Securities and Exchange Commission Historical Society
Interview with Ernesto Lanza
Conducted on March 20, 2014 by William Thomas

WT: This is an interview with Ernesto Lanza for the SEC Historical Society's virtual museum and archive of the history of financial regulation. I'm William Thomas. The date is March 20th, 2014. We're in Alexandria, Virginia at the MSRB. So, thanks very much for agreeing to talk with us. Could we begin a little bit with your personal background? You're from Chicago, did you say?

EL: That's right. I was born in Chicago, lived there until I was five and then moved to Miami.

WT: And then you went to Harvard for your undergraduate?

EL: That's right.

WT: What did you study there?

EL: Government. I started off as a biochemistry major, pretty much flubbed it the first year and decided to switch major then.

WT: And did you intend to go into law school after that, or did anything happen in the interim?

EL: No, I did go straight to law school. I didn't go into Government planning to be a lawyer, but it seemed to work out pretty well, ultimately.

WT: So, did you have any notions about what kind of law you would study when you went? You went to Penn, in '85 starting, and you finished in '88?

EL: That's right. No, I always had a real interest in public service. You know, during the summers I clerked in a couple different places, one at a private law firm, the other time at the county attorney's office, and really always had interests in the public angle of law.

WT: And then you worked for a few different law firms before you ultimately came here to the MSRB. Could you tell us a little bit about what you did, and how you got into municipal securities in the first place?

EL: Sure. I mean, as I mentioned before I was always interested in the public angle of law, and so I started off after law school at Greenberg Traurig in Miami as a bond attorney. That kind of brought the two aspects of being a lawyer into play, one was the private sector side of working with the marketplace, but in fact doing it for a public purpose, for the public good, for public infrastructure, helping city and local governments finance their needs. And so I started off as a bond attorney at Greenberg Traurig for three years. They had really, just the year before I joined them, become a big player in the marketplace on that, so I was able to dive in pretty deep to transactions very early on.

WT: Did you choose to do that, or were you assigned to it?

EL: No, I was hired in to do that kind of work and so it actually kind of met my sweet spot, in terms of my interest in doing that kind of work.

WT: And could you tell us a little bit about what the work involved on a day-to-day basis?

EL: Given that they'd ramped up from the year before and were probably, in retrospect, understaffed, I was thrown in right away to the deep end of the pool. A lot of meetings with public officials, doing lots of drafting of very long documents – trust indentures run 100 pages long – helping to draft disclosure documents, doing a lot of due diligence.

One of the fun parts of the job is that we did a lot of work with Puerto Rico, and so I was able to go down to Puerto Rico and do a lot of due diligence there, which is not always fun but it's always a nice location to do it. And so, since I spoke Spanish, I was able to go through some of the documents there as well, because a lot of the materials there are in Spanish.

WT: And you were there for three years before you moved on?

EL: That's right. My wife was in medical school at the time, and as hard as I was working she was always working harder than I was, so when she finished she got a residency in Philadelphia, so I followed her to Philadelphia and joined Ballard.

WT: Now, this was actually a fairly interesting time in the municipal bond area. I mean, you have the institution of 15c2-12. You also have the Tax Reform Act of 1986. Was there a sense of major change for the issuers, for the dealers?

EL: Well certainly when I started up in ’88 that was kind of in the aftermath of the ’86 tax law change, and so I wasn’t there at the time but the story was in 1985 people were going crazy doing so many transactions to try to meet the deadline for the old tax law. And so I kind of came in in the aftermath, where people were figuring out how to go about doing transactions under the new tax laws, and so there was a lot of opportunity to really be at the ground floor of the new structure of muni finance at the time, and so that was a real positive.

Certainly c2-12 brought about a very different type of disclosure in the primary market system. Certainly official statements had existed at the time, but it provided a little bit more certainty that you’d have it in most transactions, and started developing a better practice in the marketplace in terms of having good disclosure in the primary market.

WT: And most of the restrictions in the 1986 act I believe dealt with conduit bonds.

EL: That’s one of the main things. It also had other limitations in terms of how bond proceeds could be used, even by governmental agencies in terms of reinvestment for arbitrage gains and things like that, so it really took a little while for the market to get its footing again after the ’86 tax act, at least in a lot of sectors.

WT: And then at your next job you were there for about four-and-a-half, five years?

EL: That’s right, at Ballard Spahr. That was continuing to do bond work in a lot of different areas, a lot of governmental bond issues, doing a fair amount of conduit offerings primarily for health care, for multi-family and single-family housing. I spent the first three in Philadelphia. When my wife finished her residency she got her attending position in Washington, so I moved to the Washington office of Ballard. So I spent the last year-and-a-half, two years at Ballard Spahr in our Washington office.

WT: And do you have anything to say about the changes in this time? Of course, this was the period of pay-to-play.

EL: That’s right. Well, I mean it was a big – I was still in private practice at the time when the pay-to-play rule came into effect, it was in ’94, but it certainly was a headline issue. I think people, particularly the foot soldiers in public finance, were never very happy that pay-to-play practices existed, if for no other reason than because when bonus time came around they were writing checks and they didn’t enjoy doing that.

And so I think, quite frankly, the vast majority of market participants were actually thrilled to have a pay-to-play rule put in place so that, if nothing else, people weren’t being asked to make contributions, and it had made people feel kind of not very happy about having an industry where one could try to influence being hired based on contribution. So I think, by and large, the vast majority of the marketplace was actually very happy the rule was put into place. I didn't come to the MSRB until a couple years after the rule was in place, but certainly I was very much involved in a lot of the after-adoption process with the pay-to-play rule.

WT: Yes, I'm interested in that. Maybe we should wait until we get to the MSRB before we talk about that in a little bit more detail. Is there anything else you want to talk about, changes in the bond market and in bond law in this particular period?

EL: There was a lot of activity then, but not so much for me. I think people were getting used to the c2-12, and in '94, '95 the continuing disclosure aspect came into play. And so that, again, was another step in bringing disclosure practices into the marketplace. That didn't really hit the bond attorneys that much, so I kind of saw that from a distance because we mostly dealt with the primary market side of things. But that certainly affected a lot of what happened in the marketplace.

WT: And you had one more stop before the MSRB?

EL: Yes, I spent about a year, a year-and-a-half in the Washington office of Holland & Knight, which is a Florida law firm. I was looking to work with them to expand their reach beyond Florida, and actually it was during that time where I really got to know the

MSRB for the first time really well, because the MSRB back in 1990 had started collecting official statements after 15c2-12 was put in place. That was mostly provided to vendors through subscription feeds, but they also had a public access facility in their Alexandria office. And I found it especially useful because I spent that year-and-a-half at Holland & Knight trying to drum up new business, and part of the process was to actually go to the MSRB's offices, look at the OSs and be able to do a brief search on potential issuer clients to be in a position to make pitches for them.

And that's when I really first got to know the MSRB and the resources it had available, and was surprised to see that I was one of the few people who ever actually went to that facility to find that data. So I had, very early on, a sense of how, even though this treasure trove of information was available, it wasn't being used by the market very well. And so it was during that time, like I said, I got to know the MSRB and about a year-and--half into my time there is when the MSRB went looking for a lawyer and I said, hey, that'd be kind of fun.

WT: So how did you get alerted to that in the first place?

EL: I'm trying to remember. I don't really recall. Probably *The Bond Buyer* or something, reading through the articles and saying, hey, look at that, MSRB, I spent a lot of time there. It would be interesting to work there. Again, it kind of fed back into my interest in public service. MSRB's a non-governmental entity, but it's in the public service in terms of doing fair-practice rules and things like that, and so it immediately piqued my interest.

And, like I said, having gotten to know the organization it was something that just made a lot of sense to me.

WT: Okay, so let's talk a little bit about the situation at the MSRB when you arrived. What kind of an organization did it seem to be?

EL: A very small organization. I don't remember the exact number, but they had two offices. They had one in Washington with maybe twelve, fifteen people, primarily the lawyers, some of the policymakers, a couple of other people there as well. And then, kind of a back office in Alexandria, with people who did the IT work, people who did arbitration. We had an arbitration program at the time, as well as a couple other functions for professional qualifications as well, but it was a smaller organization.

WT: Is that where we're sitting right now?

EL: No, it's a few blocks away, not very far from here, very close by. So, you know, it was a very tight-knit group, and because it's a small organization you very quickly, again, got very much involved in all the key areas of activities the MSRB did. And so that again was a quick transition into the work at the MSRB.

WT: Could you tell me a little bit about Kit Taylor? We'll be actually speaking with him in another couple weeks, so you know.

EL: Yes, no, absolutely. He had been there for a while. He was the executive director when I joined. Again, he had a very tight-knit group, very dedicated to the work that the MSRB did, really spent a lot of time making sure that they had high quality people at the organization able to do the work we were supposed to do, and I think worked pretty tirelessly on behalf of the organization throughout the time he was there.

WT: And at the SEC at the time, it was still Chairman Levitt?

EL: I'm trying to recall his exact – he's the first I recall so I'm guessing that's right. He had been there earlier on. He was a big supporter of the MSRB, and when the pay-to-play rule was put into place a couple years earlier. Yes, I think he was still there is my recollection.

WT: And they also had the free-standing Office of Municipal Securities there at the time, under Paul Maco.

EL: That's right, Paul Maco was there, and so we did work with him on a couple of initiatives in the early days there.

WT: What would be the main things that you would interact with the SEC on?

EL: Well very early on when I came to the MSRB, because I had done the public finance side, I gravitated towards a lot of our underwriting rules, the rules of disclosure. I started doing a lot of work with our rules on official statements, submissions to – it was back then called the MSIL system, Municipal Securities Information Library – and I also got very much involved in how Rule 15c2-12 interacted with the MSRB rules.

And so on a number of occasions, whenever there was an issue in that area, we would talk to Paul and his team on issues. We had done a pretty deep data dive in terms of the timeframe under which underwriters had turned the official statement around upon having received from the issuer and made it available to us. We provided the SEC with a lot of data, in terms of how well issuers and underwriters were doing in terms of meeting the timeframes that Rule 15c2-12 provided for us. So there was a lot of communication back and forth on that front in particular.

WT: Can we return to G-37, then, and I guess G-38 as well, which were fairly new at the time?

EL: That's right. Yes, I think there was still a lot of learning to be done in the marketplace around G-37 in particular. One of the interesting things we spend a lot of time doing is – I'll take a step back: broker-dealers were providing reports to us on Form G-37/G-38 on their contributions, their deals that they were doing, and that would be filed with us on a quarterly basis and we made those available publicly on our website. What was interesting is that you will often see a headline in the press that covered the municipal marketplace of, oh, such-and-such firm made a contribution and violated rule G-37. And we'd have to spend some time with the reporters, and say, okay, understand, the rule does not prohibit contributions, so a contribution doesn't create a violation. It's whether a firm does broker-dealer underwriting business after making a contribution that then the violation occurs. And that was really – it sounds like a hyper-technical issue, but it really was very important. The rule had been challenged on constitutional grounds beforehand, before I had arrived there.

WT: That's Blount?

EL: That's right, the Blount case. And all of that was finished by the time I got there. It was still fresh in people's mind. And it was very clear, both in terms of how the rule was written, but also really key to the court's decision to uphold it, was the fact that it was not a limitation on the ability to make contributions. It had an impact on it, but that impact was narrowly tailored to further the compelling governmental purpose.

And so it was important to be clear that the MSRB wasn't prohibiting the contribution. We weren't regulating contributions. We were regulating potentially conflicted business that might occur after the contribution. And so that's been a lesson that has taken people a long time to understand, and it continues to be a lesson we have to teach people from time to time, that it's not an anti-contribution rule.

The other aspect around G-37 – and again, it's still the case even today – is there's always an urge to say we need to tighten the rule to the point where there is never a contribution made in a way that can look like it influenced the hiring of an underwriter, or, probably in the future, municipal advisor. And the fact of the matter is, part of the reason the court actually upheld the rule was the fact that it wasn't so hermetically sealed to completely shut off all contributions. It still allowed speech by broker-dealers and others to make contributions, but it provides certain safeguards. And so – in fact, my theory, it's just my personal theory – is that it will probably be constitutionally impossible to write a rule that would completely shut off all contributions in this area, because that would be a problem under the First Amendment.

WT: So when we're talking about, say, a very large firm and the application of that rule, does it apply to the entire firm, or does it apply to the sections of it that are dealing with the issuers?

EL: Right, it's a pretty technical rule so I'm not going to go that deep into it. It by and large will cover the firm as an entity, so the broker-dealer entity can't write a check without potentially raising the bar on business, if it tried to do business afterwards. But, beyond that, it applies primarily to what are called municipal finance professionals; these are the people on the ground, who do the municipal work. And, again, there are very technical definitions about who's in and who's out, but the idea is to cover just those contributors who would benefit from the business that would occur after the fact. So, by and large, contributions from people who are in other parts of the organization who are completely disconnected from the municipal aspect of the firm and who aren't receiving some direct benefit from it, the rules would not cover that.

WT: Now, at the time, surveillance and enforcement were done primarily through NASD?

EL: That's right. Enforcement of MSRB rules is done by now-FINRA, but then-NASD for broker-dealer registered firms. You did have a number of banks who engaged in municipal securities activities that aren't broker-dealers, and so in that case you either have the Federal Reserve, you have the FDIC or the Office of Comptroller of the Currency at Treasury that does the enforcement for those entities. And the SEC has overall enforcement authority, as well, so there's five different actors out there for the enforcement, depending on what the nature of the organization is.

WT: And I know that most bond lawyers don't have that much to do with that part of the market because it's a fairly exceptional thing, but then, when one comes to the MSRB, do those issues become more prevalent?

EL: Well, you mean in terms –

WT: Well, let's say for example the aftermath of Orange County, which was in 1994.

EL: Well, I think it affects how you go about looking at how our rules apply to the marketplace. So, whenever there's a big blowup or a big issue, the Board always spends a lot of time saying, okay, one, did our rules apply? Two, if they would've applied, did they apply well? And if the rules didn't apply, then who can we work with, the SEC or others, in terms of trying to define how one can avoid these happening in the future?

One of the interesting things about the way the MSRB is structured as compared to other securities regulators is that we have a pretty constrained statutory authority. Our authority was really to write rules on broker-dealers or banks in connection with their municipal securities transactions.

And so you needed to have that link to municipal trades, transactions in order for a rule to apply, so you might have a firm that is very active in the municipal marketplace dealing with a state and local government entity in some respect, but if there's no municipal transaction involved we didn't have jurisdiction to make rules in that. So it became an interesting question when you had things occurring that might affect the finances of state and local government.

You had to have that nexus to bonds. The same thing would happen, if bonds are issued, but if after the fact the proceeds of the bonds are reinvested in federal government securities, Treasury securities, i.e. yield burning. Did we have authority to reach that, when the actual transaction was a purchase and sale of a government security, a federal government security, not a municipal security? And there's always a question about derivatives. And that was an object of quite a bit of discussion at the MSRB in terms of could we reach derivatives transactions that were related to municipal securities underwriting?

WT: Even at the time that you arrived?

EL: You know, it ebbed and flowed, depending on what was going on, so I can't remember the exact timeframe, but by the late-'90s those discussions were certainly happening. And it wasn't just at the MSRB. I mean, certainly you had the CFTC, the whole episode around Brooksley Born. I think she had called for authority for CFTC to regulate over-the-counter derivatives, and ultimately Congress said no, and in fact put a law in place saying you can't touch that.

And so, whenever the issue of derivatives came up in the municipal marketplace, I think there was always a strong feeling that we'd love to be able to write rules or do something in that area to the extent that they made sense. But then ultimately the question was, well, but are those transactions in municipal securities, or is this something else that we can't regulate? And so there was always a tension that was going on throughout the time I was there on the question of derivatives.

WT: And you mentioned yield burning, actually. I wanted to ask you a little bit more about that, because you would have arrived in the middle of when that whole deal was going on.

EL: Well, it was very concerning. I think people were very unhappy about it. People felt that, if nothing else, it created a real taint to the marketplace. It was certainly a manipulation of what the tax laws expected to happen. But, as I mentioned, the question became what was the reach of our rules in that area, and our rules certainly cover the bond underwriting. The question was that yield burning, the primary activity that was going on there was that someone was investing the proceeds after the bonds were issued in federal government securities, and our rulemaking authority didn't cover that transaction. And it was the mispricing of the federal government securities that was ultimately creating that kind of arbitrage, or trying to work around the arbitrage restrictions. That was really the core violation occurring there.

So when you go back and look – and I haven't looked at them for a while – but looking at a couple of the enforcement actions that occurred after the fact, the SEC ultimately cited them under anti-fraud restrictions, and never did cite MSRB fair-practice rules, because I think it was their view that they clearly didn't apply. It was a question of whether they applied because they weren't municipal securities transactions, they were federal securities transactions.

So, yes, I think that yield burning, and probably derivatives, were a couple of areas that really were always kind of there, and I think in the end you saw that frustration with the inability to have a clear line of authority in those areas ultimately made its way into the Dodd-Frank Act, in terms of municipal advisor authority, which was extended to reach issues like municipal derivatives, to reach issues like GIC brokering and things like that.

WT: Would the MSRB have been in contact with the IRS, in terms of trying to figure out how to redress cases of yield burning?

EL: I don't recall specifically us taking action with them at the time. I was still fairly junior at that point.

WT: Okay, well I'd like to get to the thing that you're probably one of the best experts at, which is electronic disclosure. You mentioned the MSIL system, so that had originally begun here in the early '90s?

EL: That's right. I think '91 is when it first started operations and it started collecting official statements and advanced refunding documents going back to 1990.

WT: And that's the MSRB's own system?

EL: That's right. So it was an internal system that then made those documents available to subscribers, like information vendors, and the MSRB also had that public access facility that I mentioned at the start.

WT: Okay, and that's mainly just an issue of disclosure?

EL: That's right, so the initial primary market disclosure document.

WT: And when did the NRMSIRs come into the picture?

EL: The NRMSIRs came in the picture when the SEC enacted the amendments to Rule 15c2-12. That was, I guess in 1995 when it became effective, and so that was the way to have a private sector version of continuing disclosures made available to the marketplace. And so the NRMSIRs weren't new companies, they were companies that were already active in the municipal marketplace, information vendors, but then they took on this status as a nationally recognized municipal securities information repository, lovely name, NRMSIR. And by having that status, then, the issuers in their contracts – and that's a whole level of detail in terms of how that was structured – but the issuers were ultimately obligated by contract to make submissions of continuing disclosures to all of these NRMSIRs. And I think at some point there were six to eight NRMSIRs. By the end there were four NRMSIRs out there.

WT: Okay. And did those coexist with the MSIL system, or how did that work?

EL: They did. So the NRMSIRs were around – again, I mentioned the population of NRMSIRs changed over the years – but starting in 1995 that NRMSIR designation came into effect. And, again, they were getting continuing disclosures, which the MSRB wasn't by and large receiving. We were part of the rule, but only for a small sliver of the types of disclosures. And NRMSIRs generally also would receive official statements as well, because of a provision in the Rule 15c2-12 that put an obligation on underwriters to distribute OSs to the marketplace. And that was timed off of when the official statement would be available from a NRMSIR. It's kind of a complicated rule, so I don't want to go too deep into it, but they did coexist with us.

WT: And did this have anything at all to do with transaction reporting, or did that come later?

EL: That was separate. We started the transaction reporting program in, I think, 1995. It ended up begin tied a little bit to the adoption of Rule 15c2-12, because at that time there had been some discussion around potentially having rules around riskless principal disclosure of markets and markdowns. That rule ultimately didn't move forward – that was an SEC rule, by the way, the SEC withdrew that proposal – but as part of that process the MSRB agreed to start making trade prices available to the public. And so we started collecting first inter-dealer trades, then afterwards customer trade data, and then made it available in a step-wise way to the marketplace on the next business day.

WT: What was the mechanism for that?

EL: We had information feeds that went out to the marketplace, and so information vendors would receive the data and they would make it available on their platforms.

WT: And was there an evolution of the disclosure requirements through this period?

EL: Well, in terms of the requirements, they were pretty much the same in the sense that in 1990 you had an indirect obligation on underwriters to receive an official statement, and the definition of official statement really just said providing disclosures regarding the issuer and securities without any specific requirements of what the information would be.

Continuing disclosure, when it came into play in 1995, set out some general parameters around the annual financial information and a list of, I guess, eleven event disclosures. I think it was called the Eleven Deadly Sins at the time. They required dissemination to the NRMSIRs, but really did not say specifically what those disclosures would need to be. I think some of the evolution occurred through market forces, some occurred through situations where an official statement omitted important information, so there might have been an enforcement action under anti-fraud rules. So there was kind of, call it an informal process that built around Rule 15c2-12 to slowly improve the level of disclosure in the municipal marketplace.

WT: Okay, a couple of general questions about the market in this period. First, is it correct to say that municipal bond funds were an important issue at this time?

EL: Well, again, municipal bond funds were one of the significant investors in municipal securities, but the bond funds themselves aren't municipal securities, they're products that invest in municipal securities, and so they were and continue to be one of the big institutional investors in the marketplace. You know, nothing stands out in my mind in this timeframe.

WT: And it's also my understanding that the '90s in particular were a time of more high risk bonds – the collapse of Heartland Advisors is sometimes cited as the end of that. Was that your impression, or was it an MSRB concern?

EL: Well, I think the MSRB, when the Heartland case came up I think we were looking very closely at it. We wanted to ensure that our rules were working effectively in connection with those types of investors. Again, our rules are rules on broker-dealers, and so the question was did the dealers do what they were supposed to do when they were engaged in transactions with Heartland, because Heartland was a customer in that case. And so, did they meet their obligation in terms of providing the disclosures they're supposed to receive? If they made recommendations, were those recommendations suitable? So those were the types of issues that would be relevant in that context. Whether or not Heartland as an institutional investor and as an investment manager did what it was supposed to do in terms of the funds that it offered, that was something that we had an interest in but did not have any authority over.

WT: And what was the general perception of that at the time? I mean, in terms of selling of these bonds, was it the case that they were deemed to have fulfilled their obligations?

EL: Again, I don't recall specifically what the issues were around the particular bonds that Heartland invested in.

WT: Okay. So now I guess I'd kind of like to get into the 2000s, so at this time there is some change at SEC with the shift to the Office of Municipal Securities into – it's escaping me now, Market Reg?

EL: Market Reg.

WT: Yes, yes, and also the establishment of the Muni Council. Can you tell me a little bit about that?

EL: Well, sure. I guess those are kind of separate things. Throughout, wherever the Office of Municipal Securities stood, they were always one of the key areas of contact for the MSRB and the SEC, and I think we always had a very strong relationship. So, regardless of what their authority was or where they were in the organization, I think they were a key part of our rulemaking over the years and continue to be even today.

WT: They were also smaller. Did their role change, in your perception?

EL: Yes, I think when I first arrived at the MSRB and the office was reporting directly to the chair, it certainly carried a heavier voice, a stronger voice at the SEC, and was very much more deep into whether things moved forward or not between us and the SEC. I think it did lose some of that traction internally at the SEC, although I guess you'd need to ask someone at the SEC about that, but again, continued to be fully engaged. I think as it got larger or smaller it had more or less bandwidth to get involved in terms of working with us on our rulemaking.

I think throughout most of my tenure here at least, I think ultimately there was an understanding that most of the expertise in the municipal marketplace resided here at the MSRB, but there was additional expertise at the SEC that was very helpful in terms of working through various issues. So, like I said, I think it's always been a very fruitful relationship with us and the Office of Municipal Securities.

Muni Council, you know, that was kind of a very different thing. The MSRB in the late-'90s, going into the start of the 2000s, had put together several kinds of outreach events and seminars with market participants on the issue of disclosure. We did some sector-specific sessions in health care, housing, long-term care type facilities, and then some more general disclosure forums.

And given how much interest there was in the marketplace, how much evolution was going on, you know, NFMA, National Federation of Municipal Analysts, was very active in putting out proposals in terms of different sectors of disclosure. Ultimately the MSRB said, let's try to formalize these kinds of interactions with market groups, and so back in 2001 did put together the Muni Council. And that's something that I, and another attorney at the time, was very much involved in, putting together the initial meeting of that group. And we had about, I'm guessing, fifteen to twenty different organizations representing broker-dealers, issuers, investors, bond lawyers, other professionals in the marketplace, and brought them in for, I think, it was like a day-and-a-half.

We actually hired a facilitator. We created little subgroups to meet and discuss, what are the high priority areas in the municipal marketplace, where are the biggest problems, where are areas where some progress could be made on a voluntary basis. So there was a day-and-a-half of discussions and at the end of the day we ultimately issued a report among the participants identifying some areas where real progress could be made. And disclosure was one of those areas where people felt that the marketplace, separate and apart from rulemaking, could on a voluntary basis make some significant progress in improving the marketplace by improving disclosure practices. And so, you know, that kicked it off.

In 2001 there was an agreement among the groups to rotate the venue, the hosting of this. I can't remember where it was, but six months later one of the other groups, back then it was probably The Bond Market Association, might have hosted the next one.

The interesting thing is it was a group of the MSRB, as the regulator, and then maybe fifteen market groups, and after about two or three meetings, the market, the non-regulatory market professionals said, hey, we want this to be purely a non-regulatory, private-sector initiative. And so they fairly politely asked the MSRB to excuse itself from the Muni Council. But even with that, we continued to keep close contact with the Muni Council as it moved forward.

WT: When was that?

EL: I don't have the exact date. The original meeting was 2001, so it would've probably been sometime in 2002, maybe 2003, give or take a few months there. But, again, we kept pretty close tabs in terms of what was going on there and paid very close attention, and it was maybe a couple of years later that the Central Post Office concept – and I don't know if you're familiar with that – grew out of the Muni Council. So, like I said, even though we weren't there at the table we were very much interactive with a lot of the participants and watching the progress very closely.

WT: I'll definitely want to be coming back to the ongoing evolution of electronic disclosure, but, to try and keep it into the chronological span, this is also when the September 11th attacks occurred. Now, there are two things, separate things that I've read about, which is, one, that it increased the push towards a more electronic marketplace for municipal bonds.

EL: Well, I think that was certainly one of the things that was pushing in that direction.

WT: Can you tell me a little bit about that relationship?

EL: Well, yes, I'm not sure how super directly it was, but I think it certainly was the idea that infrastructures weren't always going to work the way they were expected to work. There needed to be a lot more backup, a lot of ability to engage in ongoing transactions without having the immediacy of physical contact be a necessity of doing it. I think people understood that you couldn't have systems that were vulnerable to any kind of a systemic problem so that you had to have backups. So, I think it was not so much a direct impact, but it was kind of part of the overall feeling that you needed to have a much more fulsome way of engaging in business and keeping the markets open and effective that wouldn't be so vulnerable to that kind of a –

WT: What were some of the main practices that people were still doing, personally or –

EL: I'm trying to think, in 2001, I mean I'm not sure if I ever had my thinking cap on in that sense, thinking of it in that kind of context. But I think there was still a fair – yes, I'm thinking, I think the biggest thing was that you had a lot of the communication lines all going through one central line, and so one small area of the country became incapacitated and suddenly there was no ability to communicate, no ability to settle trades, no ability to ensure that the market could continue going, but I'm not sure if I recall any more specific connection between the two.

WT: Okay, and the other thing was that MSRB sought the authority to halt trading not long after that.

EL: Well certainly, yes, that was an interesting event, and I wasn't directly involved with that and so my recollection may not be 100-percent accurate. There was discussion between the MSRB and the SEC on the question, and so I'm not entirely sure from what direction the request came in. My recollection was that the SEC thought it would actually be a good idea for the regulator to be able to say, you know, if there's going to be a dislocation in the marketplace that maybe it's best to hold trading for a while.

And so we did float a proposal – and again I don't recall the specifics of it – to have the ability to, with certain safeguards, to say it would be unfair practice to engage in transactions with municipal securities under a certain set of circumstances. Again, I don't recall specifically what it said. I think there was some significant discomfort in the marketplace, because it wasn't a central market. So I think very quickly market participants felt that that wasn't the way they wanted to go, and ultimately the MSRB withdrew that proposal.

WT: To bring things into the MSRB, now I know at a certain point – it's not listed on your bio here – but you become general counsel, is that right?

EL: That's a good bit later.

WT: That's a good bit later?

EL: Yes.

WT: Okay. And then there's some question about MSRB term limits somewhere in here, as to whether or not board members might be permitted to sit two terms?

EL: That's right. I mean – and again, I don't recall the gyrations – but certainly the norm was that the board members would not sit for consecutive terms. I know our rules prohibited that for most of the time, and there was some ability to serve a second term if you'd only served a partial term. But by and large the feeling was that it was important to get a diversity of views on the board so that it was a positive for the organization to be able to have fresh, new perspectives on the board.

Regardless of where the rules stood in terms of the ability to serve some additional time after your initial term, there was always a prohibition from having the same firm follow on its previous representative on the board, so there wouldn't be a permanent Goldman seat on the board, you know, you always had to have some level of rotation in the organization.

Ultimately, that was something that was an important thing and the board spent a lot of time thinking about it from time to time. Because what happened is that you had a board that had three-year terms – there was rotation on and off the board – and so if there are particularly difficult issues, sometimes there was some frustration that someone might not have enough time on the board to be able to see a project through from beginning to end because some things took more than three years. And so, there's always some loss of institutional knowledge, some loss of continuity by having that short of terms. And so, like I said, on occasion people thought, well, maybe we should have a longer term or maybe we should have shorter terms, and I think it's a discussion that continues to happen over time. There's a balance. You have the fresh blood, you have broad representation by having the constant turnover, but then you have the constant need to reeducate, to bring people on board, so it's a tension.

In my view, it's never been a critical tension. I don't think the organization has ever been substantially hurt by having board members rotate off. There have been times when it's been nice to be able to have continued engagement. But the fact of the matter is, I think it wasn't until sometime in the mid-00s, the first time we brought back someone who had served a full term in the past and came back on the board to serve a full term going forward. That still has been very rare for us, to bring back for a full term someone who's previously served on the board, the idea being there are many, many very well-qualified people who can serve on the board.

WT: And as far as the composition of the board is concerned, I suppose we should wait until we get to the Dodd-Frank Act to discuss that.

EL: Whenever you like.

WT: Well, you mentioned derivatives and I'm interested in some of the other novel products surrounding municipal securities. I know you were directly involved with the question of 529 plans.

EL: Well, that was an interesting thing and that came on not too long after I joined the MSRB, which is one day we get a phone call from the SEC and the next day we get a phone call from some market participant saying, "You know, there are these products out there and we've issued some no-action letters saying that because they're issued by state and local governments they're not mutual funds, but they're also exempt as municipals, so how do they fit in?"

And so what they were – and there were a couple of products actually. It was 529 plans, which are basically state-sponsored mutual funds, they're aggregation of different citizens' investments and they're turned around and invested in other mutual funds. And there was also another product, which is the local government investment pools where you'd have a sponsor, a governmental sponsor of a pool that other local governments can invest in.

WT: That was the issue that originally came up in the Orange County case, right?

EL: That was one. Now, in that case it didn't really apply to us because that was fully administered by the local officials and not administered by broker-dealers. Remember, our rules only touch on broker-dealers. And so 529 plans, that is really when it first came into being for us, although there were some local government investment pools that dealers were involved in, where you had a structure where, in effect, a state would form a governmental mutual fund – but they're not a mutual fund because they're exempted from the mutual fund rules – and they would hire a broker-dealer and a fund manager to administer and to do the investment advisory work on the one side and do the marketing on the other side.

And the question was, well, what rules apply? And you know, up until then everyone had thought of municipal securities as debt securities, it was borrowing money and repaying interest, which of course made sense. I mean, how often do local governments issue equities? They don't. But in fact, these are equities, these are special kinds of equities, but they fell into the definition of municipal securities.

I was given the responsibility to work on that, and starting in '98 when the issue first came up and our first proposal was '99, I had a big hand in helping write those rules. And so what that really was, was a marriage of existing mutual fund standards which existed out there in the FINRA or SEC rules, but then tying them to some of the unique features of having a mutual fund that's run by a governmental entity.

One of the most unique features is that as a governmental entity they're exempt from the federal securities laws, and so, one, you can't write rules that apply to the entities, and, number two, because they're not limited by the '40 Act, the Investment Company Act, they can structure them in ways that weren't just like mutual funds. So you see interesting wrinkles that were a lot like mutual funds but not identical to them, and so you'd have to then be able to write broker-dealer rules that understood that the products that they are marketing aren't always going to be just like mutual funds. They're going to be a lot like them, but not just like them.

It was an interesting few years in trying to write those rules. When we first proposed them – and I mentioned this before about municipal securities being traditionally debt obligations – a little skirmish broke out with some commentators saying, “These aren’t municipal securities, because they’re not debt obligations.” So we actually had to spend some time, back before the Internet was so prevalent and easy to search, digging through the legislative history of the ’33 Act and ’34 Act and the ’75 Act, when we were first created, to really get the full picture of what they meant by municipal securities.

I think we made a pretty good case to say that, even though they talked about them in terms of being debt obligations, it wasn’t because they said that’s the limit of what municipal securities were, but that’s what they knew, and so they used the language of debt obligations to describe them. But what they really meant were any securities issued by state and local government. So I think we ultimately were able to convince the marketplace that, yes, in fact, as much as you don’t want the MSRB to write rules, we are obligated by our statute to write rules in this area. So that was a very different thing for the organization.

WT: Yes, quite interesting actually in terms of the nuances. Also, there are the VRDOs, speaking of debt obligations, and of course auction rate securities, which are an issue throughout that decade, I believe, well before the freeze.

EL: That’s right, and particularly auction rate securities was an area where, obviously, it probably caused the greatest mayhem, so to speak, during the financial crisis, that and the bond insurer downgrades. There had been, I’ll call it a temporary break, where a small number of auction rate securities auctions failed a couple of years before the financial crisis. And so there was some interest that the MSRB took in whether or not there was appropriate disclosure in that area.

I know TBMA came out with some best practices which the MSRB looked at them. We weren't really very excited about what those best practices had to say and so we certainly did not embrace them at the time. But I think ultimately the SEC got some comfort from the fact that the industry was starting to pay some attention. Unfortunately, I think it was some false comfort, because I think we saw when the financial crisis came and what happened with the auction rate securities was that it really was a product that had some significant problems.

WT: And you mentioned bond insurance. I know that that was increasing. It had been around for a little while, but was becoming increasingly prevalent.

EL: Oh, absolutely, but up until just before the financial crisis, I don't have exact figures but I think in the new-issue market, more than half were being insured. And I'll talk about some of the positives with that, which is that – or at least the perceived positives of that – it gave a real boost to liquidity of municipal securities to the extent that people could treat them a little bit more like a commodity. Even though the municipal market has so many different unique securities, a particular security may not trade very often, so people will always talk about a particular security not having a high level of liquidity. But, to the extent that you can treat one security just like another security, that increases the ability to kind of treat them interchangeably. So, there was a sense, then, that if you had AAA bond insured security then it was just like another AAA bond security, with the same quality, features, same maturity schedule, and so that helped in that sense. The problem, of course, was that when the bond insurers turned out not to be AAA anymore, you lost that level of liquidity and so that created dislocation in the marketplace.

Obviously, to the extent that you had investors who thought they had a AAA security and suddenly realized, well heck, it wasn't a AAA security anymore, that was a problem for the marketplace. So, you know, the downgrading of the bond insurers really was driven by not the muni marketplace but their desire to diversify into other products, and it was the other products that created the problem for the bond insurers. And so the source of the problem wasn't the municipal marketplace, but it ultimately came back to the municipal marketplace by really eliminating that AAA credit that so many issuers had relied on when they got their bonds insured.

WT: Did the MSRB have any jurisdiction with respect to bond ratings?

EL: Again, we don't in terms of the agencies. We certainly had rules around disclosure. For example, confirmation disclosures, if a broker-dealer sold a security that was not rated at the time, the rules said that you need to advise the customer of that in the confirmation. Whether a bond was rated, or what the rating is is one of many material facts that a broker-dealer needs to disclose and to consider when they're engaging in a transaction with a customer. So the ratings were part of what was expected to be considered in the process of doing a transaction, but we didn't have any regulatory authority over the ratings agencies themselves, again, they're not broker-dealers.

WT: And then the last products that I wanted to ask about are interest rate swaps, which have been around awhile, but then credit default swaps which were quite novel in the 2000s, for municipal bonds.

EL: That's right. And then again, those are things that, you know, we come back to a theme here. These are things that affect the marketplace, and the question becomes to what extent is the MSRB in a position to do anything about it? And I talked about it earlier, the question is our authority is on transactions in municipal securities, and so certainly the swap itself is something that we couldn't regulate.

The question was, are they sufficiently closely tied with the underwriting in connection with which they may have entered into to give us some residual authority? That was discussed a great deal, and I think there wasn't enough comfort that we did have that authority – particularly given that Congress had said thou shalt not regulate over-the-counter derivatives – so it was an area that the Board had increasing concerns around. We probably would like to have been in a position to write rules around it. Again, it is one of the things that led to the Dodd-Frank expansion of the MSRB's jurisdiction. In fact, I think our chair at the time testified about our inability to really reach some of the practices that probably did create some harm and so we wanted to have that authority.

WT: Speaking of that authority, I was wondering – I know that Chairman Cox, about 2007, made inquiries about the Tower Amendment. Did that echo down here in any way, or was that pretty much at his level?

EL: Well, I don't remember the specifics, but I do recall that there was a discussion around that. The MSRB's view had generally been that we were created in '75 as what I'll call a creature of the federal system of government. So, the idea is that while it was important to have protections in place of a securities regulator for investors that would, one, protect investors, but also help create kind of a uniform national marketplace. We were created with the clear understanding and dictate that we weren't a regulator of state and local governments. We were kind of the grease between the federal government and the state and local governments in the federal system of government, and so our calling was to regulate in that context. The MSRB has never taken the position of saying we need more power over state and local government issuers, and so we always stayed back from discussions around the Tower Amendment. That was a policy decision made by Congress in that when Congress says don't regulate, we don't regulate. If they tell us to regulate, then we do regulate.

And so it was always a matter of interest. At the same time it has always been our policy view that the more disclosure, the better. The better information that's in the marketplace, you know, that improves the marketplace. While never saying that Congress should provide us authority to require issuers to do something, we always felt it was important to issuers on their own to make the decision that better disclosure is better for them. It protects their citizens, it gives them better market access, it gives them better pricing on securities. We never – as much as you want to be able to put in a rule you think would be ideal, we always accepted the fact that we have fences around what we can do.

WT: Why don't we pick up the electronic disclosure bit again? You mentioned the Central Post Office earlier, but why don't we get the story that leads ultimately up to EMMA?

EL: Sure. So, as I mentioned, the MSRB was politely asked to step aside in the Muni Council, and so we stepped aside in terms of the Muni Council, but we continued to have interest not just with what the Muni Council did, but we said, okay, if we step back from the Muni Council, what can we continue to do in order to move this marketplace forward into the 21st century? Back in 2001, I think, we launched in 2002, we started a system we called EOS, which was the ability for underwriters to give us the official statement that they previously sent to us in paper form to be uploaded in PDF format to the MSRB as part of our MSIL system. It wasn't a requirement, but it was an option, and we saw the growth of that option being used over time.

In 2005 we moved from next-day transaction reporting under our old transaction reporting system to the real-time transaction reporting system, so that for most trades they would become available to the public in fifteen minutes. Now, at that point we didn't have a venue to make them available to the public. It was still through a data feed to the vendors. But we, in conjunction with – it had been called The Bond Market Association, now SIFMA – they agreed to put on their website, investinginbonds.com, a direct free feed to the public of the trade data. So, in January 2005 it was for the first time that the public investors would have complete free access to the trade data. So those were two key pieces of the evolution.

The thing that really kicked off the imminent development was us looking at where the SEC was going in the registered marketplace in connection with primary market disclosures. They were moving towards what they were calling "access equals delivery" to dematerialize primary market disclosure, instead of having papers sent around. The fact that registration statements and prospectuses were available on EDGAR, then available to others through other vendors electronically, they changed their rules to no longer require physical delivery of prospectuses but just said the fact that EDGAR had them was sufficient for purposes of access to investors.

And that had a lot of pluses. One, it was a lot cheaper for the marketplace so it was savings for issuers and for other people in the marketplace, and ultimately to investors. But also it made information more broadly available. So, rather than it just being an investor who gets the document, everyone gets the document, and so it really democratized information.

We wanted to do the same thing in the muni marketplace. The catch was, even though we were receiving disclosure documents, we didn't have a public, free, centralized display, and so in order to move to the electronic dissemination of primary market disclosure, we needed to create EMMA as EDGAR's little sister to make those documents available to the public, and so that really was what started that process. It was in 2006 that we first published a concept release saying, hey, we're thinking of moving to an electronic system, what did people think? And so that was kind of the early start.

WT: Meanwhile, the Central Post Office came in, in 2005, but that was entirely separate from MSRB.

EL: That's right. So the Muni Council, ultimately I guess they put out a request for a proposal for entities that would serve the function of being a single, central site where issuers could provide their continuing disclosure documents. They wouldn't themselves post them out to the public, but they would then pass those disclosures electronically onto all the NRMSIRs in the marketplace so that issuers could comply with their contractual obligation to provide continuing disclosure to all the NRMSIRs by giving it to this one central venue. That venue would then turn around and send them on to all the NRMSIRs, and they would get proof of delivery to the NRMSIRs of those documents.

So that – and you said it was 2005, that sounds about right – that's when that process started. Again, it really was a Central Post Office because they weren't the venue through which the public can get them. The public still had to go to the NRMSIRs. They had to pick which NRMSIR they wanted to go to, they had to go through whatever the process was to find them on their website - or some didn't have them available on the website – and would have to pay the cost that a particular private vendor would charge for receiving the documents.

But that was forward, I mean, it made it easier for issuers to make their submissions, it ensured the submissions that went through the Central Post Office made it to all the different venues they were supposed to go to. Before the Central Post Office was set up, one of the big criticisms – there were a couple I guess – was that not all the NRMSIRs had the same collection. For example, an issuer might only send it to one and not to all of them. And they all had very different indexing processes, so that it might be easy to find this NRMSIR's collection but very difficult to find that NRMSIR's collection, so there was a lack of uniformity.

The CPO, which is what people called it, helped to reduce that lack of uniformity by ensuring it went to all of them at the same time. So that was a positive step, and so that's something that was a good thing. And I think the marketplace found it beneficial, and it worked for a period of time until ultimately it stopped working.

WT: I interrupted you as you were getting into the creation of EMMA and the creation of that capability here at the MSRB. I know there was a little bit of pushback from the NRMSIRs, insofar as it was essentially displacing what they were doing, but maybe you can tell us about the process.

EL: Yes, I mean, I think it's fair to say there were probably some people who put in comments saying, you know, maybe you don't need to do that. I think what really gave impetus, in particular to when we decided to fold in the continuing disclosure, was what I'll call the collapse of the Central Post Office process. Again, EMMA started off at first blush to be a venue for official statements, primary market disclosures – because we had the trade data we always intended to put trade data in there as well. Early on in the vision we did intend to put continuing disclosures, but our intention at the time was to be a subscriber to one of the NRMSIRs. And so we would have to make an assessment of which one had the best collection, which one had the best feed to us, and take that data and put it onto the EMMA website.

As we were developing this, ultimately there was some litigation that started with Texas MAC regarding the Central Post Office and some of the functionality, that then created some problems for the market. And I think there was a very quick consensus in the marketplace that maybe this NRMSIR system wasn't the way to go, because, one, the CPO didn't solve all the problems – it did make things better but didn't solve all the problems – and, two, if some of the best features or some of the most helpful features of the CPO were potentially subject to some dispute, maybe this wasn't a long-term solution.

So it was at that point in time where there was a meeting of the minds from the MSRB side saying hey, we're putting up this utility. We can easily receive the documents and process them all centrally. There was a sense in the industry that maybe that made sense.

There was a sense at the SEC that maybe that made sense. And so, really, everything all came together that this other venue that was being built for other purposes would be the perfect place to put continuing disclosures. So I think there were some in the market that said, hey, maybe you don't need to do that, but I think by and large it was pretty much an overwhelming agreement that it really made sense to move forward with the central system.

WT: And this is the first time that the transaction reporting and the disclosure come together into the single unit?

EL: That's right. That actually, I think, was one of the things that really made it particularly powerful is to have that trade data right there with the disclosure documents at the same place.

WT: Okay. I'm going to run an interesting hypothesis by you that Martha Haines had when I spoke to her, which is that if electronic disclosure had started maybe four or five years later than it originally did, that a system such as EMMA might have come into place much sooner than it did. I know that she said that it was something of her personal project and I thought it was an interesting statement. I know it's a counterfactual, so we can't speak authoritatively about it. [Note by WT: It was actually Dean Pope who hypothesized that if the amendments to Rule 15c2-12 had been made five years later, an EMMA-type system might have come about sooner than it did.]

EL: So what's the theory again?

WT: The theory is that if they had started, I guess maybe dating from the MSIL system or certainly the NRMSIRs and had started maybe four or five years after that, it would've been easier to put EMMA into place than it ultimately was starting earlier.

EL: So you're saying if we started earlier?

WT: If you'd started later, actually.

EL: Oh, later. I'm not sure about that. I don't know. That's a hard one. You know, I think early on – and this is way before EMMA, back when MSIL was set up – there was actually a lot more opposition then than there was when EMMA got set up, because I think there was some concern in the issuer community back in the late '80s or early '90s that that would be the first step to creating a registration process like on the corporate side. And so, when we set up MSIL, we actually had to be very explicit that we weren't going to do certain things. We were simply a utility, we weren't going to put obligations on issuers, and we weren't going to make them available to the public for free. We were just going to be a behind-the-scenes utility, just to keep people kind of comforted that we weren't going to be an indirect regulator of issuers.

In fact, it was a little bit of that overhang that – not the only reason, but one of the reasons – why we actually, rather than making EMMA part of the MSRB regulatory website, we actually created a separate website so it had a separate identity away from the MSRB. So it was more clear to the world that this was a utility function and not a regulatory function that we were engaging in, at least as far as continuing disclosures were concerned. But if we had waited longer, that's an interesting theory

WT: Yes, I just thought I'd run it by you and see what you said. So, then, here at the MSRB, this is around the time that Kit Taylor finally leaves after twenty-nine years, Lynette Kelly comes in. What was the institutional transition like? I've heard that there was some controversy surrounding it, but you can speak as much or as little as –

EL: Yes, I'm not really sure it was a controversy. I think they came in with different styles. I think both had a tremendous depth of knowledge of the marketplace and tremendous dedication to the marketplace. I think each person has their own style and their own ways of doing things. I think certainly Lynette very early on embraced the idea of moving forward with EMMA and she put her full weight behind, it and was instrumental in kind of getting the agreement between us and the SEC that we would act as a central repository.

So, even though the process to set up EMMA had started before her arrival and during Kit Taylor's time – and so we already had the plans to create the central website with the primary market disclosures, trade data, and at that point with a feed from one of the NRMSIRs – I think she helped to make the leap to actually make it happen by putting her full weight behind it, her and Frank Chin, who was chairman of the Board at the time.

Both were very strong proponents of doing this. So, I think it helped to make sure it got across the finish line and then also helped to really bring on board another feature we haven't talked about, although we touched on the auction rate security market, which is having the data from the auctions and from VRDO resets on the website, as well. So, I think that was an important part and I think that was something she brought to the table, coming to the Board.

WT: Was she pretty familiar here from her time at TBMA and SIFMA?

EL: Oh, sure. I was able to find many letters that she had written to me, or letters I'd written to her over the years in her other role, so we worked quite a bit with her. I think the last couple of years she had moved a little bit away on some broader issues at SIFMA, but certainly we'd worked with her quite a bit over the years.

WT: Why don't we move, unless you have anything else to add, into the final phase of, I guess, our history, which would be the aftermath of the financial crisis, Dodd-Frank and all that sort of thing. I don't know where the good place is to begin. We might talk about – we were talking a little bit about cases such as Orange County when we first started, but I know there were cases such as, there were enforcement actions against Miami, San Diego in the mid-2000s, and then ultimately you get into Jefferson County, I think, starting around 2008. What were the impacts of these sorts of things, especially after Jefferson County was the big blow up?

EL: Well, again, there were cases where there were activities that were happening – some involved broker-dealers, many of them didn't involve broker-dealers – where the Board felt that there were enough holes in terms of the ability of people to properly oversee and to regulate. That led to our call to have a broader set of regulations in the marketplace, to reach a broader set of professionals, give us a broader set of authority over products in that area, that I think ultimately led to the Dodd-Frank provisions on municipal advisors. I think it was the MSRB that first proposed that there should be regulation of non-broker-dealer financial advisors. Broker-dealer financial advisors were already regulated. We were very happy to see that Dodd-Frank included advice on municipal derivatives because that, for the first time, gave us some clear authority in the area around that.

So I think those things you mentioned, and there were other things – Jefferson County is an example of a relatively big issuer dealing with some of these issues – but there were lots of smaller issuers around the country who got involved in swaps and things like that, where you say you're not sure they really fully understood what was going on when they decided to do the swap. They heard the good part of the deal – which is you get the up-front payment and you get lower debt service overall if the market stays the way you expect it to stay – but maybe didn't really understand what happened if the market turned the wrong way. And so it's that whole set of problems that emerged during the financial crisis, and before – not all during the financial crisis – that really kind of crystalized our view that there needed to be kind of a broader set of authorities on our part.

WT: Now, the MSRB does offer guidance to issuers, is that correct?

EL: Well, from time to time we will speak on issues in the marketplace. We don't normally lecture issuers on what they should or should not do. In certain areas, for example, we'll provide some guidance about how best to use EMMA to better communicate with the marketplace. We don't tell issuers how best to levy their taxes in order to make sure they are able to cover their debt service and to meet their public needs. That's a little bit of a delicate balance as to how far we go on those types of issues.

We've talked a lot about rulemaking and our systems and those are two key tools. The rulemaking is certainly where our statutory calling is, our transparency systems fit well into that, but we do engage in what we call outreach, education and market leadership. Some of that education and outreach deals with those primary areas of rulemaking and systems, but also deals with – you know, the MSRB really has a significant expertise in the marketplace that goes beyond just the four corners of our rulemaking authority, but to understanding how the market works. And so we do from time to time talk about it, provide education, potentially advocate on issues that affect the marketplace more broadly.

Again, we try not to overstep what people's views of our role in the marketplace. We try to be very helpful; we try to work very closely with other organizations. A lot of our outreach involves things very similar to what led to the creation of the Muni Council, which are we have these twice-a-year now roundtables with industry market participants, again all the same types of people that were part of the Muni Council, just so that people meet around the table and can talk about the issues that are important to them.

So oftentimes we'll host this meeting here. We may not have any ultimate direct role in a particular matter, but the three or four groups that do have a direct role then may get together for the first time and start agreeing to work on initiatives on a voluntary basis in that area. And so a lot of initiatives that happen in the marketplace have had their initial germ come from these roundtables that we hold. For example, there was the bank loan voluntary disclosure initiative that I think a lot of people around the table that we've brought together have agreed to go out and do – that's in this case and a number of other initiatives as well.

WT: We've spoken about auction rates a little bit, but of course this is the period of the freeze. Is there anything we ought to add about that period and its aftermath?

EL: Well, I think it was, again, something that led to one of the key features of EMMA and I think EMMA has helped people get a better picture of what goes on in that market. You know, certainly no one's issuing auction rate securities now. People are finding other ways to meet those needs, ways they understand better. I think that, and again the bond insurer downgrade, really woke people up to the fact that a lot of these theoretical risks that they think about can really happen, and so people pay a lot more attention to, one, providing better risk disclosure and to doing a better job of assessing it, and, two, accepting that they in fact can happen.

So as much pain as those episodes caused – and certainly individual investors did suffer through it – I think the market has taken, we hope, to heart the lesson that you've got to take these things that can sound like a burden, i.e., describe to your counter-party all the risks that are relevant to a particular transaction, and realize that it actually matters. So hopefully there's learning. We know we have, as a regulator, and we think that the people in the marketplace who are very serious about their work certainly have taken these things to heart, and so we think ultimately there's some improvement in market practices as a result of lessons learned.

WT: Are there any particular issues that came up around the Build America Bonds?

EL: Well, it was a different type of product. We, I think, published a notice reminding people that our rules applied because they were taxable products, and to some extent many firms actually traded them off of their taxable desks as opposed to their muni desks. It brought in a new contingent of investors that really weren't typically in the municipal marketplace, and so made dealers focus on how they interacted with them and how they provide full disclosure in the marketplace.

I think once sequestration came in, it raised a lot of issues in terms of the fact that some of the subsidies coming from the federal government were being held back and that created a lot of consternation in the marketplace, not so much for us as a regulator, although I think we did speak to those as well, the issue about what the impact of sequestration would be. But because it was a new product in many respects it did make us stop and think, how do our rules apply?

And that's something that's happened throughout at least the time I've been at the Board, is every few years something new comes into the marketplace and it does make us stop and think about, well, how do our rules really work when something new comes into the market? And so it's always a little bit of a refresh on our part, whenever that comes into the marketplace in terms of how we handle our duties in the market.

WT: Okay. So now let's get to the Dodd-Frank legislation. Of course we've alluded to it on a number of occasions and the concerns that were addressed within it, but to what degree was MSRB consulted in the whole legislation process?

EL: Sure. As we mentioned, we advocated for having municipal advisory regulation and I think we published a report on that. I think our chair had testified in one of the congressional committees on that. Certainly from time to time the staff, primarily on the Senate side, the Senate Banking Committee would consult with us on our views of certain things in the legislation. I know we were just one of many organizations they were consulting with, and so we were aware of how it was coming together. When asked, we'd provide some views in terms of how things worked in the marketplace so they could do a better job in drafting that. I wouldn't say that we were a driver of how it was drafted ultimately, but certainly we had an opportunity to provide some insights.

WT: And so on the other side of that being signed, there was of course a very important rulemaking process, could you tell me a little bit about that?

EL: Well, part of the rulemaking process after Dodd-Frank is certainly affected by our changing composition of the Board, so I'll spend a little time on that. Dodd-Frank, in addition to giving us authority on municipal advisors and over a broader set of products, also changed the composition of the Board to being a majority public board with municipal advisor representation.

So, before Dodd-Frank we had a fifteen member board, we had ten who were broker-dealers or banks, five who were public members, including at least one issuer and one investor. After Dodd-Frank it was majority public, which meant we increased the size of the Board in order to have full representation, so we had twenty-one members, ten of which are regulated entities – seven of which are broker-dealers and banks, three of which are municipal advisors. The other eleven, we have several investors, several issuers and other people who have knowledge of the marketplace. Dodd-Frank actually requires that public members have some knowledge of the marketplace.

And so that change in composition I think brought some fresh perspective, and if nothing else it brought in municipal advisors who were writing rules for the first time on themselves. So I think we spent a good deal of time very early on educating ourselves on what the extent of the statutory authority was. We obviously had a significant amount of knowledge really from the broker-dealer perspective of what municipal advisors did, but now we had new people on board to give us that perspective.

We actually started off very quickly in the rulemaking process, because we thought it was important just to take that mandate and run with it. And so we put in place a couple of rules, we had registration rules so municipal advisors had to come to us and register so we knew who they were and they knew who we were, and then we also made sure that they became subject to our core fair practice rule. We have a Rule G-17 that basically says you need to deal fairly with all people in the marketplace and not lie, cheat or steal, and we thought that was important. And then it flew through, because, of course, how can you dispute that. So municipal advisors became subject to that.

We then started the process, probably starting in early 2011 I think is right, to start writing some core rules around municipal advisors. Dodd-Frank made explicit the fact that municipal advisors had a fiduciary duty to their state and local government clients; we started writing a rule on what it meant to have a fiduciary duty. We started writing rules on more details around fair practice, rules around pay-to-play, two or three other proposals that we went out for comment on and got feedback from the marketplace.

During that time the SEC was in its own rulemaking process. They were charged with registering municipal advisors with themselves, and also as part of that process providing a little bit more color around what the Dodd-Frank definition of municipal advisor meant. They put out a proposal at the end of 2010. People have issues with it, they received over

1,000 comments, and so they were working through that. And when it became clear to them –

WT: The idea was mainly that it was too broad of a definition?

EL: I think different people have different views, but I think by and large most people thought it was too broad and thought it should be narrowed in about twenty different respects – I mean different people, different views of it – and so I think the SEC was trying to very carefully and thoughtfully go through the comments and try and assess them. But during that time, as they were assessing the comments, our rulemaking was moving forward. And so, as it got closer and closer to being finalized, I think the consensus that started to form at the SEC, at the MSRB, and in the industry, was that maybe it wasn't time to write a rule yet, because, if nothing else, it was unclear whether everyone who might be a municipal advisor was actually paying attention because of the ambiguity of the definition.

So the question was, did we get full feedback from the marketplace? Were we really in a position for people to start complying with the rules? And so it was some time during the summer of 2011 that the MSRB decided that we were going to pull back our rules. And the SEC was comfortable with this, and in fact I think they would agree with us, we would pull back our rulemaking and wait until the SEC was able to finalize its rule on municipal advisors. And so we did pull back on our rulemaking at the time, kept a very close eye on what was happening in the marketplace, and provided continued outreach to the municipal advisor community, but waited until the SEC had finalized its rulemaking, which finally happened at the end of last year.

WT: Now, when one refers to the Dodd-Frank Act making the MSRB responsible for protecting issuers as well as investors, did that refer mainly to the municipal advisor aspect of things?

EL: Well, I think it's hard to read everyone's mind in Congress, but I think the constant – and the term is "municipal entities," it's a broader term than narrowly the issuers – that term came into the statute hand-in-hand with municipal advisor regulation, and municipal advisors, you know, they advise state and local governments. It also brought "obligated persons," too, into the definition.

Having said that, it's not been the view, I don't think there's any evidence that the view was – it only was in the statute because of municipal advisors, in this sense. Even before Dodd-Frank, we had our fair practice rule G-17 and basically said broker-dealers – and advisors weren't covered at that point – need to deal fairly with all people in the marketplace. And so it wasn't limited just to investors, and we had interpreted the rule to say that dealers had a fair dealing duty to issuers of municipal securities.

And so it was certainly appropriate to say, well, Dodd-Frank says specifically we should be protecting municipal entities, that in fact the rules that were protecting municipal entities wouldn't just be limited to rules on municipal advisors, it would be all the rules we would write so that it would be rules on dealers and municipal advisors. We thought that was very consistent with where we were, it made it more clear; it made it more explicit that there was an obligation, that in fact there was an obligation, a fair practice obligation to issuers even before Dodd-Frank.

WT: Now, there are also rules over brokers' brokers. I'm just curious if that's kind of a situation that's fairly peculiar to the municipal securities area.

EL: Yes – I mean I wouldn't say it's peculiar. They exist in other markets, but I think they have a bigger role in the municipal marketplace.

WT: Because there's no exchange?

EL: That's right. There aren't the central – well, now there are some ATSs – but by and large there weren't exchanges, and so if a dealer had a bond that they needed to sell and they knew nothing about the bond because their customer just said "I need to get rid of these bonds," that became, not the only venue, but one of the venues through which they could say, "Hey, brokers' brokers, do a bid wanted on this and you'll bring in all your potential bidders to do it," and so they became one of the avenues through which dealers could get out to the broader marketplace.

We engaged in some rulemaking a few years back on brokers' brokers. There had been some enforcement actions on the part of – I think primarily FINRA but I think SEC as well – calling into question some of the practices of brokers' brokers, and so we engaged in a pretty thorough rulemaking process that, I can't remember exactly, maybe 2010 or so, finished up with, or maybe a little bit after that, with our Rule G-43 which is the brokers' brokers rule, which laid down some core duties and obligations of brokers' brokers in the muni marketplace. They're not unique. They exist elsewhere, but they do have a unique position in this marketplace.

WT: If I can turn to your career again, just briefly, we mentioned earlier your move to general counsel and you said that that was later than the time period that we were talking about. Now of course you're deputy director?

EL: Right.

WT: Right, so how have your responsibilities changed?

EL: They've evolved over time. We were a small organization so, you know, people don't have a single silo. And so, before becoming general counsel in the legal department, I took off my lawyer's hat for six months and project managed the EMMA system. I put the lawyer hat back on, and was still involved with EMMA even when I became general counsel. And for a while I actually did the dual role of chief legal officer and deputy executive director, and so it's been an evolution over time.

I think it's fair to say right now what I do is kind of straddle the two sides of the organization, the rulemaking side and the transparency side, to ensure that they're both talking to each other and looking at the broader market implications of what they do. So sometimes, if there's an issue in the marketplace, maybe the best response is a rule, maybe the best response is a market transparency initiative, maybe a bit of both, so what I really concentrate on now are those broader strategic areas.

In 2012 we published our long-range plan for market transparency systems. It's one of the things I led, and part of that was to look at the broader market structure implications. So I think a lot of what I do now is really focused on market structure issues and broader questions of how the market operates and how our rules and systems interact with the market to move those forward.

WT: Okay. So why don't we just talk a little bit about the present, what's going on at the moment, insofar as you can?

EL: Yes, sure. We are hot and heavy now, so to speak, on municipal advisor rulemaking. We have now proposed a couple of rules, one on the core duties of municipal advisors that has gone out for comment, and so we're getting all the feedback from the marketplace. Some people love it, some people say make some changes. That's an important part of what we do, we have that interaction with market participants to really get the rules right. And so we started that process. We have a stable of rules still to come on that, proposals to come on that.

We are spending a lot of time moving forward on our long-range plan for the market transparency system, so looking to evolve EMMA to what we call EMMA 2.0. I'm not sure if there's a bright line between 1.0 and 2.0, but we'll know it when we get there. One of the core pieces of that is what we've dubbed for now the central transparency platform. What that really is, the idea there is that we evolve the trade reporting system that we've built up until now into a next-generation that would provide a more interactive experience for users to be able to see what's happening in the market today, to see how that links to the disclosure documents that EMMA has, have some tools to get a better sense of where the market is, things like yield curves, the ability to find similar securities and see how they're behaving in the marketplace.

We last year published a couple of concept releases around improving the trade reporting system, but also potentially bringing in pre-trade information, bid and offer information into the system. That's something that will take some time to really work through how best to do that, whether there are particular subsets to the data, whether the data's clean enough, how effective it is, how useful it is, how well-understood it would be, so that's a process over many years to try to get to a final form of that. So, really, a lot of what we're doing now is some of the core work to evolve our transparency systems to be a much more effective centralized system.

The central transparency platform is not intended to be an exchange, but it may be one step removed from that, which is a central venue for all the data so that you know where to go to find out what's happening in the market today, and then you go to the various execution facilities to do your transactions.

So those are two very important areas in which we're spending a lot of time. We are also working with the Securities and Exchange Commission. They published their report on the municipal marketplace a few months after our own long-range plan. A couple of things: one is that they said MSRB, keep working on the long-range plan. We like what you said and we want you to keep working on the systems. And then they had some ideas about rulemaking in the marketplace, particularly in areas to improve trade execution, improve transparency to customers, and we're working with the SEC on those ideas. They all make sense to some extent. The question is, do you need to do ten different rules or is it pick a little bit of this one, pick a little bit of that one? Which is the one that makes most sense for the marketplace? And a lot of that does dovetail into the question of market structure and market transparency, so that's keeping us busy.

WT: I meant to ask, the DTCC's New Issue Information Dissemination System, I guess that is mainly a separate thing on account of the fact that the MSRB doesn't deal with new issues directly?

EL: Well, it's actually an initiative that we – although we were very much involved with, I mean we worked with the industry, worked with DTCC to make it so that the information that was flowing through that system would ultimately find its way onto EMMA. Before the NIIDS system, people call it NIIDS, before that system was in place, information would need to flow during the new issue marketplace to the market so people would be able to execute their trades. It was a little cumbersome, not very efficient. Sometimes it took a long time for people, for dealers away from the syndicate to have the information they needed to be able to execute trades in the market. So it was felt that would improve the efficiency on that side of the marketplace.

By the same time, we came to the conclusion that it made sense to have the data that flowed to DTCC through that system also be the same data that feeds into the EMMA system, its primary market system, so that, instead of having to go to DTCC and give them some data, come to the MSRB and give us some data, we would simply use the data going to DTCC to help feed the EMMA system in terms of the primary market information.

We've been able to achieve, I'll say, 80 percent of our goal of straight-through processing of that data. There's still some data elements that we're working on to see if we can get that work flowing more efficiently, but that's an important initiative that the marketplace took on and that DTCC took on that we were able to leverage off of for our systems.

WT: Okay, and then finally, to what extent do things that are in the news in the municipal marketplace – of course we have Detroit, the cases of Harrisburg, Miami again, your hometown I guess – to what extent do those affect things here at the MSRB, because it's not directly –

EL: No, that's right. You know, different issues affect us in different ways. We certainly are watching the Detroit proceedings very closely. We very quickly put together the links on our EMMA system for people to find the underlying debt that was part of the whole bankruptcy matter, but we're watching very closely to see what comes out of that.

On some of the SEC enforcement actions, we actually looked at those very closely and published last year an advisory to the marketplace around particularly the Harrisburg case, because one of the things that the SEC found was, because the issuer failed to make their EMMA submissions, there was a vacuum where investors expected to find the disclosure, and so they went hunting for disclosure elsewhere.

We tried to make the point that issuers, put aside your contractual obligations, are best served by fully feeding, so to speak, the system where investors expect to find a disclosure. And so our point to the marketplace was, not only meet your 15c2-12 obligations, but consider providing additional voluntary disclosures, which the EMMA system can take, so that when investors go to EMMA they're going to find the information they need, and that's obviously a huge benefit to investors, point one, but number two is to the extent that the investors find what they expect to find when they go looking for it at EMMA, they're going to be less likely to go try to find it someplace else.

Issuers have always had the concern that political speech occurs and sometimes their officials will say things that may not be meant for the securities marketplace, and so that's always been a concern. And the Harrisburg case showed that you can actually have some significant consequence when political speech can become a securities law issue, and we tried to make the case that to the extent that you have your securities law disclosures fully met and well-understood and in a central place, you're going to be less exposed on the political speech. So we actually tried to explain to the marketplace that that's why they should be using EMMA more than they do now.

WT: All right. Well, this has all been extremely informational, but if you have anything else to add, we've been at it a while.

EL: No, I'm good.

WT: All right, terrific. Well, thank you very much.

EL: Thank you.

[End]