



October 30, 2018

***VIA Email and First-Class Mail***

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Division of Trading and Markets

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Office of Municipal Securities

**pfm**

U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

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Re: Request for Interpretive Relief from Broker-Dealer Registration for Registered Municipal Advisor Acting as Fiduciary to Municipal Entity Issuers in connection with Direct Placements

pfm.com

Dear Mr. Redfearn, Ms. Rutkowski, and Ms. Olsen:

PFM Financial Advisors LLC (“PFM”), a registered municipal advisor, hereby requests that the staff of the Division of Trading and Markets and the Office of Municipal Securities (the “Staff”) of the U.S. Securities and Exchange Commission (the “Commission” or “SEC”) provide interpretive guidance that PFM would not be required to register as a broker-dealer (“BD”) under Section 15(a) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), if PFM, acting as a registered municipal advisor (“MA”) on behalf of its municipal entity (“ME”) issuer clients, engages in certain specified municipal advisory activities in connection with municipal financings structured as direct placements to banks and similar institutions meeting specified sophistication and size criteria (“Qualified Providers,” such transactions with Qualified Providers are referred to as “Direct Placements”).<sup>1</sup> The requested interpretive guidance (“Guidance”) is essential for PFM and other MAs to fulfill their statutory mandate to protect ME issuers, and to provide clarity and transparency regarding the role of the MA in municipal financing transactions. PFM submits that such clarity and transparency would not only enhance the efficiency of the municipal financing markets but would also enable ME issuers, working with their MAs, to obtain the best financing available to better serve their constituents. PFM also submits that the Guidance, by encouraging ME issuers to outsource their financing efforts to MAs that are registered under, and subject to, the federal securities laws, will better ensure that offering materials are accurate and complete. Undoubtedly, the resulting confidence in the municipal markets will encourage capital formation.

The requested Guidance would permit PFM to provide statutorily mandated services to its ME clients without the uncertainty of violating BD registration requirements. Specifically, PFM seeks Guidance that would permit PFM to fulfill its fiduciary obligations to its ME issuer clients and obligated persons in connection with direct placements by performing the following (“Covered MA Activities”):

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<sup>1</sup> PFM is also seeking interpretive guidance that PFM would not be required to register as a BD with respect to its provision of municipal advisory activities to Obligated Person clients. See Appendix A.



- **Identify and assess qualified providers.** Outreach to previously identified qualified providers, often in a competitive bidding process or referred by the ME client and evaluation of the differential terms proposed by qualified providers.
- **Interact with qualified providers.** Management leading to acceptable structuring of the material terms and conditions associated with the direct placement (negotiation of terms with providers). Negotiation on behalf of the ME client with one or more qualified providers selected by the ME with respect to the terms approved by the ME.
- **Perform coordination necessary with selected qualified provider(s).** Coordination of meetings and communications, documents and information between the ME client and, as applicable, their respective counsel, with the qualified providers, and, as applicable, their respective counsel and other advisors in order to document and complete the financing.

## I. Introduction

### A. PFM

As a registered MA, PFM offers financial advisory and management and budget consulting services to ME clients. Specifically, with respect to financial advisory services, PFM provides ME clients with independent financial advice on capital formation, bond pricing and debt management, quantitative strategies, and capital and strategic planning, among others.

### B. Direct Placements in Municipal Finance

As the Commission recognized, the municipal securities market is a significant part of the United States credit markets with over \$3.83 trillion in principal amounts outstanding.<sup>2</sup> According to the Commission, there are approximately 44,000 state and local issuers of municipal securities, ranging from villages, towns, townships, cities, counties, territories, and states, as well as special districts, such as school districts and water and sewer authorities.<sup>3</sup> In recent years, ME issuers have increasingly chosen to raise funds through Direct Placements as an alternative to issuing publicly offered municipal securities.<sup>4</sup> Accordingly, providing comprehensive advice to ME clients necessarily involves advice in assessing the

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<sup>2</sup> See Proposed Amendments to Municipal Securities Disclosure, SEC Rel. No. 34-80130 (Mar. 1, 2017) (“SEC 2017 Release”) (citing Federal Reserve Board, *Financial Accounts of the United States: Flows of Funds, Balance Sheets, and Integrated Macroeconomic Accounts* (Dec. 8, 2016)).

<sup>3</sup> See *Id.* (citing Securities and Exchange Commission, *Report on Municipal Securities Market* (July 31, 2012)).

<sup>4</sup> From the ME’s perspective, the potential benefits of Direct Placements include the following: (1) lower true interest and transaction costs for the ME issuer; (2) greater flexibility with respect to the structuring and terms of the financing; and (3) typically, a simpler execution process as the ME issuer interacts directly with the providers purchasing the Direct Placements, rather than with multiple bondholders through intermediaries. From the provider’s perspective, providing financing by means of a Direct Placement rather than purchasing a municipal bond provides corollary advantages: (1) direct interaction with the ME issuer, including direct access to information and the opportunity for more tailored due diligence; (2) direct communication with the ME issuer regarding the transaction structure; and (3) confidence that the transaction will become part of the provider’s investment portfolio.



costs and benefits of Direct Placements relative to all available financing options, and, where the ME client selects the Direct Placement alternative, advising the ME throughout all stages of the transaction. This can include, depending on the transaction, assistance with coordinating a request for proposals (“RFP”), often in a competitive bidding process, with evaluating the varying terms and other differential elements of proposals received, obtaining information regarding current market terms, negotiating terms further with a selected provider in seeking to obtain the most advantageous financing for the ME, and with implementing the terms of the transaction selected. The ME typically requires advice tailored to its particular needs at all key stages of the transaction through taking the financing “over the finish line.” It is in the ME’s interest for all of these functions to be performed by an MA, who, with a duty of loyalty to the ME, pursues only the ME’s, not the provider’s, best interests.

### **C. The Need for Guidance**

The need for Guidance arises because the statutory definition of “municipal advisory activities,” as supplemented by the Commission’s interpretation of the scope of such activities necessary to achieve the goals of MA regulation, expressly contemplates certain functions that – when conducted by intermediaries outside of the realm of registered MAs – appear similar to activities that have historically been considered indicative of BD activities (sometimes referred to as “Broker Factors”).<sup>5</sup> Absent the requested Guidance, the uncertainty caused by this “gray area” between MA and BD activities can result in a chilling effect on a MA’s ability to provide the full range of MA services that Congress intended and the consequent unintended impairment of financing options available to MEs. The requested Guidance is designed to remove such regulatory uncertainty with respect to MA activities that PFM believes are well within the statutory definition of “municipal advisory activities,” and thus ensure that an MA can provide the complete advice and service to its ME clients that Congress expressly sought to provide MEs, without fear of unwarranted regulatory repercussions.

To be sure, in other contexts, many of the functions, on their face, may resemble one or more of the Broker Factors. However, in the context of MA and ME relationships, MEs look to MAs to perform these services, acting in their fiduciary capacities to look out for the ME’s interests. In addition, the MA will have been hired because of its extensive and valuable specialized experience assisting MEs holistically in their financing needs, and the ME will want the full advantage of that experience and expertise.

Moreover, as is clear from the legislative and regulatory history of MA registration, the term “advice with respect to the issuance of municipal securities” should be construed broadly from a timing perspective to include advice throughout the life of an issuance of municipal

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<sup>5</sup> The Securities Exchange Act of 1934 (“Exchange Act”) defines MA to mean, in pertinent part, a person that provides advice to or on behalf of an ME with respect to the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues. In adopting the rules to implement the statutory requirements for MAs, the Commission further explained that with respect to the issuance of municipal securities, MAs, “among other things, may assist municipal entities in developing a financing plan, assist municipal entities in evaluating different financing options and structures, assist in the selection of other parties to the financing (such as bond counsel and underwriters), coordinate the rating process, ensure adequate disclosure, and/or evaluate and negotiate the financing terms.” See *Registration of Municipal Advisors*, SEC Rel. No. 34-70462 (Sep. 20, 2013), 78 FR 67468, 67472 (Nov. 12, 2013) (“Adopting Release”).



securities. As described in the Adopting Release, this begins with the pre-issuance planning stage and continues through negotiation and documentation and a coordinated, timely closing. As the Commission has recognized, advice that is particularized to the needs and circumstances of the ME client, which is the hallmark of the advice at which MA regulation is aimed, can be especially important during the planning stages of a financing, where the ME client needs advice in order to make significant decisions affecting the structure, timing, terms, or other similar matters concerning an issue of municipal securities.

## **II. Discussion**

As discussed more fully below, we submit that the requested Guidance is consistent with the statutory purposes for MA registration and regulation and, because of the fiduciary obligations imposed on MAs, the BD registration of MAs would serve no regulatory purpose and would, in fact, harm the interests of ME issuers. In addition, the Guidance would be consistent with the recognition of Congress and the Commission of the importance of coordinating MA registration and regulation with other existing regulatory regimes, and in particular of avoiding duplicative and overlapping regulation. Moreover, the narrow scope of the requested Guidance addresses the investor protection concerns of the Commission and Staff. Finally, we submit that that requested Guidance, by encouraging MEs to fully rely on MAs through all stages of the financing transaction, would enable more accurate and complete offering materials which support efficiency of the municipal markets and encourage capital formation.

### **A. Requested Guidance is Consistent with the Stated Purpose of Municipal Advisor Regulation**

PFM submits that the ability to engage in Covered MA Activities is not only essential for any MA to meet its fiduciary obligations in the context of a Direct Placement but is also consistent with the statutory construct, interpreted broadly by the Commission, that an MA provide advice to or on behalf of ME clients or obligated persons with respect to all matters and stages relating to the “issuance of municipal securities.”

#### **1. Fiduciary Duty**

Section 975 of the Dodd-Frank Act, signed into law in July of 2010, enacted additions to the Exchange Act that created a new class of registered persons and a new regulatory regime for MAs, as defined in the statute. The amendments to Section 15B of the Exchange Act enacted by Dodd-Frank required MAs to register with the Commission, imposed on MAs a fiduciary duty toward their ME clients, and charged the Commission and the MSRB with developing a registration and regulatory regime designed to fulfill Congress’s purposes.

Significantly, the imposition of a fiduciary duty on MAs as a result of the Dodd-Frank Act reflects Congress’s first initiative directed specifically at protecting the issuers of municipal securities.<sup>6</sup> The protection of ME issuers as the fundamental goal of Section 15B, and of the

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<sup>6</sup> See Transcript of Field Hearing on the State of the Municipal Securities Market Panel III, IV, & V, 2 (2010), available at (stating, “To our knowledge, this is the first time a securities regulator has been charged with protecting the issuer of securities.”).



Commission's rulemaking to implement the Congressional objective, is emphasized repeatedly throughout the Adopting Release.<sup>7</sup>

Consistent with the mandates of Dodd-Frank and per the Commission's statement in the Adopting Release, new MSRB Rule G-42 imposes on MAs a standard of conduct that includes the duties of loyalty and care when advising ME clients and sets forth a broad set of responsibilities, including the disclosure of conflicts of interests, documentation of the municipal advisory relationship, and suitability of recommendations, all directed toward protecting ME issuers.<sup>8</sup> Among other matters, the duty of care requires that the MA have a reasonable basis for any advice provided to or on behalf of the client, any representations made in connection with a financing transaction, and any information provided to the ME client or other third parties involved in the transaction. The requirements to "know your client" and to provide advice on municipal securities that are "suitable" to the municipal issuer are the cornerstones of Rule G-42 and form the basis upon which an MA fulfills its duties of care and loyalty as mandated by the rule.

## 2. Advice with Respect to the Issuance of Municipal Securities

For purposes of the MA definition, the Dodd-Frank Act did not specifically define or otherwise provide a general standard to determine what constitutes "advice" to an ME client. However, the Commission's final MA rules and the Adopting Release make clear that advice to ME clients that is particularized to their needs and is provided throughout the life of the financing transaction – from selecting a suitable method of financing through taking the financing "over the finish line" – is at the core of the "advice" that Congress sought to regulate and subject to the MA's fiduciary duty. As discussed more fully below, we believe the requested Guidance is consistent with broad scope of the "advice" contemplated for MAs in the conduct of their municipal advisory activities.

First, Rule 15Ba1-1(d)(1)(ii), which is captioned as "advice standard," identifies the provision of "a recommendation regarding municipal financial products or the issuance of municipal securities, including with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues" as the core activity included as "advice."<sup>9</sup> In

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<sup>7</sup> See Adopting Release, *supra* note 5, at 67469, (noting that "[m]unicipal advisors have been largely unregulated" and "[t]he information disclosed pursuant to the proposed rules and forms would aid municipal entities, obligated persons, and others in choosing municipal advisors, engaging in transactions with municipal advisors, or participating in transactions in municipal securities issued in offerings in which a municipal advisor provided municipal advisory services").

<sup>8</sup> On December 23, 2015, after an extensive comment process, the Commission approved new MSRB Rule G-42 which establishes core standards of conduct for MAs that engage in municipal advisory activities. Specifically, MSRB Rule G-42 imposes on MAs a comprehensive set of requirements in furtherance of their duties of care and loyalty to their ME and obligated person clients. Specifically, the duty of loyalty includes, but is not limited to, dealing honestly and with the utmost good faith with an ME client and acting in the client's best interests without regard to the financial or other interests of the MA. The duty of care includes, but is not limited to, the duty to possess the degree of knowledge and expertise needed to provide the ME client with informed advice, the duty to make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis of any advice provided to the client, and the duty to undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information.

<sup>9</sup> In adopting the "advice" rule, the Commission emphasized that there is no bright line test and that whether an activity constitutes advice depends on all relevant facts and circumstances. Accordingly, the rule operates by



explaining this provision, the Commission emphasized that for purposes of the MA definition, advice includes, without limitation, a recommendation that is “particularized to the specific needs, objectives, or circumstances of a municipal entity . . . with respect to municipal financial products or the issuance of municipal securities, including with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues, based on all the facts and circumstances.” The more individually tailored the information to a specific ME client, the Commission explained, the more likely it will be a recommendation that constitutes advice under the MA definition.

Second, while the scope of the term “advice” for purposes of MA regulation covers a range of activities in addition to advice with respect to issuance of municipal securities (such as advice with respect to municipal financial products), there is no doubt that advice with respect to the issuance of municipal securities is central to the regulatory regime. Section 15B(e)(4)(A) of the Exchange Act expressly sweeps within the MA definition persons that provide advice to or on behalf of an ME client or obligated person with respect to the “issuance of municipal securities,” including advice with respect to “the structure, timing, terms, and other similar matters” concerning such issues.

Consistent with this statutory focus, the Adopting Release makes clear that, as a matter of statutory construction and policy, activities covered by the subject of the “issuance of municipal securities” should be construed sufficiently broadly to ensure appropriate protection of ME clients with respect to advice relating in some way to the issuance of municipal securities and to limit the potential for circumvention of the MA registration provision. In particular, “advice with respect to the issuance of municipal securities” should be construed broadly from a timing perspective to include advice throughout the life of an issuance of municipal securities, from the pre-issuance planning stage for a debt transaction involving the issuance of municipal securities to the repayment stage for those municipal securities.”

The Commission’s broad interpretation of “advice with respect to the issuance of municipal securities” is designed to afford ME clients with the protections of the MA registration provision during the full timeframe during which the ME client needs advice on significant matters affecting the municipal financing – from beginning to end. In this regard, the Commission expressly recognized that ME clients may make significant decisions affecting the structure, timing, terms, or other similar matters concerning an issue of municipal securities early in the planning stages of a transaction and may make significant decisions affecting ongoing compliance, repayment, or refinancing throughout the term of an outstanding bond issue.

## **B. BD Registration of MAs Serves No Regulatory Purpose**

The imposition of BD registration and regulatory requirements on an MA for the performance of municipal advisory activities will either serve no regulatory purpose or prevent the MA from acting in the best interests of its ME clients if the MA is required to also act as a BD in the same Direct Placement. Given the imposition of a statutory fiduciary duty, an MA, even if it

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excluding the provision of information that does not constitute “a recommendation regarding municipal financial products or the issuance of municipal securities, including with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues.”



also registered as a BD, could not act as both an MA and a BD in the same Direct Placement given their conflicting obligations. Accordingly, BD registration of MAs would serve no regulatory purpose in Direct Placements. Should the Commission require an MA to somehow act in both capacities in the same Direct Placement, BD registration would create a direct conflict and prevent the MA from being able to act as a fiduciary to its ME clients. Moreover, BD registration of MAs in the conduct of their municipal advisory activities would critically impair their ability to protect ME interests. Where MEs are unable to rely on an MA, who is looking solely to the MEs' interests, ME issuers seeking to meet financing needs are less likely to obtain the best financing options available, thus reducing the efficiency of the municipal financing market.

### **C. Avoidance of Dual and Conflicting Regulation**

PFM believes that the requested relief is consistent with the exemptions from MA registration provided under the relevant statute and rules for registered BDs and registered investment advisers that are engaged in certain specified activities, including an exclusion from the MA definition for broker-dealers acting as underwriters (the "underwriter exclusion").<sup>10</sup> To give the full intended scope to the underwriter exclusion from MA regulation, the Commission has expanded the scope of the exclusion to "any registered broker-dealer who participates in a particular issuance of municipal securities," even where the broker-dealer is acting as an agent and thus does not fall within the statutory terms of the exclusion. "Therefore, if a registered broker-dealer, acting as a placement agent, performs municipal advisory activities that otherwise would be considered within the scope of the underwriting of a particular issuance of municipal securities as discussed above, the broker-dealer would not have to register as a municipal advisor."<sup>11</sup>

These exemptions and exclusions, including the underwriter exclusion from MA regulation as expanded to include placement agents that are not in fact underwriters, reflect recognition by Congress and the Commission of the importance of coordinating MA registration and regulation with other existing regulatory regimes, and in particular of avoiding duplicative and overlapping regulation, and the potential for conflicting regulation, where the specific activities in question may involve advice to MEs but are adequately regulated under other provisions of the federal securities laws. Appropriate coordination of regulatory regimes in order to strike the right balance is essential to avoiding regulation that would impose undue

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<sup>10</sup> The statutory definition of "municipal advisor" explicitly excludes "a broker, dealer, or municipal securities dealer acting as an underwriter." Rule 15Ba1-1(d)(2)(i) under the Exchange Act provides that the term "municipal advisor" shall not include a "broker, dealer, or municipal securities dealer serving as an underwriter of a particular issuance of municipal securities to the extent that the broker, dealer, or municipal securities dealer engages in activities that are within the scope of an underwriting of such issuance of municipal securities." The statutory definition of "municipal advisor" also explicitly excludes "any investment adviser registered under the Investment Advisers Act of 1940, or persons associated with such investment advisers who are providing investment advice." Rule 15Ba1-1(d)(2)(ii) under the Exchange Act excludes from the definition "[a]ny investment adviser registered under the Investment Advisers Act of 1940 or any person associated with such registered investment adviser to the extent that such registered investment adviser or such person is providing investment advice in such capacity." However, for purposes of the exclusion, "investment advice does not include advice concerning whether and how to issue municipal securities, advice concerning the structure, timing, and terms of an issuance of municipal securities and other similar matters, advice concerning municipal derivatives, or a solicitation of a municipal entity or obligated person."

<sup>11</sup> Adopting Release, *supra* note 5, at 67515.



costs and burdens on industry participants, including MEs, without serving any regulatory purpose and can also create conflicts that undermine the purpose of both sets of regulation.

Allowing concerns about potential threats to investor protection that in fact are not present to trump the real needs of MEs would penalize MEs without a compensating regulatory benefit. This does not, in our view, strike an appropriate regulatory balance.

#### **D. Protection of Investors Ensured by Narrow Scope of Request**

PFM is not asking for general, wide-ranging BD registration relief for MAs participating in private placements or other direct placements of municipal securities. On the contrary, the relief requested is narrowly targeted to address only activities that PFM believes Congress intended to be performed by registered MAs for the sole benefit of MEs under the new Dodd-Frank MA regulatory regime. The specific Covered MA Activities for which PFM seeks relief in connection with Direct Placements would not include serving as “placement agent” for municipal securities. Because of the narrow scope of the request, PFM believes that the relief it seeks would not jeopardize or adversely affect in any way the Commission’s effective oversight and enforcement of its BD registration and regulation requirements in other circumstances.

We recognize that BD regulation plays an important role in investor protection that is different from the goals and requirements of MA regulation, which is designed for the protection of MEs. We also appreciate that BD regulation serves a fundamental role in the Commission’s fulfilling its overall regulatory mission, with implications beyond the MA world.

PFM believes, however, that the regulatory goals for both MAs and BDs can be fully realized in the context of MA participation on the ME issuer’s behalf in completion of Direct Placements without any sacrifice of either the protection of MEs intended by Congress under Dodd-Frank or the protection of investors in the municipal marketplace that BD registration and regulation are designed to provide. We also believe that the Guidance can be narrowly tailored to remove uncertainty about legitimate fundamental MA activities without disrupting appropriate standards for BD registration established by the Commission and the Staff for application in other circumstances.

The requested Guidance will not compromise the investor protection concerns of the Commission and Staff. PFM has intentionally narrowed the scope of the Covered MA Activities to include only financing transactions with Qualified Providers that fall within the definition of Sophisticated Municipal Market Professionals in MSRB Rule D-15. The Staff has previously recognized that the nature of the investor can alleviate the need for BD registration.<sup>12</sup> In addition, any potential Qualified Provider confusion as to PFM’s role in the financing transaction can easily be resolved through the proposed disclosure outlined in

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<sup>12</sup> *M&A Brokers*, SEC No-Action Letter (Feb. 2, 2014). The incoming letter asserted that such mergers and acquisition transactions between sellers and buyers of privately owned companies “are qualitatively different in virtually every respect from traditional retail or institutional brokerage transactions.” Specifically, the incoming letter argued that “the active role of the buyer and seller in an M&A Transaction distinguishes these transactions from the purchase and sale of securities by retail and other investors for passive investment purposes, which is appropriately effected through the services of a registered broker-dealer.” In granting no-action relief, the Staff appears to have accepted the distinction drawn between M&A Transactions and traditional securities transactions.





Appendix B that PFM will be acting solely on behalf of the ME client for the entirety of the financing transaction.

In this connection, it is noteworthy that many Qualified Providers are divisions or subsidiaries of larger organizations that have sophisticated investment banking businesses. Accordingly, the Qualified Providers' participation in the Direct Placements do not give rise to traditional investor protection concerns that underlie the federal securities laws.

#### **E. Guidance is Consistent with the Commission's Mission**

Finally, PFM submits that the requested Guidance is consistent with the Commission's mission "to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation." While in the context of Direct Placements, the Qualified Providers are investing in municipal securities of ME issuers, we believe that the Commission's mission to "protect investors" must also include the protection of those ME issuers seeking to enter into the municipal financing market to obtain the financing necessary to provide or enhance services for their constituents. The requested Guidance will permit PFM or any other MA to provide comprehensive services to ME clients without the uncertainty as to whether engaging in municipal advisory activities will require BD registration. Such uncertainty only serves to deny ME issuers the full protection contemplated by Congress when requiring the registration and regulation of MAs.

PFM also submits that the Guidance will encourage fair, orderly and efficient municipal securities markets by encouraging increased participation by MAs in Direct Placements and other municipal financing transactions. As noted above, most MEs are smaller municipalities without the in-house expertise to plan and execute municipal transactions. We believe that by eliminating the regulatory uncertainty underlying our request, the Guidance will permit MAs to act in the best interest of ME issuers throughout the entire lifecycle of a Direct Placement transaction. We believe that ME issuers will not only benefit greatly in having the necessary expertise on their side of the table to achieve the best Direct Placement terms possible, but because of the wealth of knowledge and experience of PFM, or any other MA, the price of the securities will incorporate more fully all available information, thus increasing market efficiency.

Finally, PFM submits that the Guidance will encourage capital formation. In a 2012 speech, then SEC Commissioner Luis Aguilar explained that capital formation is much more than just capital raising. He stated that simply selling a bond or security, in and of itself, does not add to the real economy, but rather "[t]rue capital formation requires that the capital raised be invested in productive assets..."<sup>13</sup> We believe that the Guidance will enable PFM or any other MA to better represent the interests of ME issuers, and, in doing so, the ME issuer will be able to achieve the best financing available to invest in productive assets that will serve their constituents.

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<sup>13</sup> Commissioner Luis Aguilar, U.S. Securities and Exchange Commission, Speech, *Capital Formation from the Investor's Perspective*, (Dec. 3, 2012).



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## VII. Conclusion

PFM respectfully submits that the requested Guidance is necessary to dispel the uncertainty as to whether PFM and other MAs to engage in the Covered MA Activities in the context of Private Placements would subject PFM and other MAs to BD registration. As discussed above, PFM submits that the Covered MA Activities are activities contemplated by Congress in mandating the new regulatory regime for MAs. Moreover, by imposing a fiduciary duty on MAs, Congress intended MAs to look solely to the interests of its ME clients. BD registration of MAs would not only contravene Congressional intent, it would also serve no regulatory purpose since a registered MA cannot act as an MA and BD in the same municipal financing transaction. Clarity and transparency regarding the role of the MA in municipal financing transactions would not only enhance the efficiency of the municipal financing markets but would also enable ME issuers, working with their MAs, to obtain the best financing available to better serve their constituents. PFM also submits that the Guidance, by encouraging ME issuers to outsource their financing efforts to MAs that are registered under, and subject to, the federal securities laws, will better ensure that offering materials are accurate and complete. Undoubtedly, the resulting confidence in the municipal markets will encourage capital formation. Accordingly, we request the Guidance summarized in Appendix B.

Sincerely,

Cheryl Maddox  
General Counsel

Leo Karwena  
Chief Compliance Officer

cc: *(via electronic mail)*

Gary Hall, Chair, MSRB

Lynnette Kelly, President and Chief Executive Officer, MSRB

Michael Post, General Counsel, MSRB

Lanny Schwartz, Chief Regulatory Officer



## Appendix A - Obligated Persons

PFM also provides municipal advisory services in the context of conduit financing. Conduit financing involves the issuance of municipal securities by an ME to finance a project to be used primarily by a third party, which may be a for-profit entity engaged in private enterprise, a non-profit organization, or another governmental entity (“Obligated Person”). In a conduit financing, the Obligated Person is liable for making debt service payments on the municipal securities.<sup>14</sup> Thus, the Obligated Person may engage an MA to provide municipal advisory services in connection with the conduit financing for the same reasons an ME client would engage an MA – to consider all available financing alternatives and advise the Obligated Person client on all necessary aspects of the financing transaction until it has been completed.

An entity will not be an Obligated Person until such entity has begun the process of applying to, or negotiating with, an ME to issue conduit bonds on behalf of the entity. Thus, PFM will not be deemed to be acting as an MA to an Obligated Person until such entity commences negotiations with an ME issuer to issue conduit bonds on behalf of the entity. However, if such entity has an outstanding issue of municipal securities for which the entity is an Obligated Person and the MA advises them as to whether such securities should be redeemed or refinanced, such entity would be an Obligated Person and the MA would provide MA services to such Obligated Person.

As discussed in the main body of this request letter, the new Dodd-Frank provisions of the Exchange Act impose a fiduciary duty on MAs with respect to ME clients but not Obligated Persons. However, while an MA would not be subject to a statutory fiduciary duty to Obligated Person clients in conduit financing transactions, the MA will still be subject to the duty of care as set forth in MSRB Rule G-42, which includes heightened standards of conduct, duties and obligations.<sup>15</sup> The MSRB requires MAs to comply with such heightened standards of conduct with respect to both MEs and Obligated Persons. Moreover, for all practical purposes, an MA seeks to provide Obligated Person clients a level of MA services substantially similar to the services it provides to ME clients. Indeed, the needs of Obligated Person clients for tailored advice at all key stages of the conduit financing transaction, including taking the conduit financing “over the finish line,” are essentially the same as the needs of ME clients. Accordingly, PFM submits that the requested Guidance should also apply to any MA’s Covered MA Activities for Obligated Person clients.

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<sup>14</sup> The Obligated Person is typically a party to a bond purchase agreement entered into with the ME and the Provider.

<sup>15</sup> See MSRB Rule G-42(a)(i) (stating that an MA to an Obligated Person client “shall, in the conduct of all municipal advisory activities, be subject to the duty of care”).



## I. Duty of Care for Obligated Person Clients

Traditional concepts of fiduciary duty, include the duty of care and the duty of loyalty. Thus, in providing municipal advisory activities for both ME and Obligated Person clients, MSRB Rule G-42 imposes on MAs the duty of care. Pursuant to Supplementary Material .01, the duty of care requires that an MA possess the degree of knowledge and expertise needed to provide the ME or Obligated Person clients with informed advice. The MA also must make a reasonable inquiry as to the facts that are relevant to a client's determination as to whether to proceed with a course of action or that form the basis for any advice provided to the client. The MA must undertake a reasonable investigation to determine that it is not basing any recommendation on materially inaccurate or incomplete information. Among other matters, the MA must have a reasonable basis for:

- any advice provided to or on behalf of a client;
- any representations made in a certificate that the MA signs that will be reasonably foreseeably relied upon by the client, any other party involved in the financing transaction or municipal financial product, or investors in the ME client's securities or securities secured by payments from an Obligated Person client; and
- any information provided to the client or other parties involved in the financing transaction in connection with the preparation of an official statement for any issue of municipal securities as to which the MA is advising.

Thus, the duty of care imposes on the MA a heightened standard of conduct with respect to its services to Obligated Person clients, similar in many ways to an MA's obligations to ME clients.

## II. Qualified Providers

The requested Guidance with respect to Obligated Persons will not compromise the investor protection concerns of the Commission and Staff. As with the request in connection with ME clients, PFM requests Guidance in regards to financing transactions with Obligated Persons to cover Covered MA Activities with Qualified Providers that fall within the definition of Sophisticated Municipal Market Professionals in MSRB Rule D-15. Again, the Staff has previously recognized that the nature of the investor can alleviate the need for BD registration.<sup>16</sup> In addition, any potential Qualified Provider confusion as to an MA's role in the financing transaction can easily be resolved through the proposed disclosure outlined in Section 1.E. that the MA will be acting solely on behalf of the Obligated Person client for the entirety of the financing transaction.

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<sup>16</sup> *M&A Brokers, supra* note 18.



### **III. MAs Treat Obligated Person Clients Substantially Similar to ME Clients**

The needs of Obligated Person clients for tailored advice at key stages of the conduit financing transaction, including taking the conduit financing “over the finish line,” are essentially the same as the needs of ME clients in municipal financing transactions. Therefore, for all practical purposes, when providing MA services to Obligated Person clients, an MA treats such clients substantially similar to ME clients. Specifically, an MA must deal honestly and with the utmost good faith with the Obligated Person client. In addition, an MA generally does not engage in MA activities with an Obligated Person client if it cannot manage or mitigate its conflicts of interest.

For the reasons discussed above, PFM submits that the requested Guidance should be applied with respect to MA services provided to Obligated Person clients.



## **Appendix B – Form of Interpretive Relief**

PFM, acting in its capacity as a registered municipal advisor (“MA”) under Section 15(B) of the Securities Exchange Act of 1934 (the “Exchange Act”) may assist municipal entity issuer clients (“MEs”) and obligated persons (“Obligated Persons,” collectively with MEs, “MA Clients”) in connection with Direct Placements, as defined below, by performing the following activities, without registering as a broker-dealer under Section 15(a) of the Exchange Act (“Covered MA Activities”).

### **I. Definitions**

**Direct Placements** – Municipal financings structured as direct placements with Qualified Providers.

**Qualified Provider** – (i) a bank, savings and loan association, credit union, insurance company, or registered investment company; (ii) an investment adviser registered with the SEC or state registered; or (iii) any other institution with total assets of at least \$50 million.

### **II. Covered MA Activities**

- (1) Assistance in the identification and assessment of Qualified Providers for Direct Placements. This requires outreach to previously identified Qualified Providers by means of communications that are not properly characterized as “solicitation,” including requests for proposals (“RFPs”);
- (2) Direct interaction with Qualified Providers leading to acceptable structuring of the material terms and conditions associated with the Direct Placement. This would require negotiation on behalf of the MA Client with providers selected by the MA Client with respect to terms approved by the MA Client; and
- (3) Coordination necessary with the selected Qualified Provider to assist the MA Client, or their respective counsel, with documentation to complete the Direct Placement.

### **III. MA Disclosure Statement**

#### **A. ME Clients**

In connection with any Direct Placement, PFM will make the following disclosures to Qualified Providers to ensure that they understand that PFM represents solely the interests of the ME and not the Qualified Provider:

- (i) MSRB Rule G-17 requires PFM to deal fairly at all times with all transaction parties, including participants.
- (ii) PFM’s role is to act as a fiduciary to the ME client and is therefore required to act in the best interests of the ME client at all times.
- (iii) PFM is not a fiduciary to the Qualified Provider and therefore is not required to act in the best interests of the Qualified Provider or any other party without regard to its



own financial or other interests. Qualified Provider may engage its own agent to act on its behalf.

(iv) PFM has no duty to ensure, and will not determine or advise the Qualified Provider, as to the suitability of the transaction to the Qualified Provider.

(v) In fulfilling its fiduciary duties to the ME client, PFM may advise the ME client that the Qualified Provider may not be a suitable counterparty for the municipal financing. The final determination to enter into any transaction, including the types of transactions contemplated herein, shall be made solely by the ME client.

(vi) The Qualified Provider may determine that it wishes to have a registered broker-dealer involved in the transaction and should consider whether it wishes to do so.

### **B. Obligated Persons**

In connection with any Direct Placement, PFM will make the following disclosures to Qualified Providers to ensure that they understand that PFM represents the interests of the Obligated Person and not the Qualified Provider:

(i) MSRB Rule G-17 requires PFM to deal fairly at all times with all transaction parties, including participants.

(ii) PFM will represent the interests of the Qualified Provider and therefore will not act in the best interests of the Qualified Provider or any other party. Qualified Provider may engage its own agent to act on its behalf.

(iv) PFM has no duty to ensure, and will not determine or advise the Qualified Provider, as to the suitability of the transaction to the Qualified Provider.

(v) In fulfilling its duty of care to the Obligated Person, PFM may advise the Obligated Person that the Qualified Provider may not be a suitable counterparty for the municipal financing. The final determination to enter into any transaction, including the types of transactions contemplated herein, shall be made solely by the Obligated Person.

(vi) The Qualified Provider may determine that it wishes to have a registered broker-dealer involved in the transaction and should consider whether it wishes to do so.