



ASSOCIATION FOR
INVESTMENT MANAGEMENT
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October 19, 2001

Ms. Jill C. Finder
Assistant General Counsel
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, Virginia 22314

Re: Rule G-37—Political Contributions and Prohibitions on Municipal Securities Business

Dear Ms. Finder:

The Municipal Securities Subcommittee of the Association for Investment Management and Research (AIMR®)¹ is pleased to respond to a request for comments on rule G-37, which prohibits a dealer from engaging in municipal securities business within two years after certain contributions are made by the dealer or certain related parties to an official of such an issuer (known as “pay to play” practices). A subcommittee of AIMR’s U.S. Advocacy Committee,² the Municipal Securities Subcommittee is charged with reviewing and responding to regulatory and legislative initiatives involving municipal bonds that affect the investment profession, the practice of investment management and the efficiency and integrity of financial markets. The Subcommittee offers its comments below.

General Comments

The Municipal Securities Subcommittee appreciates that the Municipal Securities Rulemaking Board (MSRB) has undertaken a review of existing rule G-37, in order to ascertain the industry’s experience with the provisions and to update them as needed. We generally believe that the existing pay-to-play prohibitions have been effective in stemming practices that compromise the integrity of the market by using political contributions to curry favor with politicians in positions of influence. Elected officials who allow political contributions to play a role in the management of public assets violate the public trust and affront the sense of maintaining a level playing field among market participants.

¹ The Association for Investment Management and Research (AIMR) is a global, not-for-profit organization of over 50,000 investment professionals in 100 countries. Through its headquarters in Charlottesville, VA, and more than 100 Member Societies and Chapters throughout the world, AIMR provides global leadership in investment education, professional standards, and advocacy programs.

² The U.S. Advocacy Committee is a standing committee of AIMR charged with responding to new regulatory, legislative, and other developments in the United States affecting AIMR’s membership.

The Subcommittee is unwavering in its support of promoting the highest ethical standards and practices by municipal market dealers. We therefore support the MSRB's sensitivity to practices that are perceived to threaten investor protections, compromise fiduciary integrity or otherwise undermine the fairness of procedures by which public contracts are awarded. We do, however, question the approach, scope, and substance of certain provisions of the pay-to-play provisions as they now stand. These concerns are addressed below.

Specific Comments

A. Two-Year Look-Back Provision

We believe that the current compliance requirements of the "look-back provision" impose substantial challenges, as the required level of monitoring and administrative record keeping is often difficult to meet. If the MSRB determines to retain the look-back provision in its current form, we recommend certain modifications that reflect a tempered approach in two situations.

As currently enacted, contributions above the \$250 *de minimis* amount by individuals to issuer officials may prevent a dealer from doing business with that issuer during the two years following the contribution, even in cases where (1) the municipal finance professional (MFP) was not associated with the dealer at the time of the contribution, and (2) the individual was not, at the time of the contribution, a MFP, but later becomes one by virtue of serving in a new supervisory capacity (e.g., new reporting relationships resulting from corporate restructurings). While we do not advocate the creation of a blanket exemption for these cases, we do believe that the rule should be modified as it applies to both instances to reflect the almost inadvertent manner in which the individual became a MFP.

Specifically, in response to questions posed by the MSRB, we are concerned that, on balance, applying the two-year look-back provision in both situations risks penalizing individuals without achieving counterbalancing benefits for the industry. In both cases, we recommend that rule G-37 allow a higher *de minimis* amount (in the range of \$500 to \$1000) in the two instances noted above. We believe that this approach will not undermine the underpinnings of the rule or substantially increase the risk that firms will manipulate the system to take advantage of these individuals' prior contributions.

We also recommend that the MSRB clarify the due diligence required of a firm in order to meet its obligations under the two-year look-back provisions. Particularly with new hires, the firms must rely on an individual's statement as to the timing and amount of past political contributions. To do otherwise would impose an unreasonably large administrative burden on the firm. Therefore, we ask that the MSRB make clear that a firm will satisfy its obligations under the rule if it uses reasonable grounds for making a conclusion as to an employee's political activities, including the express reliance upon that employee's statement.

B. Definition of "Primarily Engaged in Municipal Securities Representative Activities"

Currently, "municipal finance professionals" are defined as those who are "primarily engaged in municipal securities representative activities," for purposes of rule G-37. The MSRB now seeks comment on the "primarily engaged" portion of this definition.

We do not believe that a definition of "primarily engaged" should pivot on the amount of revenue generated by a dealer during a particular period of time. Instead, we urge the MSRB to focus on both the time spent on municipal securities activities, as well as the amount of benefit derived from those transactions, in calculating what will constitute being "primarily engaged." For example, a dealer who spends 10% of his time on municipal securities activities, but derives 60% of his annual income from those activities would most likely be so "primarily engaged." A dealer generating only 10% of his annual income, but spending 60% of his time, in municipal securities activities would similarly qualify.

The current understanding of what constitutes "municipal securities representative activities" includes activities in both primary and secondary securities markets. We recommend retaining this approach. We believe that drawing a distinction between the two markets in terms of limiting the application of rule G-37 would be used to circumvent the rule, and accomplishes no meaningful purpose. **Timing and**

Amount of Contributions

The MSRB is seeking comment on the appropriate timing and amount of *de minimis* contributions that should be reflected in rule G-37. We believe that there should *not* be a distinction made between general and primary elections for purposes of determining the amount of contributions subject to the rule. Regardless of when, and to what purpose the contributions were made, we believe the aggregate amount should remain subject to the *de minimis* amount set by the rule. Further, we suggest that the *de minimis* amount ultimately set by rule G-37 be adjusted for inflation on a periodic basis, in order to retain its relevancy as a deterrent.

D. Exemption Provision

The Municipal Securities Subcommittee agrees with the MSRB that exemptions to rule G-37 should be granted sparingly. In general, we do not recommend that the MSRB provide a blanket automatic exemption to the rule, even if it does relax certain of the restrictions, and broaden the list of relevant factors, that are now in place.

E. Role of Syndicate and Selling Group Members

As currently drafted, rule G-37 does not include selling group activities in the definition of "municipal securities business." While the MSRB has stated that syndicate members must report the municipal securities business in which they engage, it has not outlined the

factors it will use in making a distinction between the two. We strongly believe that selling group activities should not be excluded from the definition of municipal securities business. Doing so would overlook the large number of issuers in this area that are syndicated and inappropriately narrows the reach of the rule.

Conclusion

The AIMR Municipal Securities Subcommittee appreciates the opportunity to provide comments on rule G-37 and generally supports the rule as a mechanism for achieving a level playing field among market participants and shoring up investor confidence in the system. As noted above, we believe that these important goals can be still met, while modifying certain of the rule's existing provisions.

If you have any questions or we can provide additional information, please do not hesitate to contact Darrick Hills at 651.310.6226, darrick.hills@stpaul.com; or Linda Rittenhouse at 804.951.5333, llr@aimr.org.

Sincerely,

Darrick L. Hills, CFA
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