

MSRB Rule G-17

Conduct of Municipal Securities and Municipal Advisory Activities

Rule

In the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.

INTERPRETIVE NOTICE CONCERNING THE APPLICATION OF MSRB RULE G-17 TO UNDERWRITERS OF MUNICIPAL SECURITIES - August 2, 2012

Under Rule G-17 of the Municipal Securities Rulemaking Board (the “MSRB”), brokers, dealers, and municipal securities dealers (“dealers”) must, in the conduct of their municipal securities activities, deal fairly with all persons and must not engage in any deceptive, dishonest, or unfair practice. This rule is most often cited in connection with duties owed by dealers to investors; however, it also applies to their interactions with other market participants, including municipal entities^[1] such as states and their political subdivisions that are issuers of municipal securities (“issuers”).

The MSRB has previously observed that Rule G-17 requires dealers to deal fairly with issuers in connection with the underwriting of their municipal securities.^[2] More recently, with the passage of the Dodd-Frank Act,^[3] the MSRB was expressly directed by Congress to protect municipal entities. Accordingly, the MSRB is providing additional interpretive guidance that addresses how Rule G-17 applies to dealers acting in the capacity of underwriters in the municipal securities transactions described below. Except where a competitive underwriting is specifically mentioned, this notice applies to negotiated underwritings only. Furthermore, it does not apply to selling group members.

The examples discussed in this notice are illustrative only and are not meant to encompass all obligations of dealers to municipal entities under Rule G-17. The notice also does not address a dealer’s duties when the dealer is serving as an advisor to a municipal entity. Furthermore, when municipal entities are customers^[4] of dealers they are subject to the same protections under MSRB rules, including Rule G-17, that apply to other customers.^[5] The MSRB notes that an underwriter has a duty of fair dealing to investors in addition to its duty of fair dealing to issuers. An underwriter also has a duty to comply with other MSRB rules as well as other federal and state securities laws.

Basic Fair Dealing Principle

As noted above, Rule G-17 precludes a dealer, in the conduct of its municipal securities activities, from engaging in any deceptive, dishonest, or unfair practice with any person, including an issuer of municipal securities. The rule contains an anti-fraud prohibition. Thus, an underwriter must not misrepresent or omit the facts, risks, potential benefits, or other material information about municipal securities activities undertaken with a municipal issuer. However,

Rule G-17 does not merely prohibit deceptive conduct on the part of the dealer. It also establishes a general duty of a dealer to deal fairly with all persons (including, but not limited to, issuers of municipal securities), even in the absence of fraud.

Role of the Underwriter/Conflicts of Interest

In a negotiated underwriting, the underwriter's Rule G-17 duty to deal fairly with an issuer of municipal securities requires the underwriter to make certain disclosures to the issuer to clarify its role in an issuance of municipal securities and its actual or potential material conflicts of interest with respect to such issuance.

Disclosures Concerning the Underwriter's Role. The underwriter must disclose to the issuer that:

- (i) Municipal Securities Rulemaking Board Rule G-17 requires an underwriter to deal fairly at all times with both municipal issuers and investors;
- (ii) the underwriter's primary role is to purchase securities with a view to distribution in an arm's-length commercial transaction with the issuer and it has financial and other interests that differ from those of the issuer;
- (iii) unlike a municipal advisor, the underwriter does not have a fiduciary duty to the issuer under the federal securities laws and is, therefore, not required by federal law to act in the best interests of the issuer without regard to its own financial or other interests;
- (iv) the underwriter has a duty to purchase securities from the issuer at a fair and reasonable price, but must balance that duty with its duty to sell municipal securities to investors at prices that are fair and reasonable; and
- (v) the underwriter will review the official statement for the issuer's securities in accordance with, and as part of, its responsibilities to investors under the federal securities laws, as applied to the facts and circumstances of the transaction.

The underwriter also must not recommend that the issuer not retain a municipal advisor.