

MSRB Proposes Changes to "Pay-to-Play" Rule G-37

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On February 15, 2005, the Municipal Securities Rulemaking Board (MSRB) proposed an amendment to Rule G-37, which restricts certain political contributions made by individuals and firms within the municipal securities industry.

The MSRB, which was established by Congress to regulate banks and securities firms dealing in municipal securities, had issued Rule G-37 in 1994 to address concerns over informal "pay-to-play" requirements being imposed on some municipal securities dealers (MSDs) and municipal finance professionals (MFPs). As initially written (with some narrow exceptions), the rule provided that MSDs and MFPs were prohibited from engaging in municipal securities business with an issuer of securities within two years of making a campaign contribution to an official from the issuing entity (or within two years of their PACs' making such a contribution). While Rule G-37 was adopted to deal with the specific problem of direct contributions to issuer officials, the MSRB stated in an August 2003 Interpretive Notice that the rule also limited contributions through conduits, including political parties, PACs, consultants, lawyers, spouses and affiliates.

In recent years, however, the MSRB became concerned that a number of issuer officials have asked that contributions be made to a political party's "overhead" or "housekeeping" account if making a direct contribution to the issuing official would trigger the ban on business. In response to this practice, the MSRB proposed the February 15, 2005 amendment, which would prohibit MSDs and MFPs from "soliciting any person or PAC to make or coordinate a payment to a political party of a state or locality where a dealer is engaging or is seeking to engage in municipal securities business." MSRB Notice 2005-11 (Feb. 15, 2005).

In addition to the proposed rule, the MSRB also published a draft Q&A guidance document to help clarify the requirements of Rule G-37(d). This guidance document is designed to assist dealers in adopting certain written supervisory procedures to ensure that neither the dealer, nor its MFPs, use payments to political parties or PACs to make indirect contributions to an official of an issuer.

These documents may be viewed at www.msrb.org/msrb1/whatsnew/2005-11.asp. The MSRB will accept comments on the proposed rule and the draft Q&A guidance document through April 1, 2005.