compelling government interest.[125] The court found the interest in protecting investors from fraud and protecting underwriters from unfair, corrupt practices to be compelling.[126] The MSRB does not believe that differing *de minimis* threshold determinations for other markets precludes a determination that the MSRB's *de minimis* threshold for the municipal market is narrowly tailored. The MSRB also believes that commenter references to recent Supreme Court decisions are misplaced. Those cases, for example, did not address regulations aimed at preventing *quid pro quo* corruption or the appearance thereof with respect to individuals engaged in securities-related business with municipal entities, or even regulations regarding individuals engaged in business with a governmental entity more generally. Additionally, recent jurisprudence relating to political contributions and government contractors implicitly contradicts the notion that *Blount* does not survive *McCutcheon. Wagner, et al.,* v. *FEC,*[127] decided *en banc* by the U.S. Court of Appeals for the District of Columbia Circuit after *McCutcheon,* unanimously upheld a provision in the Federal Election Campaign Act that prohibits contributions made in connection with federal elections by federal government contractors. In upholding the provision, the *Wagner* court repeatedly cited *Blount* with approval, noting that it upheld Rule G–37 against First Amendment challenge[128] and that it found Rule G–37 to be '' 'closely drawn,' in part because it 'restrict[ed] a narrow range of . . . activities for a relatively short period of time,' and those subject to the rule were 'not in any way restricted from engaging in the vast majority of political activities.' '' [129] Accordingly, the MSRB has determined to extend the current *de minimis* threshold applicable to dealers in Rule G–37 to municipal advisors through the proposed rule change.

Adding an Additional De Minimis Exclusion

Three of the five commenters that supported greater harmonization also urged the MSRB to add an additional *de minimis* exclusion for contributions made by an MFP or MAP to an ME official for whom the MFP or MAP is not entitled to vote if such contributions do not, in total, exceed $150 per election.[130] These commenters based their arguments on First Amendment concerns. C&D cited statements by the Commission when it adopted the IA Pay to Play Rule,[131] noting that the Commission acknowledged that the $150 limit for contributions to officials for whom the investment adviser could not vote was justified because non-residents might have legitimate interests in those elections, such as the interest of a resident of a metropolitan area in the city in which the person works. C&D suggested that a similar rationale would apply with respect to personnel of dealers and municipal advisors. Similarly, CCP argued that the Supreme Court's ruling in *McCutcheon,* reiterating the importance of associational rights, would make little sense if bans on out-of-district contributions were constitutional. Callcott noted that the ''narrow tailoring'' conclusion of *Blount* cannot continue to survive and noted that the lack of a *de minimis* threshold for contributions to ME officials for whom an MAP is not entitled to vote is particularly vulnerable to First Amendment challenge.

In contrast, BDA, SIFMA and Sanchez did not advocate establishing a second *de minimis* contribution exclusion. BDA expressed concern that such an extension would create considerable chaos in the municipal securities market, and BDA and Sanchez both noted that the current approach in Rule G–37 is accepted and appears to be working well. Specifically speaking to recent Supreme Court jurisprudence, Sanchez expressed the view that Rule G–37 is narrowly tailored to only affect persons who seek specific types of business with municipal entities and not citizens at large.

As discussed above, the MSRB has determined to extend the current *de minimis* threshold applicable to dealers in Rule G–37 to municipal advisors through the proposed rule change. Current Rule G–37 and the proposed amendments are intended to address *quid pro quo* corruption and the appearance thereof in connection with the awarding of municipal securities business, municipal advisory business, and engagements to provide investment advisory services. Even in the absence of actual *quid pro quo* corruption, contributions to officials for whom an MFP or MAP is not entitled to vote are at heightened risk of the appearance of *quid pro quo* corruption, as the MFP or MAP's non–*quid pro quo* interest in that election is less likely to be immediately apparent to the public. Rule G–37 has previously withstood constitutional scrutiny and the proposed rule change would not amend the current *de minimis* thresholds in Rule G–37. The MSRB agrees with Sanchez that the proposed amendments to Rule G–37 are narrowly tailored. The MSRB notes again that comments based upon, or referring to, recent Supreme Court decisions are misplaced. Those cases presented different facts and circumstances and, for example, did not address regulations aimed at preventing *quid pro quo* corruption or the appearance thereof with respect to individuals engaged in securities-related business with municipal entities, or even regulations regarding individuals engaged in business with a governmental entity as a general matter. Further, as described above, *Wagner,* decided since *McCutcheon,* upheld a complete ban with no *de minimis* exclusion on contributions to federal campaigns by federal contractors. This suggests that Rule G–37's more tailored temporary limitation on business activities resulting from non-*de minimis* contributions to ME officials with the ability to influence the awarding of business to the regulated entity (and in the case of a municipal advisor third-party solicitor, the regulated entity clients or investment adviser clients of the municipal advisor third-party solicitor) would also survive constitutional scrutiny.

[124] *See* comment letter from Sanchez; comment letter from SIFMA.

[125] *See Blount,* 61 F.3d at 944, 947–48.

[126] *See id.* at 944.

[127] 793 F.3d 1 (D.C. Cir. 2015) (en banc) (''*Wagner*'').

[128] *Id.* at n. 19.

[129] *Id.* at 26 (quoting *Blount,* 61 F.3d at 947–48).

[130] C&D, CCP and Callcott proposed this approach.

[131] *See* comment letter from C&D, citing Order Adopting IA Pay to Play Rule, at 41035.

Look-Back

SIFMA requested that the MSRB revise the ''look-back'' for MFPs and MAPs, which would provide that a regulated entity would be subject to a ban on applicable business for a period of two years from the making of a triggering contribution, even if such contributions were made by a person before he or she became a ''municipal finance representative'' or ''municipal advisor representative'' of the regulated entity. Under SIFMA's proposed revision, a new exclusion would be added to the ''look-back'' for a contribution made by an individual that, at the time of the contribution, was subject to either the IA Pay to Play Rule or the Swap Dealer Rule if the contribution was made within the *de minimis* exceptions under those rules.

The MSRB has determined not to adopt SIFMA's proposed exclusion. The goal of Rule G–37, and the proposed amendments, is to address *quid pro quo* corruption or the appearance thereof when a contribution is made to an ME official and business of that municipal entity is awarded to the contributor. The MSRB believes that the risk of such corruption or the appearance of such corruption in the municipal securities market is not diminished simply because a contribution does not trigger a ban in a different market under a different regulatory scheme. The exclusion proposed by SIFMA would, in effect, create a bifurcated *de minimis* threshold: One for MFPs and MAPs that were formerly investment advisers or swap professionals and another for all other MFPs and MAPs. As stated above, the MSRB believes that it is important to have a consistent *de minimis* threshold applicable to all regulated entities in the municipal market, as they operate in the same market and typically with the same clients.

Official of a Municipal Entity

WMFS suggested that the MSRB remove the concept of the different types of ME officials from the draft definition of ''official of a municipal entity.'' [132] WMFS stated that it was not aware of any elected official that would be able to influence the selection of a municipal advisor without also having the ability to influence the selection of an underwriter. Thus, in its view, the draft amendments to this definition would unnecessarily complicate the rule and could create an enforcement loophole.

CCP, by contrast, welcomed the constitutional ''tailoring'' of the definition of ''official of a municipal entity'' through the creation of different categories of ME officials, although it suggested the definition was otherwise overbroad and vague. CCP noted that the definition of the term ''official of a municipal entity'' would extend to losing candidates who ultimately do not play a role in the selection of any dealer or municipal advisor, and, thus pose ''little to no danger of pay-to-play corruption.''

The MSRB recognizes that it may be uncommon for an ME official to have the ability to influence the selection of only one type of professional. However, the MSRB has not received any comments that categorically state, much less demonstrate, that there are no such officials. Further, as CCP and other commenters acknowledged, the categories of ME officials are designed to narrowly tailor the rule to ensure that there is a nexus between a contribution made to an ME official and the ability of that ME official to influence the awarding of business to the contributor's firm (or in the case of a municipal advisor third-party solicitor, a regulated entity client or investment adviser client). With regard to CCP's remaining arguments, apart from the creation of the separate categories and the renaming of the ''official of an issuer'' term to ''official of a municipal entity,'' all other elements of the longstanding ''official of an issuer'' definition are unchanged from that found in current Rule G–37. The fact that losing candidates ultimately have no influence in the selection of professionals does not avoid the potential appearance of *quid pro quo* corruption in the case of contributions to candidates. Thus, the MSRB has determined not to revise the definition of ''official of a municipal entity'' in response to the comments received.

Cross-Bans

SIFMA stated that the cross-ban provision in draft amended Rule G–37(b)(i)(C) (proposed paragraph (b)(i)(D)) should be eliminated. SIFMA argued that the cross-ban provision is overly broad and does not comport with the MSRB's stated goal of requiring a link between a triggering contribution and the business banned by that contribution.

In contrast, The Public Interest Groups supported the cross-ban provision, noting that otherwise permitting contributions from one line of business of a dealer-municipal advisory firm to an ME official that has influence over awarding business to the other line of business within the same firm would invite firms to ''create legal fictions for [contributions] between its dealer and advisory services.'' Sanchez stated that the cross-ban would be appropriate for dealer-municipal advisors because many individuals within such firms engage in both dealer and municipal advisory activity, and to the extent that they do not, the business lines can be very closely related. Thus, Sanchez concluded, a contribution from persons or entities associated with one line of business of a dealer-municipal advisory firm and the awarding of business to the other line of business within the same firm will usually constitute *quid pro quo* corruption or give rise to the appearance thereof.

The MSRB does not believe that the cross-ban provision is inconsistent with the MSRB's goal of requiring a link between a ban on applicable business and a contribution made to an ME official with the ability to influence the awarding of that type of business. On the contrary, the cross-ban is a special provision narrowly tailored to ensure that the only business a dealer-municipal advisor will be prohibited from engaging in during the two-year period is the business that the ME official to whom the contribution was made had the ability to influence. While the cross-ban would subject a dealer-municipal advisor to a ban of a scope consistent with the type of influence held by the ME official to whom the contribution was made, the scope of the ban would not be dependent on the particular line of business with which the contributor is associated. The MSRB believes that this is the appropriate result given that, even though a dealer-municipal advisor may have two lines of business, the entity should be considered a single economic unit.

Moreover, the goal of the cross-ban is to address actual *quid pro quo* corruption or its appearance. The comments submitted by Sanchez and The Public Interest Groups support the view that there is a public perception of *quid pro quo* corruption when business is awarded to a dealer-municipal advisor following the making of a contribution to an ME official with the ability to influence the selection of that firm for such business. These comments further support the MSRB's view that this appearance of *quid pro quo* corruption is not dependent on the particular line of business with which the contributor is associated.

[132] The draft amendments included two categories of ME officials: an ''official with dealer selection influence'' and an ''official with municipal advisor selection influence.'' As described above, the proposed rule change retains these categories and adds an additional category of ME official, an ''official of a municipal entity with investment adviser selection influence.'' *See* proposed Rule G–37(g)(xvi)(C).

Municipal Advisor Third-Party Solicitors

Under draft amended Rule G–37(b)(i)(A)(2) and (b)(i)(B)(2) (proposed paragraph (b)(i)(C)(2)), the triggering contributions made to an ME official by a municipal advisor third-party solicitor could trigger a ban on municipal securities business for a dealer that engaged the solicitor, or a ban on municipal advisory business for a municipal advisor that engaged the solicitor. SIFMA opposed these provisions, arguing that they would ''turn back a well-established precept that market participants do not control third parties.'' If not removed, SIFMA suggested, alternatively, that these provisions impose a ban only when the contribution is made to an ME official with selection influence over the type of business the solicitor was engaged to solicit.

The MSRB does not believe that the imposition of a two-year ban on a dealer client or municipal advisor client under these provisions as a result of political contributions made by an engaged municipal advisor third-party solicitor (or its MAP or a PAC controlled by either the municipal advisor third-party solicitor or an MAP of the municipal advisor third-party solicitor) is inappropriate or onerous. In order to achieve the purposes of the rule, the MSRB believes the two-year ban must be extended to apply to such contributions and has determined not to substantively amend the provision as suggested by SIFMA.

These provisions are narrowly tailored in that they would subject the regulated entity client to a ban on business with a municipal entity only when the regulated entity client engages a municipal advisor third-party solicitor to solicit a municipal entity for business on behalf of the regulated entity. A regulated entity may have a number of means available to help prevent its municipal advisor third-party solicitor from making triggering contributions, including as SIFMA identified, contractual provisions and the training of solicitor personnel. While such actions may not guarantee compliance with the proposed rule change, in such situations, regulated entity clients could possibly avail themselves of an automatic exemption from a ban on business under section (j), as amended by the proposed amendments to Rule G–37. Moreover, if a regulated entity becomes subject to a ban on business in such circumstances, and requests exemptive relief from the relevant agency under proposed Rule G–37(i), the extent to which, prior to the triggering contribution, the regulated entity developed and instituted procedures reasonably designed to ensure compliance with the rule, including procedures designed to ensure the compliance of any engaged municipal advisor third-party solicitor, would be among the factors that would be considered by the agency in determining whether to grant such exemptive relief.

The MSRB understands SIFMA's suggestion that a ban for a regulated entity client should apply only when the municipal advisor third-party solicitor's triggering contribution is made to an ME official with selection influence over the type of business the solicitor was engaged to solicit. However, as with the cross-ban provision, the goal of the municipal advisor third-party solicitor provisions is to address actual *quid pro quo* corruption or its appearance. Just as non-*de minimis* contributions from a person associated with a different line of business of a dealer-municipal advisory firm can present an appearance of *quid pro quo* corruption, so too do the contributions of a party specifically hired to solicit the municipal entity for business on behalf of the dealer-municipal advisor. Similar to the cross-ban, the arising of an appearance of *quid pro quo* corruption is not dependent on the particular line of business the solicitor was engaged to solicit.

Municipal Advisor Representative

SIFMA suggested that the MSRB narrow the scope of persons that could be a ''municipal advisor representative'' under draft amended Rule G–37(g)(iii) and thus could trigger a ban on applicable business or disclosure obligations for a municipal advisor. In SIFMA's view, only an associated person of a municipal advisor that is ''primarily engaged'' in municipal advisory activities should be a municipal advisor representative. By revising the term ''municipal advisor representative'' in this manner, SIFMA commented, the term would align with the relevant term for dealers and would move closer to the more narrowly defined group of persons subject to ''pay to play'' regulation under the IA Pay to Play Rule and the Swap Dealer Rule. SIFMA also commented that there is little risk that the political contributions of persons not ''primarily engaged in'' municipal advisory activities would create an appearance of *quid pro quo* corruption.

The MSRB has determined not to narrow the ''municipal advisor representative'' definition as suggested by SIFMA. Under the proposed rule change, the term ''municipal advisor representative'' would cross-reference the MSRB's ''municipal advisor representative'' definition under its municipal advisor professional qualification rules,[133] which itself is based on the scope of the definition of ''municipal advisor'' in the Dodd-Frank Act [134] and relevant rules and regulations thereunder. Under the SEC Final Rule, ''municipal advisor'' is to be broadly construed, and is not limited by the standard that a person must be ''primarily engaged in'' certain activities to be a municipal advisor.[135] Further, in granting authority to the Board to regulate municipal advisors, including regulation with respect to ''pay to play'' practices, Congress appears to have contemplated that all municipal advisors would be subject to ''pay to play'' regulation by the Board, regardless of the degree to which they engage in such municipal advisory activities.[136] Moreover, the MSRB's approach under the proposed rule change would create more consistency between defined terms in MSRB rules.

Other Constitutional Issues

Because they relate to an area of First Amendment protection, many commenters on the draft amendments framed their comments in light of their reading of the applicable constitutional standards. In addition to the policy matters discussed above, commenters expressed concerns as to the application of Rule G–37, as amended by the proposed amendments, to ''independent expenditures.'' They also urged the consideration of alternatives to the draft amendments and made various other comments, discussed below.

Independent Expenditures

Callcott and CCP stated that the Board should clarify that ''independent expenditures'' in support of ME officials are permitted under the proposed

[133] *See* Rule G–3(d)(i).

[134] *See* 15 U.S.C. 78*o*–4(e)(4).

[135] *See generally* SEC Final Rule; Order Adopting SEC Final Rule.

[136] As explained in the Request for Comment, the regulation of municipal advisors is, as the SEC has recognized, generally intended to address problems observed with the unregulated conduct of some municipal advisors, including ''pay to play'' practices. *See* Order Adopting SEC Final Rule, at 67469. ''Indeed, Congress determined to grant rulemaking authority over municipal advisors to the MSRB, in part, because it already 'has an existing, comprehensive set of rules on key issues such as pay-to-play . . . and that consistency would be important to ensure common standards.''' Request for Comment, at 2 (quoting Senate Report, at 149 (2010)).

amendments to conform to Supreme Court case law.[137]

The MSRB has previously stated in interpretive guidance under Rule G–37 that MFPs are free to, among other things, solicit votes or other assistance for an issuer official so long as the solicitation does not constitute a solicitation of or coordination of contributions for the issuer official.[138] In addition, in upholding the constitutionality of Rule G–37, the *Blount* court observed that ''municipal finance professionals are not in any way restricted from engaging in the vast majority of political activities, including making direct expenditures for the expression of their views, giving speeches, soliciting votes, writing books, or appearing at fundraising events.'' [139] In addition, the proposed amendments, like current Rule G–37, would generally not prohibit contributions to so-called ''super PACs'' or independent expenditure-only committees.[140] Like current Rule G–37, the proposed rule change would not impose any restriction on ''independent expenditures'' in support of ME officials.

Alternatives to the Draft Amendments

CCP stated that the MSRB should consider alternatives to the draft amendments, including tougher penalties, stronger investigative tools, whistleblower protections and providing exemptions for municipal advisory contracts that are put out for bid in a transparent way.

The MSRB has determined not to amend the proposed rule change in response to these comments. As part of its normal rulemaking process and consistent with its policy on economic analysis, the MSRB has considered alternatives to the proposed rule change; however, in each case, it determined that these alternatives would likely fail to achieve the same benefits as the proposed rule change or would achieve the same or substantially similar benefits at likely higher cost.[141] The MSRB is sensitive to the constitutional implications of Rule G–37 and believes that the proposed rule change strikes the appropriate balance between protecting constitutional freedoms and addressing *quid pro quo* corruption and the appearance thereof in the municipal securities market. For example, the MSRB has continued to improve its investigative tools to audit suspected ''pay to play'' activities involving dealers in the municipal market. However such tools alone would not be sufficient to meet the objectives of the proposed rule change because municipal advisors, in their capacity as such, are currently not subject to any ''pay to play'' rules. Improved tools to uncover *quid pro quo* corruption are meaningless without legal obligations designed to prohibit such practices. A similar rationale applies with respect to tougher penalties and whistleblower protections. Additionally, while the definition of ''municipal securities business'' set forth in current Rule G–37(g)(vii) and in proposed Rule G–37(g)(xii) effectively provides the exemptions CCP describes for certain municipal securities business conducted on a competitive bid basis, the MSRB understands that the nature of municipal advisory business does not currently lend itself to a competitive bid process in a manner comparable to which it is conducted for municipal securities business.

Other

Callcott interpreted the draft amendments to Rule G–37 to prohibit contributions to political parties, which would in Callcott's view have caused Rule G–37 to be unconstitutional. The proposed amendments to Rule G–37, like current Rule G–37, would not prohibit the making of political contributions to political parties. Rather, proposed amended section (c) would prohibit the solicitation and coordination of payments to a political party of a state or locality where the regulated entity is engaging or seeking to engage in business. Accordingly, the MSRB has determined not to further amend proposed section (c) in response to this comment.

CCP stated that draft amended section (e), the anti-circumvention provision, is insufficiently tailored under the First Amendment. The MSRB believes that this provision, which would be consistent with similar provisions in other federal ''pay to play'' regulations, including the IA Pay to Play Rule and the Swap Dealer Rule, would be narrowly tailored to prohibit regulated entities and their MFPs and MAPs from, directly or indirectly, doing any act that would result in a violation of sections (b) or (c) of Rule G–37. Accordingly, the MSRB has determined not to make any changes to section (e) in response to this comment.

CCP stated that a number of other terms or provisions under the draft amendments were vague or unclear. Specifically, CCP indicated that the draft amended MFP definition and draft MAP definition would make Rule G–37 less clear and difficult to determine what constitutes a sufficient ''control'' relationship for purposes of establishing vicarious liability for several categories of MFPs or MAPs. In addition, CCP expressed a belief that the draft amended definition for the term ''solicit'' was overly broad and vague because it would be difficult to determine when an ''indirect communication'' constituted a solicitation. CCP also noted that section (c) under draft amended Rule G–37 was overbroad because it would be difficult to determine whether a dealer or municipal advisor was ''seeking'' to engage in municipal securities business or municipal advisory business with a municipal entity or in a state or locality.

[137] The Federal Election Commission defines an ''independent expenditure'' generally as an expenditure ''for a communication expressly advocating the election or defeat of a clearly identified candidate that is not made in cooperation, consultation, or concert with, or at the request or suggestion of, a candidate, a candidate's authorized committee, or their agents, or a political party committee or its agents.'' 11 CFR 100.16(a).

[138] *See* Solicitation of Contributions, reprinted in *MSRB Rule Book* (May 21, 1999).

[139] *Blount,* 61 F.3d at 948; *see* Reminder of Obligations Under Rule G–37 on Political Contributions and Rule G–27 on Supervision When Sponsoring Meetings and Conferences Involving Issuer Officials, reprinted in *MSRB Rule Book* (March 26, 2007) at n. 1, quoting *Blount,* 61 F.3d at 948.

[140] However, consistent with current Rule G–37 and related interpretive guidance, regulated entities and their MFPs and MAPs would be prohibited from soliciting others (including affiliates of the regulated entity or any PACs) to make contributions to certain ME officials. Additionally, regulated entities and certain categories of MFPs and MAPs would be prohibited from soliciting others (including affiliates of the regulated entity or any PACs) to make contributions to certain ME officials. Further, contributions by a PAC controlled by the regulated entity or an MFP or MAP of the regulated entity to certain ME officials may result in a ban on municipal securities business or municipal advisory business with that municipal entity. Furthermore, regulated entities and their MFPs and MAPs would be prohibited from circumventing Rule G–37 by direct or indirect actions through any other persons or means, including, for example, using an affiliated PAC as a conduit for making a contribution to an ME official. *See* MSRB Guidance on Dealer-Affiliated Political Action Committees Under Rule G–37 (December 12, 2010).

[141] For example, the MSRB considered not requiring a nexus between the influence that may be exercised by an ME official who receives a contribution and the business in which the regulated entity is engaged or is seeking to engage. A broader set of potential ban-triggering events would likely increase costs and may negatively impact competition without significantly improving market integrity or merit-based competition. The MSRB also considered not allowing an orderly transition period for pre-existing non-issue-specific contractual obligations following a ban on business. This alternative would risk imposing significant costs on municipal entities and, because the ban-triggering event would by definition occur after a firm had been selected, does not appear to address the identified needs better than the proposed rule change. The MSRB also considered, but ultimately rejected for the reasons stated herein, modeling the ''pay to play'' regime for municipal advisors on other ''pay to play'' regimes in the financial services market in favor of the approach taken in the proposed rule change.

The MSRB disagrees with each of these assertions. The proposed amendments set forth, for municipal advisors generally, based upon their activities, functions and positions, categories that are analogous and substantially similar to those used to describe various types of MFPs under the current rule. The proposed amendments to the definition of municipal finance professional are non-substantive (*i.e.,* assigning names to the categories), and, thus would have no impact on an analysis or determination regarding control relationships for purposes of establishing vicarious liability among various MFPs, and, by extension, MAPs. Further, as discussed *supra,* Rule G–37, including section (c), previously withstood constitutional scrutiny in *Blount,* and the proposed amendments simply would extend the core of section (c) to municipal advisors. In addition, while the ''solicit'' definition would be amended under the proposed rule change, the proposed amended definition in subsection (g)(xix) would be consistent with the current definition of ''solicit'' that it would replace.[142] Both the proposed and current definitions of ''solicit'' incorporate the ''indirect communication'' language. Moreover, the MSRB previously issued interpretive guidance regarding the term ''solicitation'' for purposes of Rule G–37.[143] As discussed *supra,* the MSRB intends to extend the existing interpretive guidance on Rule G–37 for dealers to municipal advisors on analogous issues. Thus, the MSRB believes at this time that there is sufficient guidance regarding these provisions and terms.

Modification of the Two-Year Ban

Draft amended Rule G–37(b)(i)(E) would provide for a modification of the ending of the two-year ban on applicable business under certain circumstances when business with the municipal entity is ongoing at the time of the triggering contribution. SIFMA stated that this modification should be tailored to apply only to any municipal entity with which a regulated entity is engaged in business at the time of the contribution. SIFMA explained that, according to its reading of the modified two-year ban, in cases where the recipient of a triggering contribution is an ME official of *multiple* municipal entities, a regulated entity would be prohibited from engaging in applicable business with each municipal entity for the extended period of time, even if the regulated entity was engaged in ongoing business with only one of the municipal entities at the time of the contribution.

To provide additional clarity, the MSRB has amended this provision and consolidated it with the provisions pertaining to the orderly transition period in a single paragraph. Under paragraph (b)(i)(E) in the proposed rule change, a triggered ban on applicable business with a given municipal entity will be extended by the duration of the orderly transition period described in proposed Rule G–37(b)(i)(E). The length of a ban on applicable business for one municipal entity with which a regulated entity is banned from engaging in applicable business is unaffected by the length of the ban on applicable business with another municipal entity. This is the case even where the ban on applicable business with both municipal entities stemmed from the same contribution to an ME official with the ability to influence the awarding of business to both municipal entities.[144]

Recordkeeping and Reporting

Duplicate Books and Records

BDA and Sanchez sought clarification as to whether the draft amendments would require dealer-municipal advisors to keep duplicate books and records. BDA specifically expressed concern that the draft amendments would require employees who act as both a municipal advisor and serve as bankers in an underwriter capacity to keep dual records and disclosures. In addition, Sanchez suggested that Rules G–8 and G–9 should be revised to not require separate maintenance of information that is included on Form G–37 and to make clear that the availability of Form G–37 on EMMA would satisfy the maintenance requirement.

The proposed amendments would not require a dealer-municipal advisor to make and keep dual records and disclosures. The MSRB therefore has determined not to amend Rules G–8 and G–9 as suggested by commenters. In addition, as noted in the Request for Comment, dealer-municipal advisors could make all required disclosures on a single Form G–37. Additionally, the proposed amendments to Rules G–8 and G–9 would not prohibit dealer-municipal advisors from making and keeping a single set of the records that would be required under the proposed amendments. Rather, the proposed amendments would provide dealer-municipal advisors with the flexibility to consolidate such records or to keep such records separate as long as they are kept in compliance with all of the terms of Rules G–8 and G–9. If a dealer-municipal advisor were to elect to keep a consolidated set of such records, such records would need to clearly identify whether an MAP or MFP is solely an MAP, solely an MFP, or both.

The MSRB also has determined, at this time, not to further revise Form G–37 and Rules G–8 and G–9 to require the disclosure of much of the information required to be kept under those rules in lieu of separately maintaining such records. Those data are necessary for examiners to examine for compliance with the provisions of Rule G–37 and the MSRB believes that requiring the public disclosure of such information would likely unjustifiably add to, rather than reduce, the compliance burden for regulated entities.

Books and Records When No Contributions Are Made

Castle and WMFS both expressed support for regulation to curb ''pay to play'' practices, but stated that there should be no books, records or filing requirements for municipal advisors that do not make political contributions. To support this approach, WMFS cited the requirement under the Dodd-Frank Act that the Board not impose an unnecessary burden on small municipal advisors.[145] The Public Interest Groups recommended that the MSRB substantially broaden the recordkeeping that would be required under the proposed amendments to require regulated entities to disclose all political contributions made by any affiliate and to itemize these contributions for comparison to relevant underwritings.

The MSRB believes that the information that would be required to be reported to the Board on Form G–37, even in the absence of any reportable contributions for the applicable reporting period, is important to

[142] *See* discussion of proposed definition of ''solicit'' in ''Municipal Advisor Third-Party Solicitors'' and n. 39, *supra.* The current definition of ''solicit,'' which would be deleted, provides: ''Except as used in section (c), the term 'solicit' means the taking of any action that would constitute a solicitation as defined in rule G–38(b)(i).'' Rule G–37(g)(ix). Rule G–38(b)(i) provides: ''The term 'solicitation' means a direct or indirect communication by any person with an issuer for the purpose of obtaining or retaining municipal securities business.''

[143] *See* MSRB Interpretive Notice on the Definition of Solicitation Under Rules G–37 and G–38 (June 8, 2006).

[144] For example, if a ban triggering contribution is made to an ME official of three municipal entities, and the regulated entity avails itself of an orderly transition period spanning one week for one municipal entity and two weeks for the second municipal entity, but does not avail itself of an orderly transition period for the third municipal entity, its ban with the first municipal entity is extended by one week, its ban with the second municipal entity is extended by two weeks, and its ban with the third municipal entity is not extended.

[145] *See* 15 U.S.C. 78*o*–4(b)(2)(L)(iv).

evaluate compliance with the proposed amended rule and to facilitate public scrutiny of a regulated entity's political contributions (even if made in a different reporting period) and applicable business. The MSRB therefore has determined not to propose the amendments suggested by these commenters. The MSRB believes that the limited nature of the information required to be reported when a regulated entity does not have any reportable contributions and the available relief from any reporting obligations in certain circumstances under the proposed amendments to Rule G–37(e)(ii) sufficiently accommodate small municipal advisors. Similarly, the records that a municipal advisor would be required to make and keep current under the proposed amendments to Rules G–8 and G–9 are necessary to examine municipal advisors for compliance with Rule G–37, as amended by the proposed amendments, and would generally be limited for a municipal advisor that does not make any political contributions. These records would likely also be limited for a small municipal advisor, which necessarily will have fewer MAPs for which it would be required to keep records.

The MSRB seeks to appropriately balance the burden of complying with the proposed rule change's public reporting requirements with the benefit to the public of such disclosure. Moreover, the MSRB is cognizant of the constitutional implications of the proposed rule change, and seeks to narrowly tailor the rule to achieve its stated objectives. At this juncture, the MSRB does not believe that the additional public disclosure suggested by The Public Interest Groups is warranted for the proposed rule change to achieve its objectives.

Paper Submissions

Sanchez suggested that the MSRB should enhance the searchability of Form G–37 submitted to the Board in furtherance of the Board's stated objective to promote public scrutiny of the contributions made by regulated entities. Sanchez also suggested that the MSRB not allow the submission of paper versions of Form G–37.

The MSRB agrees and proposed subsection (e)(iv) of Rule G–37 would require all Form G–37 submissions to be submitted to the Board in electronic form, thereby eliminating the option to submit paper versions of these forms. The MSRB also plans to set forth in the *Instructions for Forms G–37, G–37x and G–38t,* referenced in subsection (e)(iv) of the proposed amendments to Rule G–37 a requirement that all electronic submissions be in word-searchable portable document format (PDF). All regulated entities have the ability to access the MSRB's electronic submission portal, through which electronic Form G–37 and Form G–37x are submitted. Further, given the significant technological advances since the MSRB first required the submission of Form G–37, the now widespread availability of computers and PDF software, and low percentage of Forms G–37 the MSRB currently receives in paper form, the MSRB believes the burden as a consequence of no longer accepting paper submissions will be relatively low.

Miscellaneous

ACEC expressed the view that the ''look-back'' in the draft amendments would create a potential conflict with existing employment law which, ACEC stated, does not favorably view asking an applicant questions during the hiring process that are not directly related to the job. In addition, ACEC stated that the MSRB should provide guidance as to what constitutes an indirect contribution to a trade association PAC. Regarding PACs, The Public Interest Groups expressed concern regarding political giving by PACs that may or may not be controlled by a dealer or an MFP of the dealer. It stated that the current disclosure and reporting apparatus does not provide the appropriate deterrent to prevent circumvention of Rule G–37 through the use of PACs.

While the MSRB is sensitive to the fact that regulated entities may be subject to many regulatory schemes, it does not believe that the look-back, which has existed under Rule G–37 for approximately two decades, would be inconsistent with other areas of law. The proposed rule change merely extends this same concept to municipal advisors. Similarly, the MSRB intends to extend the existing interpretive guidance under Rule G–37 for dealers to municipal advisors on analogous issues. The MSRB believes at this time that there is sufficient guidance regarding contributions to and through PACs as well as circumvention of Rule G–37.

WMFS stated that the MSRB should consider prohibiting the making of contributions to bond ballot campaigns. While the MSRB is sensitive to concerns about bond ballot contributions, the established objective of this rulemaking initiative is to extend the principles embodied in Rule G–37 to municipal advisors, with appropriate modifications to take into account the differences between the regulated entities and the existence of municipal advisor third-party solicitors and dealer-municipal advisors. While bond ballot contributions are not the subject of this initiative, the MSRB continues to review disclosures regarding contributions made to bond ballot campaigns and will separately make any determination whether to engage in further rulemaking in this area.[146]

ACEC requested that the MSRB clarify whether the *de minimis* exclusion would apply separately to primary and general elections. The Board has previously stated that, if an issuer official is involved in a primary election prior to the general election, an MFP who is entitled to vote for such official may contribute up to $250 for the primary election and $250 for the general election to the official.[147] As noted, the MSRB intends all existing interpretive guidance for dealers to apply to the analogous interpretive issues for municipal advisors. Thus, under the proposed rule change, the *de minimis* exclusion would apply separately to primary and general elections.

ACEC also urged the MSRB to reserve action on the proposed rule change until the Commission has fully clarified the definition of municipal advisory services. The MSRB has determined not to delay this rulemaking initiative. Since July 1, 2014, all municipal advisors, including municipal advisors that are also engineers and do not qualify for an exclusion or exemption under the SEC Final Rule, have been required to comply with the provisions of the SEC Final Rule. They are also subject to a number of MSRB rules, such as Rule G–17, regarding fair dealing, Rule G–44, regarding supervisory and

[146] Since February 1, 2010, the MSRB has required disclosure, under Rule G–37, of non-*de minimis* contributions to bond ballot campaigns made by dealers and certain of their associated persons. In 2013, the MSRB amended Rule G–37 to require the disclosure of additional information related to the contributions made by dealers and certain of their associated persons to bond ballot campaigns and the municipal securities business engaged in by dealers resulting from voter approval of the bond ballot measure to which such contributions relate. The proposed rule change would extend these disclosure provisions to municipal advisors. In connection with the 2013 rulemaking initiative, the MSRB stated that the more detailed disclosures will help inform the Board whether further action regarding bond ballot campaign contributions is warranted, up to and including a corresponding ban on engaging in municipal securities business as a result of certain contributions. *See* MSRB Notice 2013–09, SEC Approves Amendments to Require the Public Disclosure of Additional Information Related to Dealer Contributions to Bond Ballot Campaigns Under MSRB Rules G–37 and G–8 (April 1, 2013).

[147] *See* MSRB Rule G–37 Interpretive Notice—Application of Rule G–37 to Presidential Campaigns of Issuer Officials (March 23, 1999).

compliance obligations, and Rule G–3, regarding registration and professional qualification requirements. At this juncture, all municipal advisors should be registered as such, and in compliance with applicable rules. Accordingly, the MSRB has determined not to reserve action on this rulemaking initiative.

Anonymous stated that registered investment advisers that are also municipal advisors should be exempt from the proposed rule change because, in its view, such municipal advisors are already subject to stringent political contribution compliance and recordkeeping requirements. The MSRB has determined not to exempt such municipal advisors from the proposed rule change. As discussed *supra,* the MSRB is sensitive to the effect of differing regulation for the limited number of dealers and municipal advisors that also operate in the investment advisory market or the swap market. However, the Board does not believe that municipal advisors that also act as investment advisers should be subject to different regulation than their non-investment adviser municipal advisor counterparts.

Lastly, ACEC stated that some commercial entities not primarily in the business of providing advisory services related to municipal securities may, nonetheless, be engaged in activities that are regulated (*e.g.,* engineers). It noted that for the larger among these firms, implementing a compliance regime consistent with the proposed amendments would be challenging and that the MSRB should consider these administrative costs in the context of this rulemaking initiative. As described *supra,* the MSRB has considered the impact of the proposed rule change on all municipal advisors, including small municipal advisors and municipal advisors that have not previously been subject to federal financial regulation, and continues to believe that the proposed rule change is necessary to address *quid pro quo* corruption or the appearance thereof in the municipal market.

Economic Analysis

There were no comments received that were specific to the preliminary economic analysis presented in the Request for Comment nor did commenters provide any data to support an improved quantification of benefits and costs of the rule. Comments about the compliance burdens of specific elements of the draft amendments are discussed above.

Implementation Period and Transitional Effect

SIFMA requested an implementation period of no less than six months from the effective date of the proposed rule change.

In response to this comment, the MSRB has revised section (h) of the draft amendments to Rule G–37 to provide that the prohibitions in proposed amended section (b) of Rule G–37 (regarding the ban on business) would only arise from contributions made on or after an effective date to be announced by the MSRB in a regulatory notice published no later than two months following SEC approval of the proposed rule change. Such effective date shall be no sooner than six months following publication of the regulatory notice and no later than one year following SEC approval of the proposed rule change. This lengthening of the implementation period should mitigate compliance costs and provide sufficient time for municipal advisors to identify the MAPs and MFPs that will be subject to the proposed rule change and for dealers and municipal advisors to modify existing, or adopt new, relevant policies or procedures.

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

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period of up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, 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 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.* Please include File Number SR–MSRB–2015–14 on the subject line.

Paper Comments

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

All submissions should refer to File Number SR–MSRB–2015–14. 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 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the MSRB. 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–2015–14 and should be submitted on or before January 20, 2016.

For the Commission, pursuant to delegated authority.[148]

Brent J. Fields,

Secretary.

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[148] 17 CFR 200.30–3(a)(12).