



BEST PRACTICE

Selecting and Managing Municipal Advisors

BACKGROUND:

Note: This Best Practice (BP) is one of a group of five relating to the sale of bonds. These five BPs should be read and considered in conjunction with each other because of the interaction of the processes to which they apply. The five BPs are:

Selecting and Managing the Method of Sale of Municipal Bonds

Selecting and Managing Municipal Advisors

Selecting Bond Counsel

Selecting Underwriters for Negotiated Bond Sales

Pricing Bonds in a Negotiated Sale

State and local governments engage municipal advisors to assist in the structuring and issuance of bonds whether through a competitive or a negotiated sale process. While governments may hire municipal advisors for other types of financial transactions, such as investments and swaps, this Best Practice is focused on municipal advisors used primarily in conjunction with a bond sale. A municipal advisor represents the issuer in the sale of bonds, and unlike other professionals involved in a bond sale, has an explicit fiduciary duty to the issuer per the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

Additionally, with the implementation of the 2010 Dodd-Frank Act, municipal advisors must register with the Securities and Exchange Commission (SEC) and Municipal Securities Rulemaking Board (MSRB) and meet professional and testing standards. Issuers should be aware that MSRB Rule G-23 prohibits a broker-dealer firm that also provides financial advisory services (in contrast to a non-broker-dealer municipal advisor) from serving as a municipal advisor to the issuer and an underwriter on the same transaction. Finally, it is important for issuers to become familiar with municipal advisor and underwriter responsibilities as discussed in the materials related to the SEC's Municipal Advisor Rule. Resources to help issuers become familiar with the Rule are included in the references section of this document.

RECOMMENDATION:

The Government Finance Officers Association (GFOA) recommends that issuers hire a municipal advisor prior to the undertaking of a debt financing unless the issuer has sufficient in-house expertise and access to current bond market information. Issuers should assure themselves that the selected municipal advisor has the necessary expertise to assist the issuer in determining the best type of financing for the government, selecting other finance professionals, planning the bond sale and successfully selling and closing the bonds. While a municipal advisor plays a key role on the

financing team, it is important to note that the issuer remains in control of the decision making process necessary for the issuance and sale of the bonds or implementing the financing.

The GFOA recommends that issuers select municipal advisors on the basis of merit using a competitive process and that issuers review those relationships periodically. A competitive process using a request for proposals (RFP) or request for qualifications (RFQ) process as applicable allows the issuer to compare the qualifications of proposers and to select the most qualified firm based on the scope of services and evaluation criteria outlined in the RFP. Standards related to the selection and hiring of municipal advisors should also be included in a government's debt management policy. The selection and use of municipal advisors may vary depending on the level of municipal market knowledge, expertise, and experience of the issuer's staff.

Before starting the RFP process issuers should decide whether the municipal advisor will assist the issuer in determining whether to do a competitive or negotiated sale. Additionally, the issuer should determine if it is seeking one municipal advisor for a specific transaction or a pool of municipal advisors to select from for future transactions. Small governments may be looking to hire a municipal advisor to assist with a single transaction, whereas larger governments may retain a municipal advisor to assist them with a broad scope of work, in addition to possibly creating a pool of advisors to choose from for transactions that the government anticipates doing for a period of time (e.g., 3 years). The RFP then can be carefully written in order to result in the type of relationship desired by the issuer. Additionally, issuers should write the RFP to comply with applicable procurement requirements.

If an issuer is contemplating the possibility of selling bonds through a negotiated sale, the municipal advisor should be retained prior to selecting the underwriter(s). This allows the issuer to have professional services available to advise on the appropriate method of sale, and if a negotiated sale is selected, to prepare the underwriter RFP and assist in the evaluation of the underwriter responses.

No firm should be given an unfair advantage in the RFP process. Procedures should be established for communicating with potential proposers, determining how and over what time period questions will be addressed and determining when contacts with proposers will be restricted.

Due to potential conflicts of interest, the issuer also should enact a policy regarding whether, and under what circumstances, it would permit a firm to serve as an underwriter on one transaction and a municipal advisor on another transaction. Additionally, when an issuer has a municipal advisor and the issuer is considering hiring that advisor to serve as a broker-dealer on a different negotiated bond transaction, the appearance of a conflict may exist.

Furthermore, each government should decide for itself if they choose to use only non-broker-dealer affiliated municipal advisors or municipal advisors affiliated with broker-dealer firms, and incorporate this into their debt management policies.

Request for Proposal Content. The RFP should include at least the following components:

1. The municipal advisor is registered with the SEC and MSRB. Issuers can determine this by visiting the SEC website at <https://tts.sec.gov/MATR/index.html> and the MSRB's municipal advisor registration page at <http://www.msrb.org/msrb1/pqweb/MARegistrants.asp>.
2. A clear and concise description of the scope of work, specifying the length of the contract and indicating whether joint proposals with other firms are acceptable.

3. Clarity on whether the issuer reserves the right to select more than one municipal advisor or to form municipal advisory teams.
4. A requirement that all fee structures be presented in a standard format. Issuers also should ask all proposers to identify which fees are to be proposed on a "not-to-exceed" basis, describe any conditions attached to their fee proposal, and explicitly state which costs are included in the fee proposal and which costs are to be reimbursed. Any MSRB fees imposed upon municipal advisors should not be passed through to the issuer.
5. A requirement that the proposer provide at least three references from other public-sector clients, preferably from ones that the firm provided similar services to those proposed to be undertaken as the result of the RFP.
6. A description of the objective evaluation and selection criteria and explanation of how proposals will be evaluated.

Requested Proposer Responses. RFPs should request relevant information related to the areas listed below in order to distinguish each firm's qualifications and experience, including:

1. Relevant experience of the individuals to be assigned to the issuer, identification of the individual in charge of day-to-day management, and the percentage of time committed for each individual on the account.
2. Relevant experience of the firm with financings of the issuer or comparable issuers and financings of similar size, types and structures, including financings in same state.
3. Discussion of the firm's municipal advisory experience necessary to assist issuers with either competitive or negotiated sales.
4. Demonstration of the firm's understanding of the issuer's financial situation, including ideas on how the issuer should approach financing issues such as bond structures, credit rating strategies and investor marketing strategies.
5. Demonstration of the firm's knowledge of local political, economic, legal or other issues that may affect the proposed financing.
6. Discussion of the firm's familiarity with GFOA's Best Practices relating to the selling of bonds and the selection of finance professionals.
7. Disclosure of the firm's affiliation or relationship with any broker-dealer and whether any personnel of the municipal advisor firm who would provide advice to the issuer were associated with a broker-dealer firm within the two years preceding the RFP.
8. Analytic capability of the firm and assigned individuals and the availability of ongoing training and educational services that could be provided to the issuer.
9. Description of the firm's access to sources of current market information to assist in pricing of negotiated sales and information to assist in the issuer in planning and executing competitive sales.
10. Amounts and types of insurance carried, including the deductible amount, to cover errors and omissions, improper judgments, or negligence.
11. Disclosure of any finder's fees, fee splitting, payments to consultants, or other contractual arrangements of the firm that could present a real or perceived conflict of interest.
12. Disclosure of any pending investigation of the firm or enforcement or disciplinary actions taken within the past three years by the SEC, FINRA, MSRB, or other regulatory bodies.

Additional Considerations. Issuers should also consider the following in conducting the municipal advisor selection process:

1. Take steps to maximize the number of respondents by posting the RFP on the government's web site, using mailing lists, media advertising, resources of the GFOA and applicable professional directories.

2. Allow adequate time for firms to develop their responses to the RFP. Two weeks should be appropriate for all but the most complicated RFPs.
3. Establish evaluation procedures and a systematic rating process, conduct interviews with proposers, and undertake reference checks. Where practicable, one individual should check all references using a standard set of questions to promote consistency. To remove any appearance of a conflict of interest resulting from political contributions or other activities, elected officials should not be part of the selection team.
4. Document and retain the description of how the selection of the municipal advisor was made and the rankings of each firm.
5. Ensure that federal regulations and any state and local regulations, standards or policies related to the disclosure of gifts, political contributions, or other financial arrangements are met.

Basis of Compensation. Fees paid to municipal advisors should be on an hourly or retainer basis, reflecting the nature of the services to the issuer. Generally, municipal advisory fees should not be paid on a contingent basis to remove the potential incentive for the municipal advisor to provide advice that might unnecessarily lead to the issuance of bonds. GFOA recognizes, however, that this may be difficult given the financial constraints of many issuers. In the case of contingent compensation arrangements, issuers should undertake ongoing due diligence to ensure that the financing plan remains appropriate for the issuer's needs. Issuers should include a provision in the RFP prohibiting any firm from engaging in activities on behalf of the issuer that produce a direct or indirect financial gain for the municipal advisor, other than the agreed-upon compensation, without the issuer's informed consent.

Contract for Municipal Advisory Services. Issuers should have a written contract for municipal advisory services that should detail the scope of services and basis of compensation. As part of the RFP package, the issuer may also include a "Form of Contract" which incorporates elements and provisions conforming to prevailing law and procurement processes and requires RFP respondents to comment on the acceptability of the Form of Contract. The comments on the acceptability of the Form of Contract should be part of the evaluation process. The contract development process should allow for reasonable negotiation over the final terms of the contract. A final negotiated contract should make clear those services that will be included within the basic municipal advisor fee and any services or reimbursable expenses that might be billed separately. Additionally, the contract should be clear that the municipal advisor will only receive compensation for work specifically authorized by the issuer to avoid incurring expenses for work not authorized by the issuer.

References:

- Debt 101: Issuing Bonds and Your Continuing Obligations, 2020.
- GFOA Issue Brief: SEC Municipal Advisor Rule
- SEC Municipal Advisor Rule
- SEC MA Rule Frequently Asked Questions
- Best Practices Optimizing Debt Management, Government Finance Review, February 2013
- GFOA Best Practice: Pricing Bonds in a Negotiated Sale
- GFOA Best Practice: Selecting Bond Counsel
- GFOA Best Practice: Selecting and Managing the Engagement of Underwriters for Negotiated Bond Sales
- GFOA Best Practice: Selecting and Managing the Method of Sale of State and Local Government Bonds
- MSRB Rule G-23

