Ballard Spahr LLP

Municipal Securities Regulation & Enforcement

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The first half of 2020 was marked by the outbreak of COVID-19, an infectious respiratory disease caused by a novel strain of coronavirus, which the World Health Organization declared a global pandemic. COVID-19 affected travel, commerce, the economy, and financial markets in the United States and globally. As a result, the municipal securities market scrambled to adapt to a rapidly changing landscape from financial, operating, and regulatory aspects.

The SEC continued its push to enhance municipal disclosure practices, especially in the light of the pandemic. The agency granted a much-anticipated temporary conditional exemptive order, allowing registered municipal advisors to undertake certain solicitation activities for the first time. A federal district court applied the Reves test to a widely syndicated loan, FINRA best-execution enforcement is on the uptick, and the MSRB continues to actively push its agenda forward while offering pandemic-related relief and guidance to market participants.

FOCUS ON MUNICIPAL SECURITIES DISCLOSURE

In the midst of the pandemic, the SEC maintained its focus on municipal disclosure. The Office of Municipal Securities (OMS) published its Staff Legal Bulletin (SLB) on February 7, 2020, on the application of antifraud provisions to public statements of issuers and obligated persons of municipal securities in the secondary market. In the SLB, the SEC clarified its view that any public statement made by issuers of municipal securities and obligated persons, including elected governmental officials, that is reasonably expected to reach investors and the trading markets, is subject to the same antifraud standards applicable to primary offerings. Read our white paper on the SLB for more information on antifraud provisions and disclosure considerations.

Additionally, at the SEC Fixed Income Market Structure Advisory Committee (FIMSAC) meeting on February 10, 2020, FIMSAC recommended that the SEC be given additional statutory authority to enforce compliance with continuing disclosure agreements, and that a mechanism be provided for the SEC to enforce compliance with continuing disclosure agreements and other obligations of municipal issuers to protect municipal securities bondholders. While the buy-side community was generally supportive, the issuer community is concerned this a first step to eroding the protection of the Tower Amendment.

FIMSAC also recommended the SEC be given additional statutory authority to provide a safe harbor from private liability for forward-looking statements for municipal issuers that satisfy certain conditions, and that the SEC explore options through which it could make Rule 15c2-12 disclosure deadlines more certain and predictable.

On March 25, 2020, the SEC Division of Corporation Finance released CF Disclosure Guidance: Topic No. 9, providing the Division of Corporation Finance's views regarding disclosure and other securities law obligations to consider with respect to COVID-19. While this guidance was directed toward corporate issuer disclosure, it includes questions that any issuer should consider related to present and future financial and operational conditions due to COVID-19. Assessing the evolving effects of COVID-19 and related risks is a facts-and-circumstances analysis, regardless of the type of issuer.

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Read our e-alert on municipal disclosure during the time of COVID-19 for more information on disclosure guidance as it relates to the impacts of COVID-19.

To further the emphasis on forward-looking disclosure, SEC Chairman Jay Clayton and Rebecca Olsen, Director of the Office of Municipal Securities, issued a public statement (Public Statement) on May 4, 2020, encouraging issuers to disclose future prospects voluntarily regarding financial and operating status, in light of the economic and operational effects and uncertainties created by COVID-19. The Public Statement included examples of types of COVID-19-related disclosures the SEC believes would be most beneficial for investors and the marketplace, and set forth certain factors in favor of providing voluntary forward-looking disclosures. Read our e-alert for more information on the Public Statement and factors to consider when making primary offering and secondary market disclosures.

On June 16, 2020, the SEC held its rescheduled "Spotlight on Transparency: A Discussion of Secondary Market Municipal Securities Disclosure Practices" conference. Discussion covered voluntary disclosure practices, buy-side perspectives on secondary market disclosure, and hot topics in the area of secondary market disclosure, including COVID-19-related disclosures, and reemphasized the SEC's recent focus on more disclosure and more timely disclosure, and voluntary forward-looking disclosure due to the impacts of COVID-19.

Municipal Advisor Exemption From Broker-Dealer Registration Requirements

The SEC's proposed exemptive order (Proposed Order) on October 2, 2019, granting a conditional exemption from the broker registration requirements of Section 15(a) of the Securities and Exchange Act of 1934 (Exchange Act) for certain activities of registered municipal advisors, including acting as a placement agent in connection with the direct placement of municipal securities, continues to be a point of concern for many market participants. In October 2018, PFM Financial Advisors LLC (PFM), sought interpretive guidance from the SEC's Division of Trading and Markets and the SEC's Office of Municipal Securities that a non-dealer municipal advisor would not be required to register as a broker-dealer if it engages in certain specified activities related to direct placements of municipal debt. Since regulators generally consider placement agent activity to be broker-dealer activity, this request has trained a bright light on the respective duties and obligations of separately regulated entities in connection with the issuance of municipal securities.

Several municipal market participants, including the Securities Industry and Financial Markets Association (SIFMA) and the Bond Dealers of America, submitted letters to the SEC in June 2019 asking that PFM's request be denied because the Proposed Order would upend long settled rules while diluting the investor protections embedded in the broker dealer regulatory regime, among other objections. Despite such opposition, the SEC went ahead with the Proposed Order and another round of comments were due on December 9, 2019. In late January 2020, both SIFMA and the Bond Dealers of America made further attempts to squash, and if not successful, limit the Proposed Order to apply only in cases of single large sophisticated investors, suggesting requiring certain written disclosures to investors, requiring disclosure to issuer clients that they can choose to work with a dealer placement agent, prohibiting municipal advisors from representing obligated persons, limiting the scope of the proposal to small issuers or small issues, and delaying the effective date of any rule change until the MSRB rules are updated in conformity to allow for the new exemption to broker-dealer registration.

Despite a number of letters in opposition to the Proposed Order, on June 16, 2020, the SEC granted a temporary conditional exemption (Temporary Order) from broker registration under Section 15 of the Exchange Act, stating that the Temporary Order is intended to address disruption in the municipal securities markets as a result of the COVID-19 pandemic. The Temporary Order is in some ways narrower than Proposed Order. In its statements releasing the Temporary Order, the SEC stated that it decided not to move forward with the Proposed Order "at this time," and left open the possibility that it will be revived in some form in the future. The Temporary Order is effective from June 16, 2020, until December 31, 2020.

Subject to certain conditions described in the Temporary Order and in our June 30, 2020, alert, the Temporary Order exempts municipal advisors from the registration requirement by allowing them to solicit banks, their wholly owned subsidiaries engaged in commercial lending and financing activities, and credit unions in connection with direct placements of securities issued by their municipal issuer clients in their capacity as municipal advisors.

While the Temporary Order normally would not be available to dealer-affiliated municipal advisors acting as placement agents (since MSRB Rule G-23—which applies only to dealer-affiliated municipal advisors—prohibits a dealer municipal advisor from acting as placement agent and a municipal advisor on the same transaction) the MSRB released guidance

removing the applicability of Rule G-23. Under the MSRB guidance, since municipal advisors relying on the Temporary Order are permitted simply to perform an additional activity in their capacity as municipal advisors (solicitation of certain purchasers), they are not acting as placement agents and not subject to MSRB Rule G-23. A discussion of the Rule G-23 guidance is below.

The SEC conducted a Virtual Discussion – Temporary Conditional Order for Municipal Advisory Activities on July 7, 2020, on the Temporary Order in which members of the SEC and MSRB provided compliance and interpretative guidance on the timing of the disclosures, the expiration date of the Temporary Order, recommended changes to supervisory procedures, disclosures to issuers, the application of other MSRB rules, the par limitation and documenting compliance with the Temporary Order.

The Temporary Order leaves unaddressed the question of how to determine whether direct placement instruments and the financing participants are subject to federal regulation as securities in the first place if they are unregulated loans and not securities. This ambiguity has been a critical, but as yet unresolved, issue for dealers and municipal advisors who need to know which laws to apply to their transactions. We include a discussion of the latest case law developments in the classification of securities versus loans below.

Spotlight – Kirschner v. JPMorgan Chase Bank, N.A.: *Loan or Security?*

In recent litigation in the U.S. District Court for the Southern District of New York, the court ruled that a syndicated loan was not a security. In Kirschner v. JPMorgan Chase Bank, N.A., the court dismissed claims on a motion to dismiss against a number of banks, ruling that securities law claims against the defendants could not stand because the $1.775 billion syndicated institutional loan to the borrower was not a security. Sales of the syndicated loan were limited to sophisticated institutions with a minimum loan size of $1 million and sold to 400 mutual funds, hedge funds, and other investors. The transaction included several broker-dealers acting as arrangers. The court applied the "family resemblance test" set forth in Reves v. Ernst & Young, 494 US 56 (1994), which held that a note is presumptively a security, a presumption which may be rebutted by a showing that the note bears a strong "family resemblance" to a number of instruments commonly denominated as notes that fall outside of the security category. The court found that the second, third, and fourth Reves factors, discussed below, weighed in favor of finding the notes analogous to "the enumerated category of loans issued by banks for commercial purposes," and were therefore not securities.

In applying the first Reves factor, "the motivations that would prompt a buyer and a seller to enter into a transaction," the court found mixed motivations, because although the seller's motivation was to advance a commercial purpose other than investment (as the seller used the loan for repayment of an older loan and a dividend), the buyer's purpose was investment. On the second Reves factor, "the plan of distribution," the court compared the distribution to a public distribution and found it "relatively narrow" and noted that the initial purchase requirement of $1 million, coupled with transfer restrictions including the consent of the lender group, would limit public access to the instrument. In applying the third Reves factor, "the reasonable expectations of the investing public," the court found that the terms "loan," "lender," and "loan documents" were rife throughout the Credit Agreement and the Confidential Informational Memorandum, which put lenders on notice that they were lending money, not purchasing securities. In applying the fourth Reves factor, "whether there exists another regulatory scheme to reduce the risk of the instrument, thereby rendering the application of the Securities Act unnecessary," the court made reference to an earlier case, Banco Espanol, in remarking that loan participations to sophisticated purchasers are subject to policy guidelines from the Comptroller of the Currency. The characterization of the loan to a security would have made participants in the financing immediately subject to far-reaching state and federal securities laws and liabilities.

ENFORCEMENT ACTIONS – MID-YEAR REVIEW

FINRA Bars Chief Compliance Officer From Association With a FINRA Member for Misrepresentations Made to FINRA in Response to a FINRA Inquiry

The Financial Industry Regulatory Authority (FINRA) settled charges against a firm's chief compliance officer (CCO) for allegedly violating FINRA Rules 8210 and 2010 by misrepresenting to FINRA the frequency of the supervisory review of trade reporting compliance of municipal securities. FINRA alleged the firm failed to report 47 municipal

transactions within 15 minutes of trade execution over a three-month period in 2016. The CCO allegedly falsely represented that he reviewed trades monthly, but in fact was only reviewing municipal trade reporting on a quarterly basis at most. FINRA also alleged the CCO altered documents he produced to FINRA during the investigation to conceal his prior misstatement. Without admitting or denying the findings, the CCO consented to a bar from association with any FINRA member firm in any capacity.

FINRA Fines Investment Bank for Violating Rule G-15(f) on Minimum Denominations

On January 3, 2020, FINRA settled charges against a large investment bank for executing more than 105 municipal bond trades below the issue's minimum denomination and for failing to inform 20 customers of potential liquidity consequences over a three-year period from July 1, 2015, through June 30, 2018. MSRB Rule G-15(f) prohibits a broker, dealer, or municipal securities dealer from effecting a customer trade in municipal securities in an amount lower than the minimum authorized denomination. Rule G-15(f) provides limited exceptions to the requirement to effect a trade in amounts equal to or higher than the minimum authorized denomination; however, FINRA stated that in 105 instances, the investment bank executed municipal securities trades in amounts lower than the minimum authorized denomination without an exception. Additionally, FINRA alleged the investment bank failed to disclose to customers at or prior to the time of trade that the transactions were in amounts lower than the issue's minimum authorized denomination, thereby violating MSRB Rule G-47. Without admitting or denying the findings, the investment bank consented to a censure and a fine of $150,000.

FINRA Fines Broker-Dealer Firms for Violations of Best Execution and Excessive Mark-Ups

On January 3, 2020, FINRA settled charges against a broker-dealer firm for failing to exercise reasonable diligence in determining the best market and to sell in such market in order to get the most favorable pricing for its customers, in violation of MSRB Rules G-17, G-18, G-27, and G-30. A broker-dealer is required to use reasonable diligence to ascertain the best market for the security, and buy or sell in that market in order to get the most favorable price at prevailing market conditions for its customer. There are a number of "best execution" factors to consider when exercising reasonable diligence, including the character of the market for the security, the size and type of the transaction, the information reviewed to check the market, the number of markets checked, the accessibility of quotations and the terms and conditions of the customer's order. FINRA alleged that in 11 instances, the broker-dealer relied solely on a vendor's proprietary yield curve to determine transaction price, failed to consider all factors, and ignored contemporaneous inter-dealer transactions. FINRA also alleged the broker-dealer did not charge a fair and reasonable price in those 11 transactions and charged its customers unfair and unreasonable markups. Finally, FINRA alleged the broker-dealer failed to establish, maintain, and enforce written policies and procedures concerning best execution obligations and maintained no evidence that it conducted periodic reviews to assess the reasonableness of its policies or describe how a principal could monitor compliance. Without admitting or denying the findings, the broker-dealer consented to a censure, a total fine of $35,000, and an undertaking to revise the broker-dealer's written supervisory policies and procedures.

In another best execution case, on March 23, 2020, FINRA also settled charges against a firm for failing to purchase municipal securities for its customers at prices that were fair and reasonable in relation to prevailing market conditions, in violation of MSRB Rules G-17 and G-30. FINRA alleged that the firm bought municipal securities for its customers from an unaffiliated broker-dealer that was a counterparty for nearly all of its municipal securities transactions and that the firm did not consider other prices from other broker-dealers. FINRA also alleged the firm focused its supervisory pricing reviews on aggregated data that obscured information about individual transactions and failed to maintain written supervisory procedures with respect to periodic review of the firm's pricing across all of its municipal security transactions. In addition, FINRA cited the firm for not stating in its procedures how a designated principal shall monitor compliance with Rule G-30(b)(i)'s requirement to make a reasonable effort to obtain a price for the customer that is fair and reasonable in relation to prevailing market conditions. Without admitting or denying the findings, the firm consented to censure, a fine of $100,000, and payment of restitution (which it had already paid).

FINRA Fines Broker for Failure to Obtain Customer Acknowledgements

On March 24, 2020, FINRA settled charges against an individual broker for failing to obtain written customer acknowledgements and his firm's written approval for agency cross transactions in municipal securities between his firm's member customers, in violation of MSRB Rule G-17 requiring a dealer to deal fairly with all persons in the conduct of its

municipal securities activities. FINRA alleged that from October 31, 2017, through February 13, 2018, the firm's policies required registered representatives to obtain such consents prior to effecting any agency cross transactions between firm customers. During that time period, however, the broker effected 56 pairs of agency cross transactions and, FINRA alleged, did not deal fairly with all persons, in violation of Rule G-17. Without admitting or denying the findings, the broker consented to a fine of $5,000 and a suspension from association with any FINRA member in all capacities for fifteen business days.

FINRA Fines Broker-Dealer for Simultaneous Representation as Underwriter and Financial Advisor

On March 25, 2020, FINRA settled charges against a broker-dealer firm for providing underwriting services for a municipal issuer with which it had an active "blanket" financial advisory agreement in place, in violation of MSRB Rule G-23. Rule G-23 prohibits broker-dealers from acting simultaneously as the issuer's financial adviser and its underwriter to avoid a prima facie conflict of interest. The broker-dealer's blanket financial advisory agreement was not limited to specific issuances of bonds, but rather applied to all potential methods of financing capital improvement programs and review of possible projected revenue sources and the most appropriate sources to pay for any proposed capital improvement financing programs. Without admitting or denying the findings, the firm consented to a censure and a $10,000 fine.

FINRA Fines Broker-Dealer Firm for Failure to Timely Report Municipal Securities Transactions

On March 25, 2020, FINRA settled charges against a broker-dealer firm for late and inaccurate trade reporting of municipal securities transactions to RTRS during the periods of January 1, 2016, through March 31, 2016, and July 1, 2016, through December 31, 2016, in violation of MSRB Rule G-14 (b). Rule G-14 requires brokers, dealers or municipal securities dealers to report to the RTRS information concerning each purchase or sale of municipal securities promptly, accurately, and completely within 15 minutes of the time of trade (with limited exceptions). FINRA alleged that during the relevant time periods, the firm failed to report 126 large block municipal transactions (17.1% of the total number of large block municipal securities transactions reported during the relevant periods) within the time period required under Rule G-14. Without admitting or denying the findings, the firm consented to a censure, a $30,000 fine and written certification that the firm has reviewed its systems, policies, and procedures governing the firm's trade reporting of fixed income securities and that they are reasonably designed to achieve compliance with MSRB Rule G-14.

FINRA Fines Broker-Dealer for Failure to Report Variable Rate Demand Obligation Information

On May 7, 2020, FINRA settled charges against a broker-dealer firm for failing to submit accurate information to the MSRB's Short-Term Obligation Rate Transparency (SHORT) system, in violation of MSRB Rules G-34. Rule G-34 requires remarketing agents to submit variable rate demand obligation interest rate reset information, including minimum denominations and maximum interest rates, to the SHORT System by a certain time, based on the day and time at which the interest rate reset occurs. FINRA alleged that from March 18, 2009, through March 29, 2018, the firm failed to submit accurate information in several thousand submissions, with error rates from 2.94% to 3.35%. FINRA found that the firm's internal reporting system did not require the entry of minimum denominations and maximum interest rate, and that those fields were mistakenly left blank. FINRA also alleged the firm did not maintain an adequate supervisory system, in violation of MSRB Rule G-27. Without admitting or denying the findings, the firm consented to a censure and a fine of $47,500.

In a similar case, on June 29, 2020, FINRA settled charges against another broker-dealer remarketing agent for failing to submit the minimum denominations and maximum interest rates to the MSRB's SHORT system, in violation of MSRB Rule G-34, for a portion of their submissions from April 1, 2011, through March 15, 2018. FINRA stated that the reporting failures occurred because the firm's reporting system did not require the entry of these fields. Without admitting or denying the findings, the firm consented to a censure and a fine of $35,000.

SEC Settles Charges in California Charter School Fraud

On April 27, 2020, the SEC filed a complaint against two individuals: the chief executive officer and the director of finance of a corporation that operated two public charter schools in California, alleging violations of Section 17(a)(3) of the Securities Act.

According to the complaint, the corporation issued $25 million in bonds through a conduit issuer in May 2015 to purchase and renovate a building that would house the public charter schools

operated by the corporation and another private high school (Cal Prep). The chief executive officer of the corporation was also the founder and manager of Cal Prep. The SEC alleged that the Limited Offering Memorandum (LOM) distributed to potential investors in connection with the offering failed to disclose that the corporation was experiencing severe financial distress and included misleading financial projections. The two individuals charged in the complaint helped prepare the LOM, signed the LOM, and also executed certificates for the underwriter stating that the LOM contained no material misrepresentations or omissions. The corporation filed for bankruptcy in November 2016 and the bonds defaulted in 2017. In the complaint, the SEC alleged that the chief executive officer and director of finance misled investors about the corporation's dire financial condition.

Without admitting or denying the allegations in the complaint, the chief executive officer and director of finance settled with the SEC, agreeing to be enjoined from future violations of the anti-fraud provisions in Section 17(a)(3) of the Securities Act and from participating in future municipal bond offerings. The chief executive officer agreed to pay a $20,000 penalty, and the director of finance agreed to pay a $15,000 penalty.

Whistleblower VRDO Cases – Awaiting Decisions

As described in our 2019 Year-End Newsletter, lawsuits were filed in California, Illinois, Massachusetts, and New York (joined with suits filed by the Cities of Philadelphia and Baltimore) alleging fraud by several investment banks acting as remarketing agents in the VRDO market. The dealer firms allegedly promised to use their judgment to market and price the bonds at the lowest possible interest rates. Rather than resetting the rates individually as required, the banks are charged with engaging in a scheme to "mechanically set the rates en masse without due consideration of the individual characteristics of the bonds or the associated market conditions," thereby resulting in artificially high rates. Plaintiffs claim the higher interest rates then discouraged VRDO investors from redeeming the bonds.

On July 23, 2019, the Massachusetts Superior Court dismissed the Massachusetts lawsuit on the basis that the "public disclosure bar," a legal standard existing to prevent whistleblowers from filing lawsuits supported by information that was already known to the public, applies to the allegations. On January 10, 2020, Johan Rosenberg, the municipal advisor accusing major banks of widespread fraud in the VRDO cases, filed an appeal with the Commonwealth of Massachusetts Appeals Court.

On February 14, 2020, the office of New York Attorney General Letitia James blocked the dismissal of the New York lawsuits based on the defendant banks' motion to dismiss on the "public disclosure bar" grounds. This defense was successful in the Massachusetts Superior Court for dismissal of the Massachusetts lawsuit on July 23, 2019. In late March 2020, the New York Supreme Court dismissed another motion to dismiss, finding that the lawsuit sufficiently alleges violations of New York's false claims act to avoid being dismissed.

On July 16, 2019, an Illinois intermediate appellate court denied a motion for interlocutory appeal filed by some of the investment banks named in the lawsuits on the basis that "there is substantial ground for difference of opinion as to whether the trial court should consider the nature of the information relied upon in deciding the original-source question." In April 2020, the State of Illinois blocked dismissal of the lawsuit on public disclosure grounds, similar to the case in New York.

In late July 2019, attorneys for several of the banks filed a motion to dismiss the New York, Philadelphia, and Baltimore lawsuits in the U.S. District Court for the Southern District of New York. Responses to the motion to dismiss were filed in October and November by attorneys for the Cities of Philadelphia and Baltimore, and the Edelweiss Fund with respect to the New York lawsuit.

The California Superior Court ruled that the complaint needed more specificity before allowing the court to consider it further, and asked the plaintiffs to file an amended complaint by October 8, 2019. The amended complaint contains additional detail regarding remarketing reset rates and the alleged "bucketing" of VRDOs.

MSRB ACTIONS – MID-YEAR REVIEW

The following summarizes MSRB actions in the first half of 2020.

MSRB Files Proposed Changes to Its Governance Rules

On January 28, 2020, the MSRB published a request for comment on draft amendments to MSRB Rule A-3: Membership on the Board. The MSRB established a 60-day comment period, with an extension due to COVID-19, ending April 23, 2020, for its proposal for potential amendments to its rule establishing the parameters for composition and selection of its Board of Directors. On June 5, 2020, the MSRB filed

the proposed amendments to MSRB Rules A-3 and A-6, including (1) extending the separation period for public representatives with past associations with regulated entities from two years to five years to better avoid any appearance of a conflict of interest without significantly decreasing the qualified pool of individuals; (2) reducing the board size from 21 to 15 members; (3) changing the required composition of the regulated representatives on the board from a requirement that 30% of the regulated representatives be municipal advisors to two of the regulated representatives be municipal advisors; and (4) limiting the term of board members to no more than six years total.

MSRB to Add "Submission Calculator" to EMMA

On February 18, 2020, the SEC approved the MSRB's proposed rule change to amend the information facility of the MSRB's Electronic Municipal Market Access (EMMA) to provide for, among other things, a "submission calculator" that would reflect the automated calculation and static display of the number of days between the annual fiscal period end date for an issuer or obligated person and the date an annual financial disclosure is submitted to the EMMA system for the period. The proposed rule change was approved despite concerns from some market participants that there is a high risk that a meaningful number of calculations will be based on inaccurate information, and that some issuers would be unfairly judged by investors despite submission of information within the timeframe required in their continuing disclosure agreements. In the approval order, the SEC notes that the "Submission Calculator" would "enable investors and others to more readily locate and access the financial information available on the EMMA Portal and provide investors and others with additional tools to evaluate an issuer's disclosure practices." The effective date for the implementation of the submission calculator" was July 1, 2020.

MSRB Reminds Regulated Entities of the Application of Supervisory Requirements in Light of COVID-19

On March 9, 2020, the MSRB issued Notice 2020-07 to address concerns relating to business and operational challenges caused by COVID-19. MSRB Rule G-27 requires brokers, dealers and municipal securities dealers to supervise the conduct of the municipal securities activities of the dealer and that of its associated persons to ensure compliance with MSRB rules and applicable provisions of the Exchange Act. The MSRB highlights that, "Rule G27 does not mandate that supervision be done in-person," and recognizes that technology plays a role in how dealers conduct their supervisory reviews, allowing for remote supervision under reasonably designed supervisory systems. It is also noted that Rule G-44 governing supervisory and compliance obligations of municipal advisors does not mandate in-person supervision and likewise may incorporate remote supervision into a reasonably designed supervisory system.

MSRB Takes Regulatory Action in Response to COVID-19

Given market volatility caused by the impact of COVID-19, MSRB announced it was temporarily suspending the transmission of the price variance alerts for trade reports to MSRB's Real-Time Transaction Reporting System (RTRS) effective March 23, 2020. The MSRB sends dealers a price variance alert when a transaction is reported in RTRS as a price notably higher or lower than the price reported by other dealers in the same security within a certain time period, in order to assist dealers in identifying trades that may need to be reviewed for accuracy and complying with MSRB Rule G-14. The MSRB determined that, given the market conditions at the time, the price variance alert tool was not serving its intended purpose of helping dealers to comply with Rule G-14. Although the price variance alert tool is suspended, dealers remain obligated to comply with Rule G-14 to ensure information being reported on RTRS is accurate.

On April 9, 2020, the MSRB filed a proposed rule change with the SEC seeking immediate authorization to provide temporary regulatory relief to market participants by extending certain compliance dates and late fees in response to the impact of COVID-19 on municipal market participants. The proposed rule change makes the following changes:

1. Temporarily suspends late fees under MSRB Rule A-11 on assessments for municipal advisor professionals for annual municipal advisor professional fees owed for MSRB Fiscal Year 2020, under MSRB Rule A-12 on fees assessed under the rule, and for fees assessed under MSRB Rule A-13 on underwriting and transaction assessments for brokers and dealers. The suspension relates to fees billed by the MSRB (or come due) during the period from March 1, 2020, through July 31, 2020.

2. Extends time to complete certain supervisory functions under MSRB Rule G-27 on supervision and MSRB Rule G-44 on supervisory and compliance obligations of municipal advisors to be completed on or before March 31, 2021.

3. Extends time to complete certain professional qualification standards established under MSRB Rule G-3 on professional qualification requirements, consistent with MSRB guidance.

4. Extends previously announced compliance dates for MSRB Rule G-17 amendments to interpretive guidance and Form G-32 compliance, each from November 30, 2020, to March 31, 2021. The MSRB is discouraging firms from implementing the G-17 amendments prior to the extended implementation date to avoid confusing recipients of the disclosure.

On May 28, 2020, the MSRB announced it was waiving market activity fees for transactions with the Municipal Liquidity Facility. The MSRB filed a proposed rule change with the SEC to provide temporary relief to waive the assessment of market activities fees for transactions with the Municipal Liquidity Facility established by the Board of Governors of the Federal Reserve System, including underwriting fee amounts, transaction fees, and technology fees. The fee waiver is intended to be temporary and expire at the same time that the Municipal Liquidity Facility expires.

MSRB Files Proposed Amendments to Align With SEC Regulation Best Interest

On May 1, 2020, the MSRB filed proposed amendments to align MSRB rules with the requirements of SEC Regulation Best Interest (Reg B-I). The MSRB's proposal is designed to reduce complexity in financial regulation and facilitate compliance with Reg B-I. The proposed rule change consists of amendments to MSRB Rules G-8, G-9, G-19, G-20, and G-48, and the deletion of an interpretation of Rule G-20. Rule G-19 would be amended to apply only in circumstances in which Reg B-I does not apply. Rule G-48 would be amended to clarify that the exception from the requirement to perform a customer-specific suitability analysis when making a recommendation to a sophisticated municipal market professional is available only for recommendations that are subject to Rule G-19. Rule G-20 would be amended to require any permissible non-cash compensation to align with the requirements of Reg B-I. Under the proposed amendments, dealers also would be required to maintain books and records required by Reg B-I and related SEC forms. The effective date for these rule changes was the same as the effective date for Reg B-I: June 30, 2020.

MSRB Releases Guidance on Rule G-23 and the SEC's Temporary Conditional Order

On June 25, 2020, the MSRB released guidance in the form of FAQs addressing the interplay between MSRB Rule G-23 and the Temporary Order. Rule G-23 generally prevents a dealer that has a financial advisory relationship with a municipal entity client with respect to municipal securities from, among other things, role switching to underwriting or acting as a placement agent for the municipal securities. In its FAQs, the MSRB stated that the Temporary Order is available to registered municipal advisors that are also registered dealers, and that a "firm that is registered as both a municipal advisor and a dealer may rely on, and engage in, the activities contemplated by the [Temporary Order] in its role as a municipal advisor without role switching for purposes of MSRB Rule G-23, so long as the firm complies with the conditions set forth in the [Temporary Order]." The MSRB reminded firms of their obligations under the MSRB rules relating to municipal advisory activity when acting in a municipal advisor capacity.

The MSRB's COVID-19 Publications and Resources

In response to the ongoing COVID-19 pandemic, the MSRB has generated a series of publications and resources in service of its mission as the regulatory organization that safeguards the municipal securities market to protect investors, issuers, and the public interest. The MSRB now maintains a COVID-19 website that acts as a repository for all COVID-19-related market data and analysis, notices, resources, and press releases. Below is a sample of these materials.

Daily Market Activity Data Showing Impact of COVID-19

On March 25, 2020, the MSRB began publishing a daily analysis of trade activity to assist market participants, policymakers, and the general public with understanding the impact of COVID-19 on the liquidity of the municipal securities market. The data reflect aggregate trading activity at the end of each trading day as submitted to the RTRS. Each report includes data on (1) overall market trading activity, (2) municipal fixed-rate market trading activity, and (3) municipal variable-rate market trading activity.

Weekly COVID-19-Related Disclosure Summary

The MSRB is monitoring disclosures to the EMMA website and on April 2, 2020, began aggregating links to any disclosures that reference COVID-19. The MSRB has continued publishing this on a weekly basis. The MSRB's

weekly summary provides statistics on the growing number of disclosures from states, municipalities, and other issuers around the country that have felt the impact of COVID-19 on their financial and operating status.

Frequently Asked Questions Related to COVID-19 Pandemic Regulatory Relief

The MSRB is maintaining answers to frequently asked questions (FAQs) to address COVID19 pandemic-related regulatory measures and guidance for brokers, dealers, municipal securities dealers, and municipal advisors in light of disruptions to normal business activities. This resource is meant to be read in conjunction with applicable MSRB rules and interpretations available at http://msrb.org/Rules-and-Interpretations/MSRB-Rules.aspx. Topics covered include professional qualifications, supervision, transaction reporting, mark-up disclosure, best execution and fair pricing, regulatory fees, and additional background and resources.

Market Commentary: Trading in Municipal Bond ETFs During the COVID-19 Crisis

Published in April 2020, MSRB Chief Economist Simon Wu authored a market commentary analyzing how municipal bond fixed-income exchange-traded funds (ETFs) performed in March 2020 in the midst of the COVID-19 crisis. The commentary is an empirical analysis of the price movement of the three most frequently traded municipal bond ETFs: the iShares National Muni Bond ETF (ticker symbol: MUB), the Vanguard Tax-Exempt Bond Index fund ETF (ticker symbol: VTEB), and the VanEck Vector High Yield Municipal Index (ticker symbol: HYD). These ETFs are designed to track a benchmark index closely, with MUB and VTEB tracking the S&P National AMT-Free Municipal Bond Index, and HYD tracking the Bloomberg Barclays Municipal Custom High Yield Composite Index. The data show greater divergence between these ETFs and related indices during March 2020. Wu posits that the price divergence was potentially caused by a liquidity crunch that ultimately impacted high-yield municipal bonds more than investment-grade municipal bonds. Further deterioration in the market was stalled with the announcement on March 20, 2020, by the Federal Reserve Bank that it would begin open market support for the municipal bond market. While there may be other thoughts on why ETFs traded at large discounts during this volatile period, Wu provides the following takeaway for investors: "The degree of price divergence between ETFs and benchmark indices seems to be related to the liquidity of the underlying bonds in the indices, where an illiquid portfolio such as the high-yield municipal bond portfolio exhibited a larger divergence than the more liquid investment-grade municipal bond portfolio."

Market Commentary: COVID-19 Crisis Drives Spike in Transaction Costs

In a May 2020 market commentary published by the MSRB, the authors, Mr. Wu and Nicholas J. Ostroy, analyzed the costs for dealer-to-consumer trades during the market stress period resulting from COVID-19. This commentary extends previous MSRB research conducted in 2018, "Transaction Costs for Consumer Trades in the Municipal Bond Market: What is Driving the Decline?", and in 2019, "Mark-up Disclosure and Trading in the Municipal Bond Market." While transaction costs for all municipal securities between January 2016 and April 2020 showed a consistently downward trend, the COVID-19 crisis (March and April 2020) wiped out nearly the entire reduction realized over the preceding four-year period. While this trend was not unexpected given market volatility, the speed and magnitude of the increase was surprising. The question now facing investors and market participants is how likely and quickly effective spreads might revert to pre-crisis levels.

CONCLUSION

We expect that in the second half of 2020 the SEC will continue to focus on timely and meaningful disclosure, particularly as it relates to the impact of COVID-19 on the financial and operational conditions of issuers and obligated persons. Implementation of the MSRB's "submission calculator" will impact continuing disclosure lookback review. COVID-19 has again brought to the forefront the application of the 2019 amendments to Rule 15c2-12 as it relates to modifications of existing financial obligations and entering into new financial obligations to ease liquidity limitations due to COVID-19. With FIMSAC's recommendation that the SEC be given additional statutory authority to enforce compliance with continuing disclosure agreements, we are likely to see resistance from the issuer community and challenges as it relates to the SEC's ability to regulate issuers under the Tower Amendment.

Although the effective dates for new interpretive guidance to Rule G-17 and the new Form G-32 have been delayed until March 2021 due to COVID-19, SIFMA has published updated form G-17 letters to streamline G-17 disclosures, and

we anticipate greater focus by broker-dealers on implementing these changes as the effective date approaches. The MSRB's rule changes as it relates to Reg B-I took effect June 30, 2020, as no extension was announced for the effective date of Reg B-I. We anticipate the MSRB to continue its retroactive review of certain MSRB Rules.

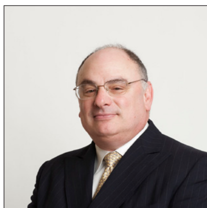
FINRA has reported seeing extreme movements in benchmarks, limited RFQ bidding, and wide variances in the pricing of the same security at the same time. FINRA has expressed concern that dealers are taking advantage of recent market volatility, and we may see dealers under increased scrutiny to defend pricing and best execution compliance, including a focus on whether policies and procedures were sufficient and followed. FINRA also expressed that its examination priorities are focused on procedures, systems, and controls in pricing an underwriting, and on required disclosures, including time of trade disclosures, material event disclosures, and conflict-of-interest disclosure for dealers under MSRB Rule G-17 and municipal advisors under MSRB Rule G-42.

Finally, the early part of 2020 saw upwards of 40 comment letters and additional submissions of several letters in opposition to the SEC's Proposed Order granting a conditional exemption from the broker registration requirements to municipal advisors. With the announcement of the Temporary Order, we saw some lawmakers, namely members of the House Financial Services Committee, question the SEC's methods and motivation for the Temporary Order. We expect all market participants to continue to be focused on the future resolution of the Temporary Order into 2021.

CONTACTS

John C. Grugan
Group Leader, Municipal Securities Regulation and Enforcement
215.864.8226
gruganj@ballardspahr.com

Teri M. Guarnaccia
Group Leader, Municipal Securities Regulation and Enforcement
410.528.5526
guarnacciat@ballardspahr.com



M. Norman Goldberger
Group Leader, Municipal Securities Regulation and Enforcement
215.864.8850
goldbergerm@ballardspahr.com

Kimberly D. Magrini
Public Finance
215.864.8365
magrinik@ballardspahr.com

Rebecca S. Lawrence
Public Finance
612.371.6224
lawrencer@ballardspahr.com