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May 5, 2005



Mr. Jonathan G. Katz  
Secretary  
Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

RE: File Number SR-MSRB-2005-04; Relating to Notice of Filing of Proposed Rule Change Relating to Solicitation of Municipal Securities Business Under Municipal Securities Rulemaking Board's Rule G-38

Dear Mr. Katz:

The Bond Market Association ("Association")<sup>1</sup> appreciates this opportunity to comment on the proposed amendment to Rule G-38, which the Municipal Securities Rulemaking Board ("MSRB") submitted to the Securities and Exchange Commission ("SEC") on March 17, 2005.<sup>2</sup> This proposed amendment prohibits a broker-dealer from paying anyone, other than the broker-dealer's or an affiliated company's partner, director, officer or employee, for soliciting municipal securities business on behalf of the broker-dealer, thus eliminating the use of any outside Consultants to solicit municipal securities business.

The MSRB submitted this proposed amendment to the SEC after issuing, and receiving comments from the industry (including the Association), on two prior drafts of the amendment.<sup>3</sup> Indeed, applying the "associated person"

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<sup>1</sup> The Association represents securities firms and banks that underwrite, trade and sell debt securities, both domestically and internationally. The Association's Member firms collectively represent in excess of 95% of the initial distribution and secondary market trading of municipal bonds, corporate bonds, mortgage and other asset-backed securities and other fixed income securities. More information about the Association is available on its website [www.bondmarkets.com](http://www.bondmarkets.com).

<sup>2</sup> 70 Fed. Reg. 20,782 (April 21, 2005).

<sup>3</sup> MSRB Notices 2004-11 (April 5, 2004), 2004-32 (September 29, 2004).

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standard proposed in the prior drafts was fraught with difficulty given its lack of clarity and broad range of implications under other securities rules. We appreciate that the Association has been able to constructively participate in this process and, while the MSRB did not accept our alternative methods of addressing the issue of consultants, we credit the MSRB for coming up with a clear and simple rule. However, there are certain portions of the proposed draft that require further clarification or modification, as described below.

**1. The Requirements for Making Transition Payments Should Be Changed**

Under the current wording of the transition provision, a broker-dealer may pay an outside Consultant after the effective date of this amendment (*i.e.*, the date that the SEC approves the amendment) only if (1) it is for services provided prior to the effective date; and (2) the broker-dealer has been selected by the issuer for the municipal securities deal prior to the effective date.

However, as a practical matter, broker-dealers will have no meaningful notice as to when the SEC will approve this amendment and thus will not have an opportunity to effectively close out their relationship with Consultants under the current provision. For example, a broker-dealer will be prohibited from paying Consultants compensation, which they have legitimately earned, and be forced to renege on its contractual obligations simply because the broker-dealer has not yet been selected for the deal. This is particularly troubling if the compensation in question is the mere reimbursement of Consultants for expenses they already incurred. Another problem arises in those instances where a broker dealer is part of a pool of selected underwriters, and rotated to a senior manager position periodically. The dealer has been "selected" but the actual selection for a lead position (which triggers compensation due to a consultant) may not occur until some point in the future. Moreover, to the extent that a Consultant is paid on a retainer basis (as opposed to a success fee arrangement), they earn their compensation regardless of whether the broker-dealer is selected and moneys may still be contractually due for time worked but not paid as of the effective date.

Thus, the transition provision should be modified to eliminate the artificial requirement that the broker-dealer be selected for a deal prior to the effective date of this amendment. It is sufficient to require a broker-dealer to make payments solely for services provided prior to the effective date of the amendment. However, to relieve any concerns that the payments may not be limited to such purpose, the MSRB could require payments to be made during a thirty (30) day window after the effective date. Please note that the detailed reporting requirement



on proposed Form G-38t will also ensure that these transition payments are beyond reproach.

**2. The Definition of Solicitation Should Be Clarified**

The amendment retains the current definition under Rule G-38 as to what constitutes a “solicitation,” i.e., a direct or indirect communication with an issuer for the purpose of obtaining or retaining municipal securities business. However, the amendment does not retain the language in the current rule, which exempts those who are paid solely for the actual provision of legal, accounting, engineering or legislative lobbying services in connection with municipal securities business and do not otherwise solicit such business.<sup>4</sup> These are essential and, in many cases, necessary services to effectively engage in municipal securities business. Moreover, these services are usually provided by outside persons (non-employees) and are not geared toward influencing an issuer’s decision to select a broker-dealer for municipal securities business.

In its comments to the MSRB, the Association pointed out the omission of the above exemption and requested that the amendment be modified to include it. The MSRB responded by informally stating in a Notice that it believed that the above services would still be exempt under the amendment.<sup>5</sup> However, given the importance of this issue,<sup>6</sup> we request that the exemptions for these vital services be expressly included in the Rule.

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<sup>4</sup> Rule G-38(a)(i)(B). The exemption for legislative lobbying services was created by the MSRB through formal Rule G-38 interpretation. Q&A 5 (February 28, 1996).

<sup>5</sup> MSRB Notice 2004-32 (September 29, 2004).

<sup>6</sup> In fact, the MSRB went as far as to say that a solicitation occurs if a person does anything that has the effect of making a broker-dealer more attractive to an issuer. G-37 Q&A IV.10 (December 7, 1994). Does this mean that broker-dealers may no longer have underwriter’s counsel under the amendment given that good legal representation could make the firm more appealing?

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**3. The Definition of Affiliated Employees**

The amendment prohibits a broker-dealer from paying anyone other than an "employee" of the broker-dealer or an affiliate for soliciting municipal securities business. There are, however, registered representatives who work for a broker-dealer or an affiliate but do so as independent contractors, not as employees. As registered representatives of a broker-dealer these individuals are subject to the same supervision, compliance and regulatory requirements as employees, but are treated as independent contractors for compensation and/or economic reasons. In fact, as NASD licensed representatives of the broker-dealer these independent contractors are also subject to the full array of MSRB rules. Given that such individuals are subject to, among other things, the broker-dealer's supervision as well as the fair practice and professionalism standards under MSRB rules, the amendment should be modified to also permit a broker-dealer, to pay any licensed representative of that broker dealer or an affiliate to solicit municipal securities business.

We look forward to discussing these issues further with the SEC staff, and appreciate your attention to our comments. Please contact the undersigned at 646.637.9218 or via e-mail at [Lhotchkiss@bondmarkets.com](mailto:Lhotchkiss@bondmarkets.com) with any questions that you might have.

Sincerely,

Lynnette Kelly Hotchkiss  
Senior Vice President and  
Associate General Counsel

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cc: ***Securities and Exchange Commission***

The Honorable William H. Donaldson, Chairman  
The Honorable Cynthia A. Glassman, Commissioner  
The Honorable Harvey J. Goldschmid, Commissioner  
The Honorable Paul S. Atkins, Commissioner  
The Honorable Roel C. Campos, Commissioner  
Giovanni P. Prezioso, General Counsel, Office of the General Counsel  
Annette L. Nazareth, Director, Division of Market Regulation  
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***The Bond Market Association***

Executive Committee, Municipal Securities Division  
Legal Advisory Committee, Municipal Securities Division  
Policy Committee, Municipal Securities Division  
Consultants Task Force, Municipal Securities Division  
Regional Advisory Committee