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.

Disclosure Concerning the Underwriter's Compensation. The underwriter must disclose to the issuer whether its underwriting compensation will be contingent on the closing of a transaction. It must also disclose that compensation that is contingent on the closing of a transaction or the size of a transaction presents a conflict of interest, because it may cause the underwriter to recommend a transaction that it is unnecessary or to recommend that the size of the transaction be larger than is necessary.

Other Conflicts Disclosures. The underwriter must also disclose other potential or actual material conflicts of interest, including, but not limited to, the following:

(i) any payments described below under "Conflicts of Interest/ Payments to or from Third Parties";

(ii) any arrangements described below under "Conflicts of Interest/Profit-Sharing with Investors";

(iii) the credit default swap disclosures described below under "Conflicts of Interest/Credit Default Swaps"; and

(iv) any incentives for the underwriter to recommend a complex municipal securities financing and other associated conflicts of interest (as described below under "Required Disclosures to Issuer").

Disclosures concerning the role of the underwriter and the underwriter's compensation may be made by a syndicate manager on behalf of other syndicate members. Other conflicts disclosures must be made by the particular underwriters subject to such conflicts.

Timing and Manner of Disclosures. All of the foregoing disclosures must be made in writing to an official of the issuer that the underwriter reasonably believes has the authority to bind the issuer by contract with the underwriter and that, to the knowledge of the underwriter, is not a party to a disclosed conflict. Disclosures must be made in a manner designed to make clear to such official the subject matter of such disclosures and their implications for the issuer. The disclosure concerning the arm's-length nature of the underwriter-issuer relationship must be made in the earliest stages of the underwriter's relationship with the issuer with respect to an issue (*e.g.*, in a response to a request for proposals or in promotional materials provided to an issuer). Other disclosures concerning the role of the underwriter and the underwriter's compensation generally must be made when the underwriter is engaged to perform underwriting services (*e.g.*, in an engagement letter), not solely in a bond purchase agreement. Other conflicts disclosures must be made at the same time, except with regard to conflicts discovered or arising after the underwriter has been engaged. For example, a conflict may not be present until an underwriter has recommended a particular financing. In that case, the disclosure must be provided in sufficient time before the execution of a contract with the underwriter to allow the official to evaluate the recommendation, as described below under "Required Disclosures to Issuers."

Acknowledgement of Disclosures. The underwriter must attempt to receive written acknowledgement (other than by automatic e-mail receipt) by the official of the issuer of receipt of the foregoing disclosures. If the official of the issuer agrees to proceed with the underwriting engagement after receipt of the disclosures but will not provide written acknowledgement of receipt, the underwriter may proceed with the engagement after documenting with specificity why it was unable to obtain such written acknowledgement.

Representations to Issuers

All representations made by underwriters to issuers of municipal securities in connection with municipal securities underwritings, whether written or oral, must be truthful and accurate and must not misrepresent or omit material facts. Underwriters must have a reasonable basis for the representations and other material information contained in documents they prepare and must refrain from including representations or other information they know or should know is inaccurate or misleading. For example, in connection with a certificate signed by the underwriter that will be relied upon by the issuer or other relevant parties to an underwriting (*e.g.*, an issue price certificate), the dealer must have a reasonable basis for the representations and other material information contained therein. In addition, an underwriter's response to an issuer's request for proposals or qualifications must fairly and accurately describe the underwriter's capacity, resources, and knowledge to perform the proposed underwriting as of the time the proposal is submitted and must not contain any representations or other material information about such capacity, resources, or knowledge that the underwriter knows or should know to be inaccurate or misleading. Matters not within the personal knowledge of those preparing the response (*e.g.*, pending litigation) must be confirmed by those with knowledge of the subject matter. An underwriter must not represent that it has the requisite knowledge or expertise with respect to a particular financing if the personnel that it intends to work on the financing do not have the requisite knowledge or expertise.

Required Disclosures to Issuers

Many municipal securities are issued using financing structures that are routine and well understood by the typical municipal market professional, including most issuer personnel that have the lead responsibilities in connection with the issuance of municipal securities. For example, absent unusual circumstances or features, the typical fixed rate offering may be presumed to be well understood. Nevertheless, in the case of issuer personnel that the underwriter reasonably believes lack knowledge or experience with such structures, the underwriter must provide disclosures on the material aspects of such structures that it recommends.

However, in some cases, issuer personnel responsible for the issuance of municipal securities would not be well positioned to fully understand or assess the implications of a financing in its totality, because the financing is structured in a unique, atypical, or otherwise complex manner (a "complex municipal securities financing").[6] Examples of complex municipal securities financings include variable rate demand obligations ("VRDOs") and financings involving derivatives (such as swaps). An underwriter in a negotiated offering that recommends a complex municipal securities financing to an issuer has an obligation under Rule G-17 to make more particularized disclosures than those that may be required in the case of routine financing structures. The underwriter must disclose the material financial characteristics of the complex municipal securities financing, as well as the material financial risks of the financing that are known to the underwriter and reasonably foreseeable at the time of the disclosure.[7] It must also disclose any incentives for the underwriter to recommend the financing and other associated conflicts of interest.[8] Such disclosures must be made in a fair and balanced manner based on principles of fair dealing and good faith.

The level of disclosure required may vary according to the issuer's knowledge or experience with the proposed financing structure or similar structures, capability of evaluating the risks of the recommended financing, and financial ability to bear the risks of the recommended financing, in each case based on the reasonable belief of the underwriter.[9] In all events, the underwriter must disclose any incentives for the underwriter to recommend the complex municipal securities financing and other associated conflicts of interest.

The disclosures described in this section of this notice must be made in writing to an official of the issuer whom the underwriter reasonably believes has the authority to bind the issuer by contract with the underwriter (i) in sufficient time before the execution of a contract with the underwriter to allow the official to evaluate the recommendation and (ii) in a manner designed to make clear to such official the subject matter of such disclosures and their implications for the issuer. The disclosures concerning a complex municipal securities financing must address the specific elements of the financing, rather than being general in nature. If the underwriter does not reasonably believe that the official to whom the disclosures are addressed is capable of independently evaluating the disclosures, the underwriter must make additional efforts reasonably designed to inform the official or its employees or agent.

Underwriter Duties in Connection with Issuer Disclosure Documents

Underwriters often play an important role in assisting issuers in the preparation of disclosure documents, such as preliminary official statements and official statements.[10] These documents are critical to the municipal securities transaction, in that investors rely on the representations contained in such documents in making their investment decisions. Moreover, investment professionals, such as municipal securities analysts and ratings services, rely on the representations in forming an opinion regarding the credit. A dealer's duty to have a reasonable basis for the representations it makes, and other material information it provides, to an issuer and to ensure that such representations and information are accurate and not misleading, as described above, extends to representations and information provided by the underwriter in connection with the preparation by the issuer of its disclosure documents (*e.g.*, cash flows).

Underwriter Compensation and New Issue Pricing

Excessive Compensation. An underwriter's compensation for a new issue (including both direct compensation paid by the issuer and other separate payments, values, or credits received by the underwriter from the issuer or any other party in connection with the underwriting), in certain cases and depending upon the specific facts and circumstances of the offering, may be so disproportionate to the nature of the underwriting and related services performed as to constitute an unfair practice with regard to the issuer that it is a violation of Rule G-17. Among the factors relevant to whether an underwriter's compensation is disproportionate to the nature of the underwriting and related services performed, are the credit quality of the issue, the size of the issue, market conditions, the length of time spent structuring the issue, and whether the underwriter is paying the fee of the underwriter's counsel or any other relevant costs related to the financing.

Fair Pricing. The duty of fair dealing under Rule G-17 includes an implied representation that the price an underwriter pays to an issuer is fair and reasonable, taking into consideration all relevant factors, including the best judgment of the underwriter as to the fair market value of the issue at the time it is priced.[11] In general, a dealer purchasing bonds in a competitive underwriting for which the issuer may reject any and all bids will be deemed to have satisfied its duty of fairness to the issuer with respect to the purchase price of the issue as long as the dealer's bid is a bona fide bid (as defined in Rule G-13)[12] that is based on the dealer's best judgment of the fair market value of the securities that are the subject of the bid. In a negotiated underwriting, the underwriter has a duty under Rule G-17 to negotiate in good faith with the issuer. This duty includes the obligation of the dealer to ensure the accuracy of representations made during the course of such negotiations, including representations regarding the price negotiated and the nature of investor demand for the securities (*e.g.*, the status of the order period and the order book). If, for example, the dealer represents to the issuer that it is providing the "best" market price available on the new issue, or that it will exert its best efforts to obtain the "most favorable" pricing, the dealer may violate Rule G-17 if its actions are inconsistent with such representations.[13]

Conflicts of Interest

Payments to or from Third Parties. In certain cases, compensation received by the underwriter from third parties, such as the providers of derivatives and investments (including affiliates of the underwriter), may color the underwriter's judgment and cause it to recommend products, structures, and pricing levels to an issuer when it would not have done so absent such payments. The MSRB views the failure of an underwriter to disclose to the issuer the existence of payments, values, or credits received by the underwriter in connection with its underwriting of the new issue from parties other than the issuer, and payments made by the underwriter in connection with such new issue to parties other than the issuer (in either case including payments, values, or credits that relate directly or indirectly to collateral transactions integrally related to the issue being underwritten), to be a violation of the underwriter's obligation to the issuer under Rule G-17.[14] For example, it would be a violation of Rule G-17 for an underwriter to compensate an undisclosed third party in order to secure municipal securities business. Similarly, it would be a violation of Rule G-17 for an underwriter to receive undisclosed compensation from a third party in exchange for recommending that third party's services or product to an issuer, including business related to municipal securities derivative transactions. This notice does not require that the amount of such third-party payments be disclosed. The underwriter must also disclose to the issuer whether it has entered into any third-party arrangements for the marketing of the issuer's securities.

Profit-Sharing with Investors. Arrangements between the underwriter and an investor purchasing new issue securities from the underwriter (including purchases that are contingent upon the delivery by the issuer to the underwriter of the securities) according to which profits realized from the resale by such investor of the securities are directly or indirectly split or otherwise shared with the underwriter also would, depending on the facts and circumstances (including in particular if such resale occurs reasonably close in time to the original sale by the underwriter to the investor), constitute a violation of the underwriter's fair dealing obligation under Rule G-17. Such arrangements could also constitute a violation of Rule G-25(c), which precludes a dealer from sharing, directly or indirectly, in the profits or losses of a transaction in municipal securities with or for a customer.

Credit Default Swaps. The issuance or purchase by a dealer of credit default swaps for which the reference is the issuer for which the dealer is serving as underwriter, or an obligation of that issuer, may pose a conflict of interest, because trading in such municipal credit default swaps has the potential to affect the pricing of the underlying reference obligations, as well as the pricing of other obligations brought to market by that issuer. Rule G-17 requires, therefore, that a dealer disclose the fact that it engages in such activities to the issuers for which it serves as underwriter. Activities with regard to credit default swaps based on baskets or indexes of municipal issuers that include the issuer or its obligation(s) need not be disclosed, unless the issuer or its obligation(s) represents more than 2% of the total notional amount of the credit default swap or the underwriter otherwise caused the issuer or its obligation(s) to be included in the basket or index.

Retail Order Periods

Rule G-17 requires an underwriter that has agreed to underwrite a transaction with a retail order period to, in fact, honor such agreement.[15] A dealer that wishes to allocate securities in a manner that is inconsistent with an issuer's requirements must not do so without the issuer's consent. In addition, Rule G-17 requires an underwriter that has agreed to underwrite a

transaction with a retail order period to take reasonable measures to ensure that retail clients are bona fide. An underwriter that knowingly accepts an order that has been framed as a retail order when it is not (*e.g.*, a number of small orders placed by an institutional investor that would otherwise not qualify as a retail customer) would violate Rule G-17 if its actions are inconsistent with the issuer's expectations regarding retail orders. In addition, a dealer that places an order that is framed as a qualifying retail order but in fact represents an order that does not meet the qualification requirements to be treated as a retail order (*e.g.*, an order by a retail dealer without "going away" orders[16] from retail customers, when such orders are not within the issuer's definition of "retail") violates its Rule G-17 duty of fair dealing. The MSRB will continue to review activities relating to retail order periods to ensure that they are conducted in a fair and orderly manner consistent with the intent of the issuer and the MSRB's investor protection mandate.

Dealer Payments to Issuer Personnel

Dealers are reminded of the application of MSRB Rule G-20, on gifts, gratuities, and non-cash compensation, and Rule G-17, in connection with certain payments made to, and expenses reimbursed for, issuer personnel during the municipal bond issuance process.[17] These rules are designed to avoid conflicts of interest and to promote fair practices in the municipal securities market.

Dealers should consider carefully whether payments they make in regard to expenses of issuer personnel in the course of the bond issuance process, including in particular, but not limited to, payments for which dealers seek reimbursement from bond proceeds or issuers, comport with the requirements of Rule G-20. For example, a dealer acting as a financial advisor or underwriter may violate Rule G-20 by paying for excessive or lavish travel, meal, lodging and entertainment expenses in connection with an offering (such as may be incurred for rating agency trips, bond closing dinners, and other functions) that inure to the personal benefit of issuer personnel and that exceed the limits or otherwise violate the requirements of the rule.[18]

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[1] The term "municipal entity" is defined by Section 15B(e)(8) of the Securities Exchange Act (the "Exchange Act") to mean: "any State, political subdivision of a State, or municipal corporate instrumentality of a State, including—(A) any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (B) any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (C) any other issuer of municipal securities."

[2] *See* Reminder Notice on Fair Practice Duties to Issuers of Municipal Securities, MSRB Notice 2009-54 (September 29, 2009); Rule G-17 Interpretive Letter — Purchase of new issue from issuer, MSRB interpretation of December 1, 1997, reprinted in MSRB Rule Book ("1997 Interpretation").

[3] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 § 975, 124 Stat. 1376 (2010).

[4] MSRB Rule D-9 defines the term "customer" as follows: "Except as otherwise specifically provided by rule of the Board, the term "Customer" shall mean any person other than a broker, dealer, or municipal securities dealer acting in its capacity as such or an issuer in transactions involving the sale by the issuer of a new issue of its securities."

[5] *See* MSRB Reminds Firms of Their Sales Practice and Due Diligence Obligations When Selling Municipal Securities in the Secondary Market, MSRB Notice 2010-37 (September 20, 2010).

[6] If a complex municipal securities financing consists of an otherwise routine financing structure that incorporates a unique, atypical or complex element and the issuer personnel have knowledge or experience with respect to the routine elements of the financing, the disclosure of material risks and characteristics may be limited to those relating to such specific element and any material impact such element may have on other features that would normally be viewed as routine.

[7] For example, an underwriter that recommends a VRDO should inform the issuer of the risk of interest rate fluctuations and material risks of any associated credit or liquidity facilities (e.g., the risk that the issuer might not be able to replace the facility upon its expiration and might be required to repay the facility provider over a short period of time). As an additional example, if the underwriter recommends that the issuer swap the floating rate interest payments on the VRDOs to fixed rate payments under a swap, the underwriter must disclose the material financial risks (including market, credit, operational, and liquidity risks) and material financial characteristics of the recommended swap (e.g., the material economic terms of the swap, the material terms relating to the operation of the swap, and the material rights and obligations of the parties during the term of the swap), as well as the material financial risks associated with the VRDO. Such disclosure should be sufficient to allow the issuer to assess the magnitude of its potential exposure as a result of the complex municipal securities financing. The underwriter must also inform the issuer that there may be accounting, legal, and other risks associated with the swap and that the issuer should consult with other professionals concerning such risks. If the underwriter's affiliated swap dealer is proposed to be the executing swap dealer, the underwriter may satisfy its disclosure obligation with respect to the swap if such disclosure has been provided to the issuer by the affiliated swap dealer or the issuer's swap or other financial advisor that is independent of the underwriter and the swap dealer, as long as the underwriter has a reasonable basis for belief in the truthfulness and completeness of such disclosure. If the issuer decides to enter into a swap with another dealer, the underwriter is not required to make disclosures with regard to that swap. The MSRB notes that dealers that recommend swaps or security-based swaps to municipal entities may also be subject to rules of the Commodity Futures Trading Commission or those of the Securities and Exchange Commission ("SEC").

[8] For example, a conflict of interest may exist when the underwriter is also the provider of a swap used by an issuer to hedge a municipal securities offering or when the underwriter receives compensation from a swap provider for recommending the swap provider to the issuer. See also "Conflicts of Interest/Payments to or from Third Parties" herein.

[9] Even a financing in which the interest rate is benchmarked to an index that is commonly used in the municipal marketplace (*e.g.*, LIBOR or SIFMA) may be complex to an issuer that does not understand the components of that index or its possible interaction with other indexes.

[10] Underwriters that assist issuers in preparing official statements must remain cognizant of their duties under federal securities laws. With respect to primary offerings of municipal securities, the SEC has noted, "By participating in an offering, an underwriter makes an implied recommendation about the securities." *See* SEC Rel. No. 34-26100 (Sept. 22, 1988) (proposing Exchange Act Rule 15c2-12) at text following note 70. The SEC has stated that "this recommendation itself implies that the underwriter has a reasonable basis for belief in the truthfulness and completeness of the key representations made in any disclosure documents used in the offerings." Furthermore, pursuant to SEC Rule 15c2-12(b)(5), an underwriter may not purchase or sell municipal securities in most primary offerings unless the underwriter has reasonably determined that the issuer or an obligated person has entered into a written undertaking to provide

certain types of secondary market disclosure and has a reasonable basis for relying on the accuracy of the issuer's ongoing disclosure representations. SEC Rel. No. 34-34961 (Nov. 10, 1994) (adopting continuing disclosure provisions of Exchange Act Rule 15c2-12) at text following note 52.

[11] The MSRB has previously observed that whether an underwriter has dealt fairly with an issuer for purposes of Rule G-17 is dependent upon all of the facts and circumstances of an underwriting and is not dependent solely on the price of the issue. See MSRB Notice 2009-54 and the 1997 Interpretation. *See also* "Retail Order Periods" herein.

[12] Rule G-13(b)(iii) provides: "For purposes of subparagraph (i), a quotation shall be deemed to represent a "bona fide bid for, or offer of, municipal securities" if the broker, dealer or municipal securities dealer making the quotation is prepared to purchase or sell the security which is the subject of the quotation at the price stated in the quotation and under such conditions, if any, as are specified at the time the quotation is made."

[13] *See* 1997 Interpretation.

[14] *See also* "Required Disclosures to Issuers" herein.

[15] *See* MSRB Interpretation on Priority of Orders for Securities in a Primary Offering under Rule G-17, MSRB interpretation of October 12, 2010, reprinted in MSRB Rule Book. The MSRB also reminds underwriters of previous MSRB guidance on the pricing of securities sold to retail investors. See Guidance on Disclosure and Other Sales Practice Obligations to Individual and Other Retail Investors in Municipal Securities, MSRB Notice 2009-42 (July 14, 2009).

[16] In general, a "going away" order is an order for new issue securities for which a customer is already conditionally committed. *See* SEC Release No. 34-62715, File No. SR-MSRB-2009-17 (August 13, 2010).

[17] *See* MSRB Rule G-20 Interpretation — Dealer Payments in Connection With the Municipal Securities Issuance Process, MSRB interpretation of January 29, 2007, reprinted in MSRB Rule Book.

[18] *See* In the Matter of RBC Capital Markets Corporation, SEC Rel. No. 34-59439 (Feb. 24, 2009) (settlement in connection with broker-dealer alleged to have violated MSRB Rules G-20 and G-17 for payment of lavish travel and entertainment expenses of city officials and their families associated with rating agency trips, which expenditures were subsequently reimbursed from bond proceeds as costs of issuance); In the Matter of Merchant Capital, L.L.C., SEC Rel. No. 34-60043 (June 4, 2009) (settlement in connection with broker-dealer alleged to have violated MSRB rules for payment of travel and entertainment expenses of family and friends of senior officials of issuer and reimbursement of the expenses from issuers and from proceeds of bond offerings).

Excerpt from Notice of Application of MSRB Rules to Solicitor Municipal Advisors

May 4, 2017

Conduct of Municipal Securities and Municipal Advisor Activities, Rule G-17

The MSRB amended Rule G-17, regarding fair dealing, to require that, in the conduct of their municipal advisory activities, municipal advisors, including solicitor municipal advisors, and their associated persons must deal fairly with all persons and not engage in any deceptive, dishonest, or unfair practice. (Previously, the rule applied only to dealers and their associated persons.) Rule G-17 became applicable to all municipal advisors, including solicitor municipal advisors, and their associated persons, on December 22, 2010.

Rule G-17 contains an anti-fraud prohibition similar to the standard set forth in Rule 10b-5 adopted by the SEC under the Exchange Act. Thus, all municipal advisors must refrain from engaging in certain conduct and must not misrepresent or omit the facts, risks, or other material information about municipal advisory activities undertaken. However, Rule G-17 does not merely prohibit deceptive conduct on the part of a municipal advisor. The rule also establishes a general duty of a municipal advisor to deal fairly with all persons, even in the absence of fraud.

Rule G-17 imposes a duty of fair dealing on solicitor municipal advisors when they are soliciting business from municipal entities and obligated persons on behalf of third parties. Again, municipal advisors are reminded that the term "municipal entity" also includes certain entities that do not issue municipal securities. Thus, in addition to owing the specific obligations discussed below to issuers of municipal securities, solicitor municipal advisors also owe such obligations to, for example, state and local government sponsored public pension plans and local government investment pools.

The duty of fair dealing includes, but is not limited to, a duty to disclose to the municipal entity or obligated person being solicited material facts about the solicitation, such as the name of the solicitor's client; the type of business being solicited; the amount and source of all of the solicitor's compensation; payments (including in-kind) made by the solicitor to another solicitor municipal advisor (including an affiliate, but not an employee) to facilitate the solicitation regardless of characterization; and any relationships of the solicitor with any employees or board members of the municipal entity or obligated person being solicited or any other persons affiliated with the municipal entity or obligated person or its officials who may have influence over the selection of the solicitor's client.

Additionally, if a solicitor municipal advisor is engaged by its client to present information about a product or service offered by the third-party client to the municipal entity or obligated person, the solicitor municipal advisor must disclose all material risks and characteristics of the product or service. The solicitor municipal advisor must also advise the municipal entity or obligated person of any incentives received by the solicitor (that are not already disclosed as part of the solicitor municipal advisor's compensation from its client) to recommend the product or service, as well as any other conflicts of interest regarding the product or service, and must not make material misstatements or omissions when discussing the product or service.

Under the Exchange Act, municipal advisors and their associated persons are deemed to owe a fiduciary duty to their municipal entity clients.* Similarly, Rule G-42 (which applies only to non-solicitor municipal advisors) follows the Exchange Act in deeming municipal advisors to owe a fiduciary duty, for purposes of Rule G-42, to such municipal entity clients. However, because a solicitor municipal advisor's clients are not the municipal entities that they solicit, but rather the third parties that retain or engage the solicitor municipal advisor to solicit such municipal entities, solicitor municipal advisors do not owe a fiduciary duty under the Ex-

change Act or MSRB rules to their clients (or the municipal entity) in connection with such activity. Nonetheless, as noted above, solicitor municipal advisors are subject to the fair dealing standards under Rule G-17 (including with respect to their clients and the entities that they solicit).

* *See* Order Adopting SEC Final Rule [Release No. 34-70462 (September 20, 2013), 78 FR 67467 (November 12, 2013) (File No. S7-45-10)], at n. 100 (noting that the fiduciary duty of a municipal advisor, as set forth in Section 15B(c)(1) of the Exchange Act, extends only to its municipal entity clients).

See also:

Rule G-11 Interpretations — Notice Concerning Syndicate Expenses, November 14, 1991.

- **Syndicate Expenses: Per Bond Fee for Bookrunning Expenses,** June 14, 1995.

Rule G-15 Interpretations — Notice Concerning Confirmation, Delivery and Reclamation of Interchangeable Securities, August 10, 1988.

- **Notice Concerning Stripped Coupon Municipal Securities,** March 13, 1989.

Rule G-20 Interpretation — Dealer Payments in Connection with the Municipal Securities Issuance Process, January 29, 2007.

Rule G-21 Interpretation — Interpretation on General Advertising Disclosures, Blind Advertisements and Annual Reports Relating to Municipal Fund Securities Under Rule G-21, June 5, 2007

Rule G-30 Interpretation — Interpretive Notice on Commissions and Other Charges, Advertisements and Official Statements Relating to Municipal Fund Securities, December 19, 2001.

Rule G-32 Interpretations — Notice Regarding the Disclosure Obligations of Brokers, Dealers and Municipal Securities Dealers in Connection with New Issue Municipal Securities Under Rule G-32, November 19, 1998.

Rule G-43 Interpretation — Notice to Dealers That Use the Services of Broker's Brokers, December 22, 2012.

Interpretive Letters

"Wooden tickets." This is in response to your letter of February 4, 1981 asking whether the practice of a broker-dealer using "wooden tickets" is prohibited by Board rule G-17. According to your letter, this practice refers to the mailing of confirmations of sales to customers who, in fact, have not placed orders to purchase securities. Thereafter, if any customer objects, stating that it never authorized the transaction, the sale is canceled. You state that, in some cases, customers accept the transaction and make payment.

The Board has determined that the practice by a municipal securities dealer of knowingly issuing confirmations of sales to customers who have not placed orders to purchase the bonds is a deceptive, dishonest, and unfair practice under rule G-17. *MSRB interpretation of March 3, 1981.*

Put option bonds: safekeeping, pricing. I am writing in response to your recent letter regarding issues of municipal securities with put option or tender option features, under which a holder of the securities may put the securities back to the issuer or an agent of the issuer at par on certain stated dates. In your letter you inquire generally as to the confirmation disclosure requirements applicable to such securities. You also raise several questions regarding a dealer's obligation to advise customers of the existence of the put option provision at times other than the time of sale of the securities to the customer.

Your letter was referred to a committee of the Board which has responsibility for interpreting the Board's confirmation rules, among other matters. That committee has authorized my sending you the following response.

Both rules G-12(c) and G-15, applicable to inter-dealer and customer confirmations respectively, require that confirmations of transactions in securities which are subject to put option or tender option features must indicate that fact (*e.g.*, through inclusion of the designation "puttable" on the confirmation). The date on which the put option feature first comes into effect need be stated on the confirmation only if the transaction is effected on a yield basis and the parties to the transaction specifically agree that the transaction dollar price should be computed to that date. In the absence of such an agreement, the put date need not be stated on the confirmation, and any yield disclosed should be a yield to maturity.

Of course, municipal securities brokers and dealers selling to customers securities with put option or tender option features are obligated to disclose adequately the special characteristics of these securities at the time of trade. The customer therefore should be advised of information about the put option or tender option feature at this time.

In your letter you inquire whether a dealer who had previously sold securities with a put option or tender option feature to a customer would be obliged to contact that customer around the time the put option comes into effect to remind the customer that the put option is available. You also ask whether such an obligation would exist if the dealer held the securities in safekeeping for the customer. The committee can respond, of course, only in terms of the requirements of Board rules; the committee noted that no Board rule would impose such an obligation on the dealer.

In your letter you also ask whether a dealer who purchased from a customer securities with a put option or tender option feature at the time of the put option exercise date at a price significantly below the put exercise price would be in violation of any Board rules. The committee believes that such a dealer might well be deemed to be in violation of Board rules G-17 on fair dealer and G-30 on prices and commissions. *MSRB interpretation of February 18, 1983.*

Description provided at or prior to the time of trade. This is in response to your February 27, 1986 letter and our prior telephone conversation concerning the application of Board

rules to the description of municipal securities exchanged at or prior to the time of trade. You note that it is becoming more and more common in the municipal securities secondary market for sellers, both dealers and customers, to provide only a "limited description" and CUSIP number for bonds being sold. Recently you were asked by a customer to bid on $4 million of bonds and were given the coupon, maturity date, and issuer. When you asked for more information, you were given the CUSIP number. You then bid on and purchased the bonds. After the bonds were confirmed, you discovered that the bonds were callable and that, when these bonds first came to market, they were priced to the call. You state that the seller was aware that the bonds were callable.

Your letter was referred to a Committee of the Board which has responsibility for interpreting the Board's fair practice rules. That Committee has authorized this response.

Board rule G-17 provides that

> In the conduct of its municipal securities business, *each broker, dealer, and municipal securities dealer* shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice. (emphasis added)

The Board has interpreted this rule to require that, in connection with the purchase from or sale of a municipal security to a customer, at or before execution of the transaction, a dealer must disclose all material facts concerning the transaction which could affect the customer's investment decision and not omit any material facts which would render other statements misleading. The fact that a municipal security may be redeemed in-whole, in-part, or in extraordinary circumstances prior to maturity is essential to a customer's investment decision and is one of the facts a dealer must disclose.

I note from our telephone conversation that you ask whether Board rules specify what information a customer must disclose to a dealer at the time it solicits bids to buy municipal securities. Customers are not subject to the Board's rules, and no specific disclosure rules would apply to customers beyond the application of the anti-fraud provisions of the federal securities laws. I note, however, that a municipal securities professional buying securities from a customer should obtain sufficient information about the securities so that it can accurately describe these securities when the dealer reintroduces them into the market.

In regard to inter-dealer transactions, the items of information that professionals must exchange at or prior to the time of trade are governed by principles of contract law and essentially are those items necessary adequately to describe the security that is the subject of the contract. As a general matter, these items of information may not encompass all material facts, but must be sufficient to distinguish the security from other similar issues. The Board has interpreted rule G-17 to require dealers to treat other dealers fairly and to hold them to the prevailing ethical standards of the industry. Also, dealers may not knowingly misdescribe securities to another dealer. *MSRB interpretation of April 30, 1986.*

Purchase of new issue from issuer. This is in response to your letter in which you ask whether Board rule G-17, on fair dealing, or any other rule, regulation or federal law, requires an underwriter to purchase a bond issue from a municipal securities issuer at a "fair price."

Rule G-17 states that, in the conduct of its municipal securities business, each broker, dealer and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice. Thus, the rule requires dealers to deal fairly with issuers in connection with the underwriting of their municipal securities. Whether or not an underwriter has dealt fairly with an issuer is dependent upon the facts and circumstances of an underwriting and cannot be addressed simply by virtue of the price of the issue. For example, in a competitive underwriting where an issuer reserves the right to reject all bids, a dealer submits a bid at a net interest cost it believes will enable it to successfully market the issue to investors. One could not view a dealer as having violated rule G-17 just because it did not submit a bid that the issuer considers fair. On the other hand, when a dealer is negotiating the underwriting of municipal securities, a dealer has an obligation to negotiate in good faith with the issuer. If the dealer represents to the issuer that it is providing the best market price available on this issue, and this is not the case, the dealer may violate rule G-17. Also, if the dealer knows the issuer is unsophisticated or otherwise depending on the dealer as its sole source of market information, the dealer's duty under rule G-17 is to ensure that the issuer is treated fairly, specifically in light of the relationship of reliance that exists between the issuer and the underwriter. *MSRB interpretation of December 1, 1997.*

See also:

Rule G-15 Interpretive Letters — Callable securities: pricing to call and extraordinary mandatory redemption features, *MSRB interpretation of February 10, 1984.*

- **Callable securities: pricing to mandatory sinking fund calls,** *MSRB interpretation of April 30, 1986.*
- **Disclosure of pricing: calculating the dollar price of partially prerefunded bonds,** *MSRB interpretation of May 15, 1986.*
- **Disclosure of investment of bond proceeds,** *MSRB interpretation of August 16, 1991.*
- **Securities description: prerefunded securities,** *MSRB interpretation of February 17, 1998.*

Rule G-21 Interpretive Letters — Disclosure obligations, *MSRB interpretation of May 21, 1998.*

- **529 college savings plan advertisements,** *MSRB interpretation of May 12, 2006.*

Rule G-17 Amendment History (since 2003)

Release No. 34-72129 (May 8, 2014), 79 FR 27662 (May 14, 2014); MSRB Notice 2014-11 (May 12, 2014)

Release No. 34-67064 (May 25, 2012), 77 FR 32704 (June 1, 2012); MSRB Notice 2012-27 (May 29, 2012)

Release No. 34-66927 (May 4, 2012), 77 FR 27509 (May 10, 2012); MSRB Notice 2012-25 (May 7, 2012)

Release No. 34-63599 (December 22, 2010), 75 FR 82199 (December 29, 2010); MSRB Notice 2010-59 (December 23, 2010)

Release No. 34-62715 (August 13, 2010), 75 FR 51128 (August 18, 2010); MSRB Notice 2010-26 (August 15, 2010)

Release No. 34-60359 (July 21, 2009), 74 FR 37079 (July 27, 2009); MSRB Notice 2009-42 (July 14, 2009)

Release No. 34-53959 (June 8, 2006), 71 FR 34654 (June 15, 2006); MSRB Notice 2006-16 (June 15, 2006)

Release No. 34-51020 (January 11, 2005), 70 FR 3079 (January 19, 2005); MSRB Notice 2005-01 (January 5, 2005)

Rule G-18
Best Execution

(a) In any transaction in a municipal security for or with a customer or a customer of another broker, dealer, or municipal securities dealer ("dealer"), a dealer must use reasonable diligence to ascertain the best market for the subject security and buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions. Among the factors that will be considered in determining whether a dealer has used "reasonable diligence," with no single factor being determinative, are:

(1) the character of the market for the security (e.g., price, volatility, and relative liquidity);

(2) the size and type of transaction;

(3) the number of markets checked;

(4) the information reviewed to determine the current market for the subject security or similar securities;

(5) the accessibility of quotations; and

(6) the terms and conditions of the customer's inquiry or order, including any bids or offers, that result in the transaction, as communicated to the dealer.

(b) In any transaction for or with a customer or a customer of another dealer, a dealer must not interject a third party between itself and the best market for the subject security in a manner inconsistent with paragraph (a) of this rule.

(c) The obligations described in paragraphs (a) and (b) above apply to transactions in which the dealer is acting as agent and transactions in which the dealer is acting as principal. These obligations are distinct from the fairness and reasonableness of commissions, markups or markdowns, which are governed by Rule G-30.

Supplementary Material

.01 Purpose. The principal purpose of this rule is to promote, for customer transactions, dealers' use of reasonable diligence in accordance with paragraph (a). A failure to have actually obtained the most favorable price possible will not necessarily mean that the dealer failed to use reasonable diligence.

.02 Maintenance of Adequate Resources. A dealer's failure to maintain adequate resources (*e.g.*, staff or technology) is not a justification for executing away from the best available market. The level of resources that a dealer maintains should take into account the nature of the dealer's municipal securities business, including its level of sales and trading activity.

.03 Execution of Customer Transactions. A dealer must make every effort to execute a customer transaction promptly, taking into account prevailing market conditions. In certain market conditions a dealer may need more time to use reasonable diligence to ascertain the best market for the subject security.

.04 Definition of "Market." The term "market" or "markets," for the purposes of this rule, unless the context requires otherwise, encompasses a variety of different venues, including but not limited to broker's brokers, alternative trading systems or platforms, or other counterparties, which may include the dealer itself as principal. The term is to be construed broadly, recognizing that municipal securities currently trade over the counter without a central exchange or platform. This expansive interpretation is meant both to inform dealers as to the breadth of the scope of venues that must be considered in the furtherance of their best-execution obligations and to promote fair competition among dealers (including broker's brokers), alternative trading systems and platforms, and any other venue that may emerge, by not mandating that certain trading venues have less relevance than others in the course of determining a dealer's best-execution obligations.

.05 Best Execution and Executing Brokers. A dealer's duty to provide best execution in any transaction "for or with" "a customer of another dealer" does not apply in instances when the other dealer is simply executing a customer transaction against the dealer's quote. A dealer's duty to provide best execution to customer orders received from other dealers arises only when an order is routed from another dealer to the dealer for handling and execution.

.06 Securities with Limited Quotations or Pricing Information. Although the best-execution requirements in this rule apply to transactions in all municipal securities (other than municipal fund securities), markets for municipal securities may differ dramatically. One of the areas in which a dealer must be especially diligent in ensuring that it has met its best-execution obligations is with respect to customer transactions involving securities for which there is limited pricing information or quotations available. Each dealer must have written policies and procedures in place that address how the dealer will make its best-execution determinations with respect to such a security in the absence of pricing information or multiple quotations and must document its compliance with those policies and procedures. For example, a dealer generally should seek out other sources of pricing information and potential liquidity for such a security, including other dealers that the dealer previously has traded with in the security. Additionally, a dealer generally should, in determining whether the resultant price to the customer is as favorable as possible under prevailing market conditions, analyze other data to which it reasonably has access.

.07 Customer Instructions Regarding Handling of Bids or Offers. If a dealer receives an unsolicited instruction from a customer designating a particular market for the execution of the customer's transaction, the dealer is not required to make a best-execution determination beyond the customer's specific instruction. Dealers are, however, still required to process that customer's transaction promptly and in accordance with the terms of the customer's bid or offer.

.08 Review of Policies and Procedures and Execution Quality.

(a) A dealer must, at a minimum, conduct annual reviews of its policies and procedures for determining the best available market for the executions of its customers' transactions. While no more frequent interval is specifically required, a dealer must conduct these reviews at a frequency reasonably related to the nature of its municipal securities business, including but not limited to its level of sales and trading activity. In conducting its periodic reviews, a dealer must assess whether its policies and procedures are reasonably designed to achieve best execution, taking into account the quality of the executions the dealer is obtaining under its current policies and procedures, changes in market structure, new entrants, the availability of additional pre-trade and post-trade data, and the availability of new technologies, and to make promptly any necessary modifications to such policies and procedures as may be appropriate in light of such reviews.

(b) A dealer that routes its customers' transactions to another dealer that has agreed to handle those transactions as agent or riskless principal for the customer (*e.g.*, a clearing firm or other executing dealer) may rely on that other dealer's periodic reviews as long as the results and rationale of the review are fully disclosed to the dealer and the dealer periodically reviews how the other dealer's review is conducted and the results of the review.

.09 Exemption for Municipal Fund Securities. The provisions of this rule do not apply to transactions in municipal fund securities.

Rule G-18 Interpretations

Implementation Guidance on MSRB Rule G-18, on Best Execution

(As updated February 7, 2019)

Background

MSRB Rule G-18, establishing the first best-execution rule for transactions in municipal securities, became effective March 21, 2016. The best-execution rule requires brokers, dealers and municipal securities dealers (dealers) to use reasonable diligence to ascertain the best market for the subject security and buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions. Related amendments to MSRB Rule G-48, on transactions with sophisticated municipal market professionals (SMMPs), and to MSRB Rule D-15, on the definition of an SMMP, exempt transactions with SMMPs from the best-execution rule. This implementation guidance provides answers to frequently asked questions about the best-execution rule and the SMMP exemption.

Use of This Document

The MSRB is providing in this document general implementation guidance on certain aspects of new Rule G-18 and amended Rules G-48 and D-15 (rules) in a question-and-answer format. This guidance is designed to support compliance with the best-execution rule and the SMMP exemption.[1] The answers are not considered rules and have neither been approved nor disapproved by the Securities and Exchange Commission (SEC).

The MSRB may update these questions and answers periodically, and any updates will include appropriate references to dates of new or modified questions and answers.

Questions and Answers Concerning Best Execution and the Exemption for Transactions with Sophisticated Municipal Market Professionals: Rules G-18, G-48 and D-15

I. Best-Execution Standard — General

I.1: Reasonable Diligence

Q: What do dealers need to do to use reasonable diligence when selling (purchasing) municipal securities out of (into) their inventory to (from) customers[2] who are not sophisticated municipal market professionals (SMMPs)?[3]

A: *Overview of Best-Execution Standard*. Section (a) of MSRB Rule G-18, on best execution, requires dealers, in any transaction for or with a customer or a customer of another dealer, to use reasonable diligence to ascertain the best market for the subject security and to buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions. This obligation applies to transactions in which the dealer is acting as agent and transactions in which the dealer is acting as principal.[4] Section (a) includes a non-exhaustive list of factors that dealers must consider when exercising this diligence, which includes: the character of the market for the security (*e.g.*, price, volatility, and relative liquidity), the size and type of transaction, the number of markets checked, the information reviewed to determine the current market for the subject security or similar securities, the accessibility of quotations, and the terms and conditions of the customer's inquiry or order, including any bids or offers, that result in the transaction, as communicated to the dealer. A dealer must make every effort to execute a customer transaction promptly,[5] but the determination as to whether a firm exercised reasonable diligence necessarily involves a "facts and circumstances" analysis, and actions that in one instance may meet a dealer's best-execution obligation may not satisfy that obligation under another set of circumstances. The rule is designed to complement existing fair and reasonable pricing standards and improve execution quality for retail investors in municipal securities, while promoting fair competition among dealers and improving market efficiency.