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FOR FINANCIAL REFORM
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Americans for Financial Reform
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PROTECT TAXPAYERS AND STOP WALL STREET'S PREDATORY BEHAVIOR IN MUNICIPAL FINANCE: OPPOSE S. 710

Dear Senator,

On behalf of the undersigned organizations, we urge you to OPPOSE S. 710, the so-called "Municipal Advisors Relief Act of 2013". This legislation exempts all banks, domestic and foreign, from new rules enacted in the Dodd-Frank Act designed to prevent predatory behavior in Wall Street financial dealings with states and municipalities. The new fiduciary protections are critical to protecting taxpayers and communities from unfair dealing that has cost them many billions of dollars. S. 710's blanket exemption for banks would create a major new loophole in the law. It must be rejected.

The Dodd-Frank Act's fiduciary protections respond to the revelation of massive financial abuses of municipal borrowers by banks and derivatives dealers. The most notorious case was in Jefferson County, Alabama, which was driven into bankruptcy due to billions in losses suffered in exploitative swaps deals sold by JP Morgan Chase. Yet Jefferson County is just the tip of the iceberg. For example, the Justice Department has brought numerous criminal cases against major banks for manipulation and bid-rigging in municipal markets.[1] Across the country, hundreds of cities and towns have been trapped in deceptive swaps deals requiring them to pay exorbitant fees. Public entities, public employees, taxpayers, and users of public services across the country, including many members of our organizations, have been deeply harmed by this abusive behavior.

In response to these problems, Congress required those providing financial advice to municipalities to register with the Securities and Exchange Commission (SEC), and to respect a fiduciary duty to respect the best interests of taxpayers and the municipal client in the advice they give. Under the new law financial advisors to public entities will be required to hold to the highest ethical standards and refrain from advice that benefits the advisor at the expense of local taxpayers or governments. The municipal advisor protections are based on the common sense principle that those providing financial advice to public entities should put the interests of their clients and their taxpayers first.

S. 710 would drastically undercut this standard in ways that are both harmful and unnecessary. S. 710 is harmful because it exempts all banks, domestic and foreign, from designation as municipal advisors and the accompanying Dodd-Frank protections. This new exemption would open up numerous possibilities for financial institutions to provide advice on complex financial transactions to

[1] O'Toole, James, "Bankers Nabbed in Bid-Rigging Scandal", CNN, September 18, 2012.

public entities without having to respect a fiduciary duty to taxpayers. The apparent justification for this sweeping new exemption is that banks are regulated under other prudential rules. However, the fact that banks are prudentially regulated does not in any way reduce the potential harm of granting them a blanket exemption from the municipal advisor fiduciary duty. Prudential regulation addresses only the financial soundness of the bank and does not include fiduciary duty protections that are created by municipal advisor designation.

The exemption in S. 710 would permit banks to provide financial advice on borrowing, investment, and other issues to public entities without any requirement to follow a fiduciary duty ensuring that such advice is in the best interests of their clients. In many cases financial advice is provided during the solicitation of a municipality for a complex financial transaction, or during the performance of such a transaction. While there may be no separate charge for the advice, it can still be highly profitable due to fees or profits generated as a result of having the customer follow the advice. Banks are frequently involved in providing such complex financial services to municipalities, and the involvement of commercial banking entities in these municipal transactions is increasing.[2] In addition, many of the entities that are specifically engaged and paid as municipal financial advisors are affiliated with commercial banks. At least three of the top ten financial advisors during the first half of 2013 were owned by commercial banks.[3]

S. 710 is also unnecessary, because existing law already exempts a wide range of ordinary business dealings with municipalities from municipal advisor designation. First, the mere provision of neutral financial information to a municipality would not constitute ‘advice’ triggering an advisor designation. Any bank that was only providing information to a municipality about the availability and costs of financial products would not and should not be covered by the municipal advisor designation. In addition, the Dodd-Frank Act already exempts many professionals from advisor designation when they are performing professional duties. This includes underwriters when they are acting simply as underwriters (as defined in Section 2a(11) of the Exchange Act), as opposed to providing more extensive financial advice. The legislation also includes similar exemptions for attorneys, accountants, engineers, registered investment advisors, and other professionals when providing professional advice.

S. 710 does address an issue in the initial SEC proposal involving the financial advice provided by elected or appointed public officials in their capacity as members of public advisory boards. The initial proposal would have classified such officials as municipal advisors. However, after this proposal attracted criticism the SEC has several times committed to fix this issue by narrowing the definition of financial advisor in the final rule to exclude elected and appointed officials. Should the SEC not follow through on these promises, Congress could legislate in this particular narrow area after the final rule is passed. Criticisms concerning this narrow issue should not lead Congress to pass a wider bill like S. 710, which contains a broad and sweeping new bank exemption that would greatly undermine important taxpayer protections.

[2] Corkery, Michael, "In Shift, Municipalities Turn to Banks for Loans", Wall Street Journal, July 14, 2011.

[3] The financial advisors in question are First Southwest (PlainsCapital Bank), RBC Capital Markets (Royal Bank of Canada) and KNN Public Finance (ZionsBank). They are respectively numbers 3, 6, and 7 on the Thomson Financial list of the largest municipal financial advisors by volume for the first six months of 2013.

If Congress passes this bill, it will unnecessarily create additional financial risks for states and localities, and for their residents who pay taxes and use public services. When states and localities suffer financial losses, the typical result is tax increases or budget cuts to education, health care, public safety, infrastructure, and other vital public services.

In sum, we urge you to OPPOSE S. 710 because it would weaken accountability for financial advice to municipalities, harm communities, and is unnecessary given the exemptions that already exist in the law and the authority of the SEC to address any outstanding issues. If you have any questions, please contact Marcus Stanley at Americans for Financial Reform at marcus@ourfinancialsecurity.org or (202) 466-3672.

Sincerely,

AFL-CIO (American Federation of Labor and Congress of Industrial Organizations)

AFSCME (American Federation of State, Country, and Municipal Employees)

Americans for Financial Reform

Consumer Federation of America

U.S. PIRG (Public Interest Research Group)

SEIU (Service Employees International Union)