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July 25, 2012

Mr. Alan D. Polsky
Chair of the Board of Directors
Municipal Securities Rulemaking Board
1900 Duke Street
Alexandria, VA 22314

Dear Mr. Polsky:

The Committee on Oversight and Government Reform (Committee) is conducting oversight of the use of economic analysis in financial services regulation. The Committee has been concerned with the role and use of cost-benefit analysis in rulemaking at the U.S. Securities and Exchange Commission (SEC). Significant and inexcusable deficiencies in this analysis have drawn strong criticism from the U.S. Court of Appeals for the District of Columbia Circuit,[1] this Committee,[2] the Administration,[3] stakeholders,[4] and scholars.[5]

On March 16, 2012, the SEC's Office of the General Counsel and the Division of Risk, Strategy, and Financial Innovation circulated a memorandum entitled Current Guidance on Economic Analysis in SEC Rulemakings (Current Guidance).[6] The Current Guidance contains a set of clear procedural directives to all SEC rulewriting staff mandating the application of rigorous economic analysis. In an effort to inform both SEC staff and the public of the specific and mandatory nature of the Current Guidance, the Commission has posted the document on its website.[7]

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[1] *See, e.g., Business Roundtable v. SEC*, 647 F. 3d 1144, 1148-49 (D.C. Cir. 2011)
[2] *See generally The SEC's Aversion to Cost-Benefit Analysis: Hearing Before the Subcomm. on TARP, Financial Services and Bailouts of Public and Private Programs of the H. Comm. on Oversight and Gov't Reform*, 112th Cong. (2012) [hereinafter *Hearing I*].
[3] Exec. Order No. 13,563, 76 Fed. Reg. 3,821 (Jan. 21, 2011).
[4] *See, e.g.*, Letter from Hal S. Scott, Director, Committee on Capital Markets, et al., to Tim Johnson, Chairman, Sen. Comm. on Banking, Housing, and Urban Affairs, et al., Mar. 7, 2012, *available at* http://capmktsreg.org/2012/03/lack-of-cost-benefit-analysis-in-dodd-frank-rulemaking/.
[5] *See, e.g., Hearing I*, *supra* note 2 (statements of Dr. Henry Manne, Dean Emeritus, George Mason University School of Law, and J.W. Verrett, Assistant Professor, George Mason University School of Law).
[6] Memorandum from RSFI and OGC to Staff of the Rulewriting Divisions and Offices (Mar. 16, 2012), *available at* http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf.
[7] *Id.*

On April 17, 2012, SEC Chairman Mary Schapiro testified before the Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs.[8] In both her testimony and in a letter to the Committee, Chairman Schapiro expressed her unequivocal commitment to the policies and principles of the Current Guidance.[9] Chairman Schapiro explicitly stated that the Current Guidance is binding upon all SEC rulewriting staff, and embodies the best practices for agency rulemaking.[10]

While the Committee is hopeful that the implementation of the policies and principles of the Current Guidance will improve the economic analysis underlying Commission rules, a major outstanding concern is the role of economic analysis in rulemakings by self-regulatory organizations (SROs). At another Subcommittee hearing on June 28, 2012, Chairman Schapiro directly addressed the applicability of the Current Guidance to SRO rulemaking.[11] While contending that the majority of SRO rules are "routine and operational" in nature, Chairman Schapiro nonetheless recognized that "major" rules should contain the rigorous economic analysis prescribed by the Current Guidance. Chairman Schapiro acknowledged deficiencies in current SRO rulemaking procedure, stating that there are some categories of SRO rules "where more analysis ought to be done." [12] She added that ". . . on [SRO] rules that have a more major, profound impact, we should be seeking more economic analysis."[13]

Chairman Schapiro's endorsement of the application of rigorous economic analysis to major SRO rulemaking accords with the President's conception of regulatory best practices. Executive Order 13563, signed by President Obama on January 18, 2011, makes clear that "[o]ur regulatory system . . . must identify and use the best, most innovative and least burdensome tools for achieving regulatory ends. It must take into account benefits and costs, both quantitative and qualitative."[14] The Municipal Securities Rulemaking Board (MSRB), as a statutorily-recognized self-regulatory agency, is an integral and influential part of our national regulatory system. Accordingly, it should comply with these constructive regulatory standards.

Notwithstanding the unanimous agreement of the President of the United States, the Chairman of Securities and Exchange Commission, this Committee, and the U.S. Court of Appeals for the D.C. Circuit as to the desirability of rigorous cost-benefit analysis, it appears some rulemaking has relied on substandard economic analysis. On May 4, 2012, the Commission considered a proposed rule change by MSRB concerning the application of MSRB Rule G-17 to underwriters of municipal securities. In a reasoned and persuasive dissent, SEC Commissioners Gallagher and Paredes observed:

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[8] *Hearing I, supra* note 2 (statement of Mary Schapiro, Chairman, U.S. Securities and Exchange Commission).
[9] *Id.*; Letter from Mary Schapiro, Chairman, U.S. Securities and Exchange Commission, to Darrell Issa, Chairman, H. Comm. on Oversight and Gov't Reform, June 11, 2012.
[10] *Id.*
[11] *The JOBS Act in Action, Part II: Overseeing Effective Implementation of the JOBS Act at the SEC: Hearing Before the Subcomm. on TARP, Financial Services and Bailouts of Public and Private Programs of the H. Comm. on Oversight and Gov't Reform*, 112th Cong. (2012) (testimony of Mary Schapiro, Chairman, U.S. Securities and Exchange Commission in response to question from Chairman Patrick McHenry).
[12] *Id.*
[13] *Id.*
[14] Exec. Order No. 13,563, 76 Fed. Reg. 3,821 (Jan. 21, 2011).

> Any rulemaking — whether by a self-regulatory organization, such as the MSRB, or by the Commission itself — should be the product of a careful and balanced assessment of the potential consequences that could arise. Such an assessment should entail a thorough analysis of both the intended benefits and the possible costs of a proposed rulemaking in order to ensure that any regulatory decision to proceed with the initiative reflects a well-reasoned conclusion that the benefits will come at an acceptable cost. This requires identifying the scope and nature of the problem to be addressed, determining the likelihood that the proposed rulemaking will mitigate or remedy the problem, evaluating how the rule change could impact affected parties for better and for worse, and justifying the recommended course of action as compared to the primary alternatives.
>
> The decision-making process that led to the Commission's approval of the MSRB's proposed rule change falls far short of meeting this benchmark.[15]

While a majority of the Commission ultimately approved the interpretive notice concerning MSRB Rule G-17, there should be little disagreement with Commissioners Gallagher and Paredes' fundamental premise: any and every rulemaking body should methodically analyze a proposed policy so as to ensure that it is likely to promote the public interest. Compliance with the policies and principles of the Current Guidance is essential to this proposition.

Compliance with the policies and principals of the Current Guidance is rendered all the more necessary by virtue of MSRB's quasi-governmental status. While MSRB is a private, non-governmental entity, its rulemaking authority exists by operation of Section 15B of the Securities Exchange Act of 1934.[16] The exercise of this extraordinary grant of power makes it all the more critical that MSRB conform to a government-wide consensus as to best practices for regulatory analysis.

The Committee recognizes the valuable and important role SROs can play in the marketplace. Self-regulation can be an effective and efficient means of serving the public interest. However, to be effective, self-regulation must be informed by rigorous economic analysis. To enable the Committee to better understand MSRB's policy and practice with regard to economic analyses, we request that you provide responses to the following requests for information, producing documents as requested and as necessary to sufficiently support your answers. **Please answer each question individually, specifying the question number to which you are responding.**

1. Please provide all internal policies, procedures, or guidelines governing the use of economic analysis in MSRB rulemaking.

2. Do you believe the policies and principles of the Current Guidance can assist MSRB in meeting its rulewriting responsibilities?

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[15] Daniel M. Gallagher and Troy A. Paredes, Commissioners, U.S. Securities and Exchange Commission, Statement Regarding Commission Approval of MSRB Rule G-17 Interpretive Notice (May 14, 2012), *available at* http://www.sec.gov/news/speech/2012/spch051412dmgtap.htm.

[16] Securities Exchange Act of 1934 § 15B, 15 U.S.C. § 78*o*-4 (2012).

3. Do you agree that rigorous economic analysis is a necessary step in determining whether a given policy serves the public interest?

4. Do you agree that the economic analysis supporting MSRB's rulemaking should be subject to advance public comment?

5. Please provide all guidance MSRB has requested from the SEC on the applicability or implementation of the policies and principles of the Current Guidance to MSRB rulemaking.

6. Please provide all records of all internal discussions as to the applicability or implementation of the policies and principles of the Current Guidance.

7. Do you agree with Chairman Schapiro's testimony that for a certain category of SRO rules, "more analysis ought to be done?"[17]

8. Section 1 of Executive Order 13563, signed by President Obama on January 18, 2011, states: "Our regulatory system . . . must identify and use the best, most innovative and least burdensome tools for achieving regulatory ends. It must take into account benefits and costs, both quantitative and qualitative."[18] Do you agree that MSRB, as a statutorily-recognized SRO, is an integral and influential component of our national regulatory system?

9. Please provide records of any internal or external discussion of the applicability of Executive Order 13563 or 13579.

10. Please state whether MSRB registrants are involved in MSRB rulemaking.

    a. Please specifically identify the opportunity for, and degree of, registrant consultation in the rulemaking process.

    b. Please specifically identify the opportunity for, and degree of, registrant review of formulated rules.

11. MSRB is a non-governmental entity that nonetheless shares in the government's monopoly on legal compulsory power. Please state whether the statutory grant of rulemaking authority entails that MSRB follow clear, methodical, and explicitly enunciated procedures to ensure that each proposed rule serves the public interest.

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[17] *The JOBS Act in Action, Part II: Overseeing Effective Implementation of the JOBS Act at the SEC: Hearing Before the Subcomm. on TARP, Financial Services and Bailouts of Public and Private Programs of the H. Comm. on Oversight and Gov't Reform*, 112th Cong. (2012) (statement of Mary Schapiro, Chairman, U.S. Securities and Exchange Commission)

[18] Exec. Order No. 13,563, 76 Fed. Reg. 3,821 (Jan. 21, 2011).

The Committee on Oversight and Government Reform is the principal oversight committee of the House of Representatives and may at "any time" investigate "any matter" as set forth in House Rule X. An attachment to this letter provides additional information about responding to the Committee's request.

Please provide all such responses as soon as possible, but no later than 5:00 p.m. on Wednesday, August 8, 2012. When producing documents to the Committee, please deliver production sets to the Majority Staff in Room 2157 of the Rayburn House Office Building and the Minority Staff in Room 2471 of the Rayburn House Office Building. The Committee prefers to receive all documents **in electronic format**.

If you have any questions about this request, please contact Christopher Hixon or Brian Daner with the Committee Staff at 202-225-5074. Thank you for your attention to this matter.

Sincerely,

Darrell Issa
Chairman

Patrick McHenry
Chairman
Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs

Enclosure

cc: The Honorable Elijah E. Cummings, Ranking Minority Member

The Honorable Mike Quigley, Ranking Minority Member
Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs

The Honorable Mary L. Schapiro, Chairman
U.S. Securities and Exchange Commission

The Honorable Elisse B. Walter, Commissioner
U.S. Securities and Exchange Commission

The Honorable Luis A. Aguilar, Commissioner
U.S. Securities and Exchange Commission

The Honorable Troy A. Paredes, Commissioner
U.S. Securities and Exchange Commission

The Honorable Daniel M. Gallagher, Commissioner
U.S. Securities and Exchange Commission

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Responding to Committee Document Requests

1. In complying with this request, you are required to produce all responsive documents that are in your possession, custody, or control, whether held by you or your past or present agents, employees, and representatives acting on your behalf. You should also produce documents that you have a legal right to obtain, that you have a right to copy or to which you have access, as well as documents that you have placed in the temporary possession, custody, or control of any third party. Requested records, documents, data or information should not be destroyed, modified, removed, transferred or otherwise made inaccessible to the Committee.

2. In the event that any entity, organization or individual denoted in this request has been, or is also known by any other name than that herein denoted, the request shall be read also to include that alternative identification.

3. The Committee's preference is to receive documents in electronic form (i.e., CD, memory stick, or thumb drive) in lieu of paper productions.

4. Documents produced in electronic format should also be organized, identified, and indexed electronically.

5. Electronic document productions should be prepared according to the following standards:

   (a) The production should consist of single page Tagged Image File ("TIF"), files accompanied by a Concordance-format load file, an Opticon reference file, and a file defining the fields and character lengths of the load file.

   (b) Document numbers in the load file should match document Bates numbers and TIF file names.

   (c) If the production is completed through a series of multiple partial productions, field names and file order in all load files should match.

   (d) All electronic documents produced to the Committee should include the following fields of metadata specific to each document;

   BEGDOC, ENDDOC, TEXT, BEGATTACH, ENDATTACH, PAGECOUNT,CUSTODIAN, RECORDTYPE, DATE, TIME, SENTDATE, SENTTIME, BEGINDATE, BEGINTIME, ENDDATE, ENDTIME, AUTHOR, FROM,

CC, TO, BCC, SUBJECT, TITLE, FILENAME, FILEEXT, FILESIZE, DATECREATED, TIMECREATED, DATELASTMOD, TIMELASTMOD, INTMSGID, INTMSGHEADER, NATIVELINK, INTFILPATH, EXCEPTION, BEGATTACH.

6. Documents produced to the Committee should include an index describing the contents of the production. To the extent more than one CD, hard drive, memory stick, thumb drive, box or folder is produced, each CD, hard drive, memory stick, thumb drive, box or folder should contain an index describing its contents.

7. Documents produced in response to this request shall be produced together with copies of file labels, dividers or identifying markers with which they were associated when the request was served.

8. When you produce documents, you should identify the paragraph in the Committee's schedule to which the documents respond.

9. It shall not be a basis for refusal to produce documents that any other person or entity also possesses non-identical or identical copies of the same documents.

10. If any of the requested information is only reasonably available in machine-readable form (such as on a computer server, hard drive, or computer backup tape), you should consult with the Committee staff to determine the appropriate format in which to produce the information.

11. If compliance with the request cannot be made in full by the specified return date, compliance shall be made to the extent possible by that date. An explanation of why full compliance is not possible shall be provided along with any partial production.

12. In the event that a document is withheld on the basis of privilege, provide a privilege log containing the following information concerning any such document: (a) the privilege asserted; (b) the type of document; (c) the general subject matter; (d) the date, author and addressee; and (e) the relationship of the author and addressee to each other.

13. If any document responsive to this request was, but no longer is, in your possession, custody, or control, identify the document (stating its date, author, subject and recipients) and explain the circumstances under which the document ceased to be in your possession, custody, or control.

14. If a date or other descriptive detail set forth in this request referring to a document is inaccurate, but the actual date or other descriptive detail is known to you or is otherwise apparent from the context of the request, you are required to produce all documents which would be responsive as if the date or other descriptive detail were correct.

15. Unless otherwise specified, the time period covered by this request is from January 1, 2009 to the present.

16. This request is continuing in nature and applies to any newly-discovered information. Any record, document, compilation of data or information, not produced because it has not been

located or discovered by the return date, shall be produced immediately upon subsequent location or discovery.

17. All documents shall be Bates-stamped sequentially and produced sequentially.

18. Two sets of documents shall be delivered, one set to the Majority Staff and one set to the Minority Staff. When documents are produced to the Committee, production sets shall be delivered to the Majority Staff in Room 2157 of the Rayburn House Office Building and the Minority Staff in Room 2471 of the Rayburn House Office Building.

19. Upon completion of the document production, you should submit a written certification, signed by you or your counsel, stating that: (1) a diligent search has been completed of all documents in your possession, custody, or control which reasonably could contain responsive documents; and (2) all documents located during the search that are responsive have been produced to the Committee.

Schedule Definitions

1. The term "document" means any written, recorded, or graphic matter of any nature whatsoever, regardless of how recorded, and whether original or copy, including, but not limited to, the following: memoranda, reports, expense reports, books, manuals, instructions, financial reports, working papers, records, notes, letters, notices, confirmations, telegrams, receipts, appraisals, pamphlets, magazines, newspapers, prospectuses, inter-office and intra-office communications, electronic mail (e-mail), contracts, cables, notations of any type of conversation, telephone call, meeting or other communication, bulletins, printed matter, computer printouts, teletypes, invoices, transcripts, diaries, analyses, returns, summaries, minutes, bills, accounts, estimates, projections, comparisons, messages, correspondence, press releases, circulars, financial statements, reviews, opinions, offers, studies and investigations, questionnaires and surveys, and work sheets (and all drafts, preliminary versions, alterations, modifications, revisions, changes, and amendments of any of the foregoing, as well as any attachments or appendices thereto), and graphic or oral records or representations of any kind (including without limitation, photographs, charts, graphs, microfiche, microfilm, videotape, recordings and motion pictures), and electronic, mechanical, and electric records or representations of any kind (including, without limitation, tapes, cassettes, disks, and recordings) and other written, printed, typed, or other graphic or recorded matter of any kind or nature, however produced or reproduced, and whether preserved in writing, film, tape, disk, videotape or otherwise. A document bearing any notation not a part of the original text is to be considered a separate document. A draft or non-identical copy is a separate document within the meaning of this term.

2. The term "communication" means each manner or means of disclosure or exchange of information, regardless of means utilized, whether oral, electronic, by document or otherwise, and whether in a meeting, by telephone, facsimile, email (desktop or mobile device), text message, instant message, MMS or SMS message, regular mail, telexes, releases, or otherwise.

3. The terms "and" and "or" shall be construed broadly and either conjunctively or disjunctively to bring within the scope of this request any information which might otherwise be construed to be outside its scope. The singular includes plural number, and vice versa. The masculine includes the feminine and neuter genders.

4. The terms "person" or "persons" mean natural persons, firms, partnerships, associations, corporations, subsidiaries, divisions, departments, joint ventures, proprietorships, syndicates, or other legal, business or government entities, and all subsidiaries, affiliates, divisions, departments, branches, or other units thereof.

5. The term "identify," when used in a question about individuals, means to provide the following information: (a) the individual's complete name and title; and (b) the individual's business address and phone number.

6. The term "referring or relating," with respect to any given subject, means anything that constitutes, contains, embodies, reflects, identifies, states, refers to, deals with or is pertinent to that subject in any manner whatsoever.

7. The term "employee" means agent, borrowed employee, casual employee, consultant, contractor, de facto employee, independent contractor, joint adventurer, loaned employee, part-time employee, permanent employee, provisional employee, subcontractor, or any other type of service provider.