



Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

December 6, 2019

Re: Notice of Proposed Exemptive Order Granting a Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Registered Municipal Advisors, File No. S7-16-19 (“Proposed Exemptive Order”)

Dear Ms. Countryman:

The American Securities Association (“ASA”)¹ submits this letter in response to the Securities and Exchange Commission’s (“SEC” or “Commission”) request for comment regarding the October 2, 2019 Proposed Exemptive Order (“Proposal”).² If adopted, the Proposed Exemptive Order would weaken critical investor protections by allowing registered municipal advisors to engage in activities related to municipal securities that would normally require registration as a broker-dealer under the Securities Exchange Act of 1934 (“Exchange Act”). Specifically, the Proposed Exemptive Order would allow municipal advisors to participate in the direct placement of municipal securities with investors and receive transaction-based compensation *without* having to register as broker-dealers.

ASA strongly opposes the adoption of ANY facet of the Proposal because it will investors at risk, leave municipalities vulnerable to the activities of bad actors, and undermine the SEC’s longstanding position regarding broker-dealer regulation in the area of municipal securities. There is absolutely no room to compromise on any policy that would allow unregulated actors to sell securities to America’s retail investors through sales to “investment advisors” as set forth in the Proposal. We care deeply about the reputation of our industry and we refuse to support a policy that will paint us with the same brush as the firms who would benefit from the Proposal when things go south, and investors are harmed.

Equally troubling, the Commission’s consideration of fundamental changes to the broker-dealer regulatory regime through a request for exemptive relief instead of through a formal rule, is an end-run around the transparency and accountability requirements governing federal agency rulemaking. Congress did not provide for this type of an exemption in statute, and specifically required entities engaged in the activities set forth in the Proposal to register as broker-dealers. To be clear, the adoption of any “exemption” in this area would result in the SEC engaging in policymaking that has not been

¹ The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA’s mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership base that spans the Heartland, Southwest, Southeast, Atlantic, and Pacific Northwest regions of the United States.

² <https://www.sec.gov/rules/exorders/2019/34-87204.pdf>

explicitly authorized by Congress. Even if Congress had spoken on this issue, an agency is only permitted to adopt this type of policy change through a transparent rulemaking governed by the processes outlined in the Administrative Procedure Act. Entertaining the use of an Exemptive Order to change a policy, which impacts investors and the general functioning of the market, displays a blatant disregard for that fundamental tenet of due process.

The Proposed Exemptive Order is legally deficient and suffers from several irredeemable flaws. Specifically, the Proposed Exemptive Order:

- Harms investors by empowering bad actors in the municipal market who are not be subject to a robust regulatory regime;
- Provides no empirical justification for why an exemption for municipal advisors from broker-dealer registration requirements is necessary or in the public interest;
- Will set a damaging precedent that fundamentally weakens regulation of broker-dealer activities in the future; and
- Directly contravenes Congressional intent regarding the regulation of broker-dealers in the area of municipal securities.

ASA's concerns are discussed in greater detail below.

I. The Proposed Exemptive Order will harm investors by empowering bad actors in the municipal market that will not be subject to a robust regulatory regime.

Inexplicably, the Proposal makes no mention of the large number of recent fraud cases involving municipal advisors.³ These cases, individually and collectively, demonstrate that many small towns, school districts, and other municipal entities are highly vulnerable to the activity of bad actors. It is astonishing that the SEC refuses to even acknowledge that both issuers and buyers of municipal securities will be put at risk by this Proposal.

Granting a broad class of municipal advisors a *loophole* from broker-dealer registration would only increase the instances of fraud, which will ultimately harm investors. As a reminder, investor protection is a fundamental prong of the agencies mission that we believe the current make-up of the Commission takes very seriously.⁴ It is an abdication of the Commission's authority to consider a staff-driven exemptive order instead of going through a normal rulemaking process for such a consequential issue. Moreover, it is abundantly clear that the entities pushing for this exemption want all the benefits of being a broker-dealer without having to deal with any the costs of registration, liability, and compliance. Such a nakedly self-interested request does not warrant consideration by the full Commission and should

³ See e.g. "South Carolina School District Sues FA and Bond Counsel" (Bond Buyer, March 8th 2019); "Commentary Duty of Care Enforcement for Municipal Advisors" (Bond Buyer, August 30 2017); "SEC Starts 2018 with an MA Enforcement Action" (Bond Buyer, January 5th 2018); "SEC Settles Charges of Unregistered Activities on Behalf of Municipal Advisor" (Bond Buyer, July 16th 2019).



have been promptly rejected. It is concerning that a request which promotes the interests of a single firm seeking to operate with a competitive advantage in America's municipal bond market was taken this seriously by the government. This Proposal embodies the exact type of agency capture by connected insiders that Americans on both sides of the aisle are pushing back on through protests, in elections, and in court rooms.

II. The Proposed Exemptive Order provides no empirical justification for why an exemption for municipal advisors from broker-dealer registration requirements is in the public interest

While the Proposed Exemptive Order includes a cursory discussion regarding the increased role that municipal advisors have played in the municipal securities market over the last decade, it provides no empirical analysis as to the existence of any market failure it seeks to address, or how such an exemption from Exchange Act registration requirements would benefit issuers or investors. The Proposed Exemptive Order is devoid of any type of economic analysis and seems to be predicated solely upon the requests of a market participant that wishes to perform the same functions as broker-dealers but spare themselves of the costs of registration and compliance.

Importantly, another SEC mandate, which Commissioner Jackson has stressed, is to look at the impact an agency action would have on competition.⁵ In this case, if the SEC were to adopt this proposal, it would put its finger on the scale of competition by favoring unregulated entities over those who are regulated. There is no empirical or legal justification for the SEC to adopt a such an outcome. To be crystal clear, this is a fundamental shortcoming of the Proposal and it smacks of agency overreach, especially given that Congress has NOT spoken on this point other than to require registration for entities undertaking traditional broker-dealer activities, such as the receipt of transaction-based compensation.

As you know, broker-dealers are subject to a comprehensive regulatory regime that includes suitability requirements and "know your customer" obligations, the maintenance of minimum capital requirements, fair commission and pricing standards, proper custody of customer assets, as well as rules governing sales practices and communications with investors. Broker-dealers are also subject to regular examinations by the Financial Industry Regulatory Authority (FINRA) and, for brokers involved in municipal securities transactions, they are subject to rules promulgated by the Municipal Securities Rulemaking Board (MSRB).

These longstanding rules and examinations requirements have served market participants and investors well for decades. Investors know when they interact with a registered broker-dealer that they are transacting with a *highly* regulated and transparent entity.

Moreover, the municipal private placements have been a very robust market in recent years, with issuers selling some \$40 billion of securities via private placements in 2017 and \$19 billion in 2018. In contrast

⁵ <https://www.sec.gov/news/speech/speech-jackson-101118>; Commissioners must consider "whether the action will promote efficiency, *competition*, and capital formation." Securities Act of 1933, 15 U.S.C. §77b(b) (2012) (emphasis added); Securities Exchange Act of 1934, 15 U.S.C. § 77b(f) (emphasis added).

with other aspects of securities regulation, there is no compelling justification to support the need for “regulatory relief” in a market that is functioning properly.

Regrettably, the Proposed Exemptive Order provides no justification as to how or why this system has failed the municipal market. It also provides no estimate as to the costs that would be imposed upon issuers or investors by exempting a broad class of market participants from these regulations. Leaving Main Street market participants to “fend for themselves” as they seek to transact in the municipal bond market is the exact opposite of what Congress provided for in the laws governing municipal securities transactions.

III. While this initiative is done under the guise of a narrow exemption for municipal advisors, it will set a damaging precedent that will fundamentally weaken regulation of broker-dealer activities in the future.

The Commission has long held that the receipt of transaction-based compensation, identifying purchasers of securities, and soliciting securities transactions, among other activities, are ALL functions of a broker-dealer, and therefore, require registration under the Exchange Act. The Proposal would effectively allow certain municipal advisors to engage in all of these activities without having to register as a broker-dealer.

While the Proposal states that the exemption would apply “only with respect to...limited activities,” this would set a damaging precedent for future regulation of broker-dealer activity. The SEC has in the past provided for exemptions from broker-dealer registration, however these exemptions were typically not available to individuals that received transaction-based compensation.⁶ This Proposal, if adopted, would break new ground for the SEC and increase the likelihood that the Commission would in the future further weaken the standards for broker-dealer registration. Again, this is something that Congress has not spoken about and the agency has no authority to inject itself into this type of policymaking without an explicit legislative directive to do so.

IV. The Proposed Exemptive Order is contrary to Congressional intent regarding the regulation of broker-dealers in the area of municipal securities.

Due to the perceived lack of transparency in the municipal securities market, Congress included provisions in the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) that required certain municipal advisors to register with the SEC and comply with both SEC and MSRB regulations. The SEC issued rules implementing the Dodd-Frank Act’s provisions in 2013.

Congress made clear with the Dodd-Frank Act that more, not less, supervision of municipal advisory activities specifically, and the municipal securities market was warranted, particularly given the number of high-profile frauds involving municipalities over the last decade. It defies logic to interpret Congressional intent as warranting less supervision for these advisors. Put simply, the Proposal undermines the important protections Congress put in place to protect the ultimate buyer and issuer by ignoring the lessons of previous frauds and crises at the municipal level.

⁶ See e.g. Exchange Act Rule 3a4-1



Conclusion

The ASA strongly opposes the Proposed Exemptive Order and believes that the SEC has a legal obligation to refrain from moving forward with this ultra vires initiative. No evidence exists to suggest that exempting certain entities from complying with regulations intended to protect investors is a good idea, will result in a good outcome, or will improve the functioning of the municipal bond market. The SEC *should* stick to its Congressional mandate and focus on ensuring that those who act on behalf of municipalities are complying with all applicable rules. What it should not do is enable fraudulent actors by creating loopholes in the securities laws that Congress never intended.

Sincerely,

Christopher A. Iacovella
Chief Executive Officer
American Securities Association