

# Annual G-42 Training and Regulatory Update



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# Speaker

Ed Fierro

Senior Counsel  
Bracewell

Former Senior Counsel  
Office of Municipal Securities  
Securities and Exchange Commission

# Topics

- MSRB Rule G-42 Overview
- Rule G-42 and SEC's MA Rule
- New Rules
- Special Topics
  - Off Channel Communications
  - Pricing and MAs
  - Disclosure and MAs
- Upcoming Issues
- NAMA Resources

# Standards of Conduct

- A. Duty of Care (Applies to all Client Types)
  - 1. Must possess degree of knowledge and expertise necessary to provide informed advice
  - 2. **Must make reasonable inquiry to the facts**
    - a. **Client assumptions**
    - b. **Transaction origins**
  - 3. Must undertake reasonable investigation to determine that recommendation is not based on materially inaccurate or incomplete information
  - 4. Must have reasonable basis for:
    - a. Providing advice to client
    - b. Representations made in certifications of the municipal advisor
    - c. **Any information provided to client or others in connection with preparation of OS where the MA is advising**

# Standards of Conduct

- B. Duty of Loyalty (Applies to Municipal Entity Clients)
  - 1. Deal honestly and with utmost good faith
  - 2. **Act in the client's best interests without regard to the financial or other interests of MA**
    - a. **having "difficult" conversations with client**
  - 3. Conflicts of interest are managed or mitigated
  
- C. Duty to Municipal Entity vs. Obligated Person

# Disclosures/Conflicts of Interest

- G-42 (b) Disclosures of Material Conflicts of Interest **Prior to or Upon Engaging in MA Activities** Provided to Client or Potential Client in Writing
  - A. **Conflicts arising from compensation for MA activities where payment is contingent on the size of closing of transaction**
  - B. Affiliate of the MA provides advice or services related to MA activities for a client
  - C. Payments made by MA, directly or indirectly, to obtain or retain an engagement
  - D. Payments to MA from third party
  - E. Fee-splitting arrangements (other than with UW which are prohibited)

# Disclosures/Conflicts of Interest

- G-42 (b) Disclosures of Material Conflicts of Interest Prior to or Upon Engaging in MA Activities Provided to Client or Potential Client in Writing
  - F. Other or potential conflicts of interest
  - G. **Statement of how conflicts will be mitigated**
  - H. **Statement of no material conflicts of interest exist**
  - I. Information of legal or disciplinary events and reference to Forms MA/MA-I

# MA Relationship with Client

- G-42 (c) Documentation of MA Relationship in Writing and Sent to Client Upon or Promptly After Establishment of MA Relationship, Must Include:
  - A. Form and basis of compensation for MA activities
  - B. Disclosures noted in G-42 (b) (conflicts and legal/disciplinary events)
  - C. Legal and Disciplinary events per Form MA and MA-I and date of last material changes to Forms
  - D. **Scope of MA activities to be performed and any limitations on the scope of engagement**
    - 1. **Co and Sub MAs**
  - E. Date, triggering event or means for termination of the relationship
  - F. Terms, if any, related to withdrawal from the MA relationship



# Recommendations

- Recommendations and Review of Recommendations of Other Parties

- A. Have reasonable basis to believe the recommendation for municipal securities transaction/product is **suitable to client**
  1. BIG R/little r recommendations
  2. Suitability must be based on numerous factors including client's:
    - a. **Financial situation and needs**
    - b. Objectives
    - c. Tax status
    - d. **Risk tolerance**
    - e. Liquidity needs

# Recommendations

- Recommendations and Review of Recommendations of other Parties
  - 2. Suitability Must be Based on Numerous Factors Including client's:
    - f. Experience with municipal securities transaction/product,
    - g. Financial capacity to withstand changes in market conditions during term of product/length of bonds
    - h. Any other material information known by MA about client and the transaction/product after reasonable inquiry.

# Recommendations

- Recommendations and Review of Recommendations of other Parties
  - B. If reviewing recommendations of others is part of scope of services, **MA must determine through reasonable diligence whether the transaction is suitable for the client**
  - C. MA must inform client:
    1. MA's evaluation of material risks, potential benefits, structure and other characteristics of municipal securities transaction/product
    2. Basis for which the MA believes that the recommended transaction/product is or is not suitable
    3. Whether MA has investigated or considered other reasonably feasible alternatives to the recommendation that might also serve the client's objectives

# Know Your Client

- A. MA must use reasonable diligence in regard to maintaining the MA relationship
- B. **MA must know and retain essential facts concerning the client and authority of persons acting on behalf of client**
- C. MA must **effectively service the relationship with client**
- D. MA must act in accordance with special directions from client
- E. MA must comply with applicable laws, regulations and rules

# Prohibitions

- A. Receiving excessive compensation for MA services
- B. Delivering a materially inaccurate invoice for fees or expenses
- C. Making **representations or submitting information that the MA knows or should know is materially false or misleading due to omission of fact**
- D. Making or participating in fee-splitting arrangements with underwriters, and any undisclosed fee-splitting arrangements with providers of investments or services to client

# Prohibitions

- E. Making payments for obtaining or retaining an engagement to perform MA activities outside of payments for permitted solicitation purposes.
- F. Principal transaction with the client that is related to the transaction where the MA is providing advice

# Documentation and G-42

- Documents - External
  - Disclosure of Conflicts
  - Engagement Letters/Client Contracts
  - Scope of Services**
    - **What is included**
    - **What is excluded**
    - **Sub and Co**
  - Recommendations
  - Review of Information from Other Parties

# Documentation and G-42

- MSRB Rules G-8 and 9
- Documents - Internal
  - Recommendations
    - Suitability
    - Know Your Client
    - **Other Notes to File**
  - Transaction
    - Correspondence
    - Meetings
    - “Notes”
  - WSP
    - Process
    - Documenting the Process
- NAMA G-42 Checklist



# Supervision and G-42

- MSRB Rule G-44
- Supervisory Systems: How to Review and Update
- How to Identify Conflicts of Interest
- How to Monitor that Contracts and Disclosures are Being Distributed
- How to Ensure MAs Have Sufficient Knowledge
- **How to Supervise MA Communications**
- Supervising Remotely

# Special Topic: Rule G-42 and SEC MA Rule

- Recommendation/Rule G-42
- **Advice/MA Rule**

# Special Topic: MAs and Pricing

- Inherent or specific MA duty?
  - What is in the written scope of work?
  - What is performed?
  - What is client expecting?**
- **Focus on MA obtaining “independent” information in pre pricing and pricing tasks**
- **Other MA responsibilities related to pricing**
  - Method of sale**
  - Post closing monitoring/trading**
- Documentation standards “showing your work”
  - WSP
  - Transaction

# Special Topic: Off Channel Communications

- MA Rule – “all written communications”
  - *§240.15Ba (1) Originals or copies of all written communications received, and originals or copies of all written communications sent, by such municipal advisor (including inter-office memoranda and communications) relating to municipal advisory activities, regardless of the format of such communications;*
- Understand scope of off channel communications: texting, personal email, business system chat features, social media chat features, communications apps
- Have Firm policy prohibiting use of off channel communications for MA activity
- Have method to capture off channel communications into firm’s recordkeeping system
- Have documented training/reminders that are Firm specific
- Conduct electronic communication review as part of annual compliance review
- Determine Firm risk of off channel communication use
- Have supervisory procedures in place regarding off channel communications
- Consider implementing quarterly attestations
- Determine whether other actions are needed
  - Capturing off channel communications

# New Rulemaking - 2023

- Rule A-12
  - Primary Regulatory Contact must be a Firm Principal
- Rule G-3
  - Under certain conditions, 3-year grace period before taking S50
- Rule G-40
  - Use of testimonials in advertisements with appropriate disclaimers and parameters
  - NAMA recommends NOT utilizing PAID testimonials
- Rule G-46 – Solicitor MA
  - **Could a MA engage in solicitor MA activity, unintendedly?**

# Exams Focus

- Fiduciary Duty and Pricing
- MSRB Rules and SEC MA Rule
- Off Channel Communications
- Registration and Forms
- Continuing Education
- Testimonials
- Information on Firm web site
- Supervision

# Regulatory Reminders

- WSP Review
- Form MA Annual Update
  - **Is Solicitor MA box checked?**
- Form MA-I filings
  - **MA outside activities**
- A-12 Affirmations (**primary regulatory contact = CCO**)
- MSRB Fees (**\$100 per MA increase/check your # of MAs**)
- G-44 CEO Certification
- G-3 Continuing Education Review and Implementation
  - **Annual needs assessment**
  - **What are you committing to?**

# Other Focus Areas

- Addressing MA and non-MA Services
- MAs and Issuer Disclosure Work
- Solicitor MAs
- Recordkeeping and Supervisory Procedures
- Focus on Continuing Education



# NAMA Resources

- NAMA Compliance Resources

- <https://nama2.memberclicks.net/nama-compliance-resources>
- NAMA Compliance Resource and Webinar Recording on Testimonials
  - NAMA Resource – Using Testimonials in Advertisements
    - <https://nama2.memberclicks.net/assets/updatedadvertisingresourceJune2023.pdf>
  - NAMA Webinar Recording and Slide Deck
    - [https://nama2.memberclicks.net/index.php?option=com\\_jevents&task=icalrepeat.detail&evid=103&Itemid=114&year=2023&month=06&day=20&title=nama-webinar-rule-g-40using-testimonials&uid=9ad273f68cf2f24f8a01999797c1e073](https://nama2.memberclicks.net/index.php?option=com_jevents&task=icalrepeat.detail&evid=103&Itemid=114&year=2023&month=06&day=20&title=nama-webinar-rule-g-40using-testimonials&uid=9ad273f68cf2f24f8a01999797c1e073)
- NAMA Compliance Resource and Webinar Recording on Off Channel Communications
  - NAMA Resource –  
<https://nama2.memberclicks.net/assets/recordkeepingguidancenov2023FINAL.pdf>
  - NAMA Webinar Recording and Slide Deck -  
[https://nama2.memberclicks.net/index.php?option=com\\_jevents&task=icalrepeat.detail&evid=107&Itemid=114&year=2023&month=11&day=27&title=compliance-spotlight-off-channel-communications&uid=664c839976b9622e0a14a685225fce22](https://nama2.memberclicks.net/index.php?option=com_jevents&task=icalrepeat.detail&evid=107&Itemid=114&year=2023&month=11&day=27&title=compliance-spotlight-off-channel-communications&uid=664c839976b9622e0a14a685225fce22)

# Resources

- MSRB Rule Book and Compliance Resources
  - <https://www.msrb.org/Rules-and-Interpretations/MSRB-Rules>
- SEC OMS – Municipal Advisors Page
  - <https://www.sec.gov/municipal/municipal-advisors>
- Dave Sanchez, Closing Remarks - SEC Compliance Event
  - <https://www.sec.gov/news/speech/sanchez-remarks-compliance-conference-120723>

# Dave Sanchez, Closing Remarks

- MAs FD should start with the question of whether this financing even needs to be done
  - Must be a reasonable basis to borrow especially if determination is based on inaccurate or misleading information
  - No analysis on borrowing is even more concerning
  - Questionable deal structures and arrangements including those issued by privately run entities
- Concern with the number of negotiated sales
  - Body of research suggest competitive sales are more efficient in the majority of transactions.
  - MAs failing to provide appropriate information to issuers before method of sale is determined
  - Even when method of sale is determined prior to hiring MA, a non-binding agreement for issuer to engage in a negotiated sale does not absolve the MA of its FD to explore and present alternatives
  - MAs have regulatory responsibility with respect to pricing, which could include monitoring post-issuance sales activity
- Unregistered MAs
  - MA activity conducted by other regulated entities or deal participants
  - Unregistered MAs in P3 space
- Need for simplifying and streamlining rules and guidance to engender greater compliance
- SEC reminders on delinquency of Form MA filings and general Form deadline reminders
- Importance of complete, fair, and accurate disclosures including ESG and cybersecurity risks