National Association *of* Bond Lawyers

Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-205)
Key Provisions Related to Municipal Securities

I. Municipal Securities Rulemaking Board ("MSRB") (*Title IX, Subtitle H, section 975*) (*Effective October 1, 2010*)

Board Composition

- Fifteen-member MSRB Board will include eight independent members unaffiliated with a broker-dealer or municipal advisor.

- Independent members will include at least one investor, one issuer, and one member of the "general public" with knowledge of or experience in the municipal industry (referred to as the "public representative").

- Industry board members will include at least one non-bank dealer, one bank dealer, and at least one municipal advisor (referred to as the "regulated representatives").

- May expand Board beyond 15 members, so long as public representatives exceed number of regulated representatives and the number of total board members is odd.

Expanded MSRB Authority

- Authorizes the MSRB to assist the Securities and Exchange Commission ("SEC") and Financial Industry Regulatory Authority ("FINRA") in examinations and enforcement actions regarding MSRB rules, and to retain half of any penalties collected by the SEC in such enforcement actions.

- Authorizes the MSRB to establish information systems and to impose fees for submission of information to these systems.

- Expands the MSRB's authority to regulate advice provided to or on behalf of municipal entities as well as "obligated persons," which includes any person who is committed to support the payment of all or part of the obligations on municipal securities.

- Requires the MSRB to meet with the SEC and FINRA at least twice a year to share information about the interpretation of MSRB rules and examination and enforcement of compliance with such rules.

Municipal Advisors

- Requires registration and oversight of "municipal advisors" and provides the MSRB with rulemaking authority regarding municipal advisors. The term "municipal advisor" includes financial advisors, guaranteed investment contract brokers, third-party marketers, placement agents, solicitors, finders, and swap providers, but excludes (among others) underwriters, investment advisors registered under the *Investment Advisors Act of 1940*, and attorneys offering legal advice or providing services of a traditional legal nature.

- Provides that municipal advisors and any person associated therewith are "deemed to have a **fiduciary duty** to any municipal entity for whom such municipal advisor acts as a municipal advisor, and no municipal advisor may engage in any act, practice, or course of business which is not consistent with a municipal advisor's fiduciary duty or that is in contravention of any rule of the [MSRB] Board."

- Requires the MSRB to adopt rules that provide continuing education requirements for municipal advisors and professional standards.

- Requires that MSRB rules not impose an inappropriate regulatory burden on small municipal advisors.

II. Governmental Accounting Standards Board (GASB) (*Title IX, Subtitle H, section 978*)

- Grants authority for the SEC to direct FINRA to assess and collect a fee on dealers to fund GASB.

- Mandates a Government Accountability Office ("GAO") study of the role, importance and funding of GASB. *This study must be completed within six months of the date of enactment.*

III. SEC Office of Municipal Securities (*Title IX, Subtitle H, section 979*)

- Creates an Office of Municipal Securities within the SEC, which shall administer the rules related to municipal securities brokers and dealers, municipal securities advisors, municipal securities investors, and municipal securities issuers and coordinate with the MSRB with regard to rulemaking and enforcement actions as required by law.

- Requires that the Office "be staffed sufficiently" to carry out such purposes.

- The head of the Office of Municipal Securities will be the Director, who will report directly to the Chairman.

IV. Municipal Securities Exempt from Prohibitions on Bank Proprietary Trading (*Title VI, section 619*)

- The Act adopts a modified version of the so-called Volcker Rule, named for former Federal Reserve Chairman Paul Volcker, restricting proprietary trading by insured depository institutions and their affiliates.

- There are a total of ten exemptions from the ban on bank proprietary trading and municipal securities are among these ten exemptions.

V. Exemption from Jurisdiction of the Bureau of Consumer Financial Protection (*Title X, sections 1002 and 1027*)

- The Act creates a new executive branch agency, the Bureau of Consumer Financial Protection ("CFPA"), with broad powers. The CFPA will supersede existing federal regulators with regard to many current consumer protection oversight functions.

- The Act carves out many activities and entities from the CFPA's jurisdiction, including persons regulated by the SEC and the Commodity Future Trading Commission ("CFTC"), the business of insurance, "registered municipal securities dealers," and "any other person that is required to be registered under the Securities Exchange Act of 1934."

VI. Credit Rating Agencies (*Title IX, Subtitle C, sections 931-939H*)

New Requirements

- Creates an Office of Credit Ratings within the SEC with its own compliance staff and the authority to fine agencies. The SEC is required to examine Nationally Recognized Statistical Ratings Organizations ("NRSROs") at least once a year and make key findings public. The head of the Office will be the Director, who will report directly to the Chairman

- Requires disclosure of NRSROs methodologies, reliance on third parties for due diligence efforts, and ratings track record.

- Requires issuers and underwriters of asset-backed securities to disclose the findings and conclusions of any third party due diligence report. Third party provider must provide a certification to the NRSRO which then must be disclosed by the NRSRO.

- Provides that enforcement and penalty provisions of the *Securities Exchange Act of 1934* (the "1934 Act") apply to statements made by a credit rating agency in the same manner and to the same extent as such provisions apply to statements made by a registered public accounting firm or a securities analyst. Statements are not deemed forward-looking for purposes of the safe harbor for forward-looking statement under Section 21E of the 1934 Act.

- Requires that NRSROs consider information about an issuer that the NRSRO has, or receives from a source other than the issuer or underwriter, that the NRSRO finds credible and potentially significant in its rating decision.

Conflicts of Interest

- Requires NRSROs to conduct a one year look-back review when an NRSRO employee goes to work for an obligor or underwriter of a security or money market instrument subject to a rating by that NRSRO.

- Requires NRSROs to report to the SEC when certain employees leave to work for an entity that the NRSRO has rated in the previous twelve months.

- Directs the SEC to create a new mechanism to prevent issuers of asset-backed securities from picking the NRSRO they think will give the highest rating, after conducting a study and reporting to Congress.

Enhances Enforcement

- Creates a private right of action against NRSROs for "knowingly or recklessly" failing to conduct a reasonable investigation of the facts or to obtain analysis from an independent source.

- Authorizes the SEC to deregister an NRSRO for providing bad ratings over time.

- Requires ratings analysts to pass qualifying exams and requires continuing education.

- Eliminates many statutory and regulatory requirements to use NRSRO ratings.

- Rule 436(g) of the *Securities Act of 1933* (the "1933 Act") has no force or effect – NRSROs are now subject to liability as experts under Section 11 and registrants under the 1933 Act must file the consent of the NRSRO with their registration statement pursuant to Section 7. Municipal securities are not subject to registration under the 1933 Act.

VII. Securitization (*Title IX, Subtitle D, sections 941-944*)

Broad Definition of Asset-backed Security

- Defines "asset-backed security" as "a fixed-income or other security collateralized by any type of self-liquidating financial asset (including a loan, a lease, a mortgage, or a secured or unsecured receivable) that allows the holder of the security to receive payments that depend primarily on cash flow from the asset." These include a collateralized mortgage obligation, a collateralized debt obligation, a collateralized bond obligation, a collateralized debt obligation of asset-backed securities, a collateralized debt obligation of collateralized debt obligations, or a security that the SEC determines to be an asset-backed security for the purpose of this definition.

Retention Requirement

- Requires issuers of asset-backed securities ("securitizers") to retain at least 5% of the credit risk, unless the underlying loans meet certain standards that reduce riskiness.

- A securitizer is not required to retain credit risk if all of the assets that collateralize the asset-backed security are qualified residential mortgages.

- Directs the SEC to provide a "a total or partial exemption for any asset-backed security that is a security issued or guaranteed by any State of the United States, or by any political subdivision of a State or territory, or by any public instrumentality of a State or territory that is exempt from the registration requirements of the Securities Act of 1933 by reason of section 3(a)(2) of that Act (15 U.S.C. §77c(a)(2)), or a security defined as a qualified scholarship funding bond in section 150(d)(2) of the Internal Revenue Code of 1986, as may be appropriate in the public interest and for the protection of investors."

- Requires the federal banking agencies and the SEC to jointly prescribe risk retention regulations not later than 270 days after enactment. Regulations under this Section will become effective (i) with respect to securitizers and originators of asset-backed securities backed by residential mortgages, 1 year after the date they are published in the Federal Register and (ii) with respect to securitizers and originators of all other asset-backed securities, 2 years after the date they are published in the Federal Register.

Disclosure Requirements

- Requires the SEC to adopt regulations requiring each issuer of an asset-backed security to disclose more information about the underlying assets, including asset-level or loan-level data if such data is necessary for investors to independently perform due diligence.

- The Act does not establish a deadline for the disclosure regulations.

VIII. Derivatives and Swaps Provisions (*Title VII, Part II, section 731*)

- Divides jurisdiction over derivatives and rulemaking into three categories: "security based swaps" generally covered by the SEC, "swaps" generally covered by the CFTC, and "mixed" swaps subject to joint regulation. In general, although the existing exemption for State and municipal obligations contained in the *Commodity Exchange Act* should be expected to continue to be applicable to State and municipal swaps, the new provisions requiring reporting of municipal swap transactions will apply, as will the new rules regarding the business conduct standards for swap providers and swaps advisors providing services to municipal entities, all as further described below.

- The Act provides that swaps are generally not required to be cleared if one of the counterparties is not a financial entity, is using swaps to hedge commercial risk, and notifies the SEC or CFTC, as applicable, how it generally meets its financial obligations relative to entering into non-cleared swaps. However, the applicability of this particular

exemption will depend in part on the extent to which a governmental entity may be considered to be hedging "commercial risk" in a transaction.

- Swap dealers are subject to new business conduct and risk and other disclosure requirements, and, when dealing with governmental parties, (a) if acting as an advisor, must comply with special rules against fraud, deception or manipulation and (b) if acting as a swap provider, must have a reasonable basis to believe that the governmental entity has an independent representative meeting certain qualifications and providing certain enumerated duties.

- Defines "special entity" to include "a State, State agency, city, county, municipality, or other political subdivision of a state."

- Imposes stringent "business conduct" requirements on "swap dealers and major swap participants" in their dealings with special entities, including (1) prohibiting a swap dealer or major swap participant from engaging in fraud, deception or manipulation, (2) requiring a swap dealer, but not a major swap participant, to act in the "best interests" of the special entity, and (3) requiring a swap dealer to disclose to the special entity in writing the capacity in which the swap dealer is acting before the initiation of the transaction.

- Excludes from the application of the business conduct standards any transaction that is (1) initiated by a special entity on an exchange or swap execution facility or (2) one in which the swap dealer or major swap participant does not know the identity of the counterparty.

- With certain exceptions, rules generally to be promulgated by SEC and CFTC within 360 days of enactment.

IX. Studies Relating to Municipal Markets (*Title IX, sections 976 and 977*)

- Requires the GAO to study the value of enhanced municipal issuer disclosure and the advisability of the repeal or retention of the Tower Amendment. *This study must be completed within 24 months of the date of enactment*.

- Requires the GAO to study the municipal securities markets, including: (i) an analysis of the mechanisms for trading, quality of trade executions, market transparency, trade reporting, price discovery, settlement, clearing, and credit enhancements; (ii) provide recommendations on how to improve transparency, fairness and liquidity in such markets; and (iii) potential uses of derivatives in the municipal securities markets. *This study must be completed within 18 months of the date of enactment.*