

*January 27, 2012*

## IDEA OF THE WEEK

### **The State of the Union**

On Tuesday, January 24, 2012, President Barack Obama delivered his annual State of the Union speech to a joint session of Congress. This precedes the annual release of the federal budget for the subsequent year, 2013, currently scheduled for February 13, 2012. The speech contained several proposals for tax changes that we anticipate will be set forth in the FY 2013 budget documents, including creating an unspecified “rule” that would require households who earn more than \$1 million per year to pay a minimum 30% federal income tax and limit deductions, various incentives to deter U.S. firms from shifting operations abroad, reduced tax rates for manufacturing firms. Other proposals that would affect public finance include a proposed \$200 billion for new transportation infrastructure to be paid for with savings from winding down the wars in Iraq and Afghanistan. Details on these proposals are likely to be in the FY 2013 federal budget documents. Most observers believe few, if any, of these proposals will be enacted by Congress in this election year, where it is expected that gridlock will, if anything, worsen.

## LEGISLATIVE

### **House Committee Members Question the Effects of Volcker Rule on Muni Markets**

On January 18, 2012, the House Financial Services Committee held a hearing on the so-called “Volcker Rule,” the provision of the *Dodd–Frank Wall Street Reform and Consumer Protection Act* that would limit the ability of banks and other financial institutions to engage in proprietary trading. Witnesses included regulators, including SEC Chair Mary Schapiro, industry representatives and economists. The rule has provoked concern because it would exempt from the restrictions certain municipal securities issued directly by “states or political subdivisions” of states but not bonds issued by state or local agencies or authorities. The proposal would also effectively prohibit banks from sponsoring tender option bond (TOB) transactions. NABL’s Committee on Securities Law and Disclosure is drafting a comment on the proposal.

Republicans on the committee appeared unified in their view that the four agencies responsible for promulgating the rule had gone too far and that, as proposed, the rule would disrupt liquidity in capital markets broadly. Several Members objected to the application of the rule on municipal markets specifically, including Representative Michael Grimm (R-NY) who argued that the rule would “limit liquidity in these securities and raise the borrowing costs for municipalities for cities like New York City.”

SEC Chairman Schapiro indicated an awareness of the problem and suggested that the exemption be broadened to conform it with the definition of a municipal security in the *Securities Exchange Act of*

1934, stating, "... we have flagged that in the proposal and sought comment directly on whether we should use a broader definition of government obligations, like the definition of municipal securities under the '34 Act, to provide a broader exemption."

Comments are due on this proposal on February 13, 2012.

## **House and Senate Republicans Vote to Block President Obama's Request to Raise Debt Ceiling**

President Obama requested and received an increase of the debt ceiling this week using a provision in the *Budget Control Act of 2011*. A resolution of disapproval against raising the nation's debt ceiling passed the House on Wednesday, January 25, 2012 with a vote of 239-176. The measure, however, failed to pass the Senate on Thursday. Due to the agreement in August of 2011, the debt ceiling will automatically be raised by \$1.2 trillion, unless the House and Senate could pass the resolution of disapproval with the two-thirds vote necessary to overcome a likely presidential veto.

# **REGULATORY**

## **Treasury Secretary Announces He Will Not Stay in Job Regardless of Election Outcome**

On Thursday, January 25, 2012, Treasury Secretary Timothy Geithner said in a Bloomberg interview that he believes President Obama will not ask him to stay on for another four years after this November's presidential election. According to BusinessWeek, Erskine Bowles, Chief of Staff under President Clinton and Senator Kent Conrad (D-ND) could be among potential candidates to replace Mr. Geithner.

## **Treasury Sends Recommendations to Congress on Tribal Bonds**

On January 19, 2012, the Treasury released the report *Report and Recommendations to Congress regarding Tribal Economic Development Bond provision under Section 7871 of the Internal Revenue Code*. The report, dated December 19, 2011, was mandated by the *American Recovery and Reinvestment Act of 2009*. Recommendations include: adopt the State and local government standard for tax-exempt "governmental bonds" for Tribal Economic Development Bonds and allow Indian tribal governments to issue tax-exempt private activity bonds for the same types of projects and activities allowed for State and local governments under Section 141(e).

The full Treasury report to Congress is available on the NABL web site library under Federal Tax Materials here: <http://www.nabl.org/library/documents/1306>

NABL comments relating to the definition of essential government function under Section 7871 is available here: <http://www.nabl.org/uploads/cms/documents/NABLCommentLetters-NABL7871Comments.pdf>

## **CFTC Approves Business Conduct Standard for Swap Dealers**

On January 11, 2012, the Commodity Futures Trading Commission (CFTC) approved the final rules on the business conduct standard for swap dealers. Among other things, the rules establish disclosure obligations and prohibitions against certain abusive practices. The rules also establish a safe harbor for swap dealers when fulfilling their institutional suitability obligation for recommendations made to counterparties. Special entities, such as states, municipalities, and employee benefit plans subject to the *Employee Retirement Income Security Act* (ERISA), will face heightened requirements.

## **MSRB Seeking Applicants to Fill Positions on its Board**

On January 9, 2012, MSRB announced that it is seeking “qualified applicants to fill 7 positions on its Board beginning October 1, 2012.” The MSRB will announce the new Board members by September 30, 2012. Applications must be submitted by March 1, 2012.

## **MSRB Publishes 2012 Rule Book**

On January 18, the MSRB published its electronic 2012 Rule Book, which describes rules for municipal securities dealers and municipal advisors effective as of January 1, 2012, which can be accessed here: <http://www.msrb.org/msrb1/pdfs/MSRB-Rule-Book-2012.pdf>

## **SIFMA Submits Letter on Issue Price**

On Friday January 20, 2012, SIFMA submitted a letter to the Internal Revenue Service regarding the determination of issue price. The IRS has been concerned about the flipping of bonds following issuance, especially direct pay Build America Bonds, which raise concerns about whether the bonds were correctly priced. The letter can be accessed here:

<http://www.nabl.org/uploads/cms/documents/SIFMATreasuryIssuePrice.pdf>

# **NEWS FROM AROUND WASHINGTON**

## **GAO Releases Two Studies Related to Municipal Bonds**

On January 17, 2012, the Government Accountability Office (GAO) released the study *Municipal Securities: Overview of Market Structure, Pricing, and Regulation*, GAO-12-265, which was mandated by the *Dodd–Frank Wall Street Reform and Consumer Protection Act*. Although, the GOA found that, although both retail and institutional investors buy municipal bonds in the secondary market, trade data showed that institutional investors generally trade at more favorable prices than individual investors, but that various legitimate reasons exist for the difference. The Municipal Securities Rulemaking Board and the Securities and Exchange Commission (SEC) are also studying the issue with a report expected in 2012.

The GAO also released *Credit Rating Agencies: Alternative Compensation Models for National Recognized Statistical Rating Organizations*, GAO-12-240. The study was also mandated under the *Dodd–Frank Wall Street Reform and Consumer Protection Act*. As of January 2012, GAO has identified seven alternative models for compensating NRSROs. The models were designed to ameliorate issues that were highlighted following the financial crash in 2008, including conflicts of interest in the issuer-pays model. The report was designed to aid the SEC in its ongoing study, reform, and oversight of credit rating agencies.

The reports are available on the GAO web site.