THE BOND BUYER

SEC, MSRB provide guidance on muni advisor exemptive order

By

Sarah Wynn

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The Securities and Exchange Commission’s temporary exemption to allow municipal advisors to arrange certain private placement deals is indeed narrow and conditions included in the order will discourage retail access to the market, regulators say.

In a discussion hosted by the SEC Tuesday afternoon, regulators answered questions on how they decided on narrowed conditions for an order to allow MAs to arrange those deals without registering as broker-dealers. They also discussed how Municipal Securities Rulemaking Board rules apply. The temporary exemption was announced in June and will last until Dec. 31, 2020.

“The conditions are intended to discourage retail access to this market,” said Kelly Shoop, special counsel in the SEC’s Division of Trading and Markets. “Our understanding of direct placement has typically been a bank will purchase it and hold it for the duration. There have been concerns raised over time about retail access to this market. Some of the conditions are really designed to get at that.”

Some of the conditions applied to the temporary exemption included capping the size of the direct placement deal at $20 million, and that the placement must be issued in denominations of $100,000 or more.

SEC staff also commented on a statement made by Bond Dealers of America that based on 2019 issuance patterns, a $20 million dollar threshold would make up about 72% of municipal issuances and is therefore not "narrow."

Dealers have long opposed allowing muni advisors who are not broker-dealers to arrange private placements, viewing such activity as explicitly within the responsibility of a broker-dealer placement agent.

While Shoop acknowledged that those issuances were more than 70% of public issuances, they did not represent nearly so large a chunk of the market by volume

“We understand that those deals amounted to only about 13% of the total par volume issued," Shoop said. "Through that lens, we think this is a narrow slice of the market.”

Under the temporary exemption, MAs will need to amend their supervisory procedures if they plan to partake of the temporary exemption, said Gail Marshall, MSRB chief compliance officer.

“They would need to determine if their supervisory procedures as written covered this activity in its entirety,” Marshall said. “It’s likely that they do not because of the additional solicitation activity that is permitted under the temporary order and they would need to amend their WSP’s (written supervisory procedures) to reflect that.”

Municipal advisors will need to amend their supervisory procedures, said Gail Marshall, MSRB chief compliance officer.

That could be in the form of an appendix to the document itself, Marshall added. MAs will also need to amend client contracts to account for solicitation activity under the temporary exemption.

The National Association of Municipal Advisors echoed the requirements, saying it was important for MAs to comply with MSRB rules while engaging in the temporary exemption.

“It will be important for MAs conducting business under the parameters of the order to comply with MSRB rules, including updating their WSPs, documentation requirements, and when needed agreements/contracts with their clients, as was discussed on the webinar,” Susan Gaffney, NAMA executive director wrote in an email.

Marshall also said during the discussion that MAs should not be charging an extra placement fee on top of their MA fees.

“MAs are not engaging in private placement activities, so I hope that they’re not going to assess an additional fee for placement agent activity because they’re not engaging in that,” Marshall said.

If MAs are contemplating fee structures in light of the temporary exemption, they should look to MSRB Rule G-42, the core muni advisor conduct rule and what it says on disclosures of conflicts of interest.

BDA said some of the MAs requirements under the temporary exemption make it less attractive to use.

“For example, MAs who want to use the exemption will have to update their supervisory plans; they'll need to amend their client contracts to account for solicitation activity; they'll have to make disclosures and representations to all potential investors, not just the one that buys the deal; and MAs can't charge a placement fee, among others,” said Michael Decker, BDA senior vice president of policy and research. “None of those are deal-killers, but taken together, the compliance burden for MAs using the exemption is higher than I thought.”

The Securities Industry and Financial Markets Association said in an email that the exemption is likely to hurt smaller broker-dealers that act as placement agents, and urged that the SEC make public the uses of the exemption. The order requires MAs to report uses of the exemption to the SEC, but SEC Chair Jay Clayton has said he is not sure if the SEC will make that information public.

SEC regulators also confirmed during the webinar that under the temporary exemption, placement agents would not be cut out of the direct placement deal.

“There seems to be a lot of confusion in this space about whether exemptive relief for MAs, whether temporary or permanent would preclude the engagement of a placement agent — effectively whether placement agents are getting cut out

of direct placements through this exemptive relief," Shoop said. "The answer is no."

Sarah Wynn

Reporter

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