
Many Firms Unaware of Municipal Advisor Registration and Compliance Requirements: MSRB Advises Municipal Entities to Check the Registration Status of Their Advisors

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On July 5, 2011, the Municipal Securities Rulemaking Board ("MSRB") issued a press release highlighting its concern that many firms may be engaging in activities as "municipal advisors," as defined in the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), without having registered as such with both the MSRB and the Securities and Exchange Commission ("SEC"). Firms providing municipal advisory services may be in violation of federal securities laws and MSRB rules if they are not registered as municipal advisors with both self-regulatory organizations. In addition — and even if registration requirements have not been met — municipal advisors and their employees who engage in municipal advisory business owe a federal fiduciary duty to their municipal entity clients. In its press release, the MSRB encouraged municipal clients that retain municipal advisors to verify the advisor's registration status with the MSRB and the SEC.

Firms that provide services or market securities to public pension funds and other municipal entities should consider whether their activities require them to register as municipal advisors (even if they are already registered as broker-dealers).

Municipal Advisor Status. The Dodd-Frank Act amends the Securities Exchange Act of 1934 ("Exchange Act") to require "municipal advisors" who solicit or provide certain advice to municipal entities and certain other persons to register with the SEC.¹ "Municipal advisor" is defined generally as a person who (1) provides advice to a municipal entity² or obligated person³ regarding municipal financial products or the issuance of municipal securities, including advice regarding structure, timing, terms and similar matters; or (2) that undertakes a solicitation of a municipal entity.⁴ The definition is broad; it includes certain financial advisors (including broker-dealers), investment advisers (subject to an exclusion discussed below), and third-party marketers and solicitors.⁵ Among other things, "municipal financial product" is defined to include "investment strategies," which the SEC has interpreted to include plans for the investment of any funds held by a municipal entity. As a result, in many cases registration is required to provide advice on the investment of municipal funds. Certain placement agents also are included; for example, the SEC has noted that a placement agent who solicits a municipal entity to invest in a private equity fund generally would be required to register.⁶ Excluded from the definition, and therefore from the registration requirement, are (among others): broker-dealers acting as underwriters (but not when acting in other capacities), registered investment advisers providing investment advice within the meaning of the Investment Advisers Act of 1940, and attorneys offering legal advice to municipalities.⁷

The SEC has proposed rules defining certain of the statutory terms, and provided interpretive guidance on others.⁸ Further interpretive guidance can be expected when the proposed rules are finalized.

SEC Registration. At present, municipal advisor firms are required to be

registered with the SEC on Form MA-T, pursuant to the SEC's interim final temporary Rule 15Ba2-6T. Under the temporary rule, only municipal advisor firms and sole proprietors are required to register; employees of such firms who engage in municipal advisory activities are not, although they are subject to certain MSRB rules (discussed below), and Form MA-T solicits certain information regarding disciplinary history of "associated municipal advisor professionals."⁹

MSRB Registration. Municipal advisors also must register separately with the MSRB on Form G-40. Firms already registered with the MSRB as brokers or municipal securities dealers may register as municipal advisors by updating their existing MSRB account. Firms not previously registered with the MSRB may file a new Form G-40 following payment of a \$100 fee, pursuant to MSRB Rule A-12, and assignment of an MSRB registration number. Registration with the SEC as a municipal advisor must precede registration as such with the MSRB.

SEC Proposed Rules. Rule 15Ba2-6T is currently set to expire on December 31, 2011. The SEC has proposed permanent rules to govern municipal advisors, including a permanent registration form which is more detailed than the current temporary Form MA-T¹⁰; the rules generally would govern registration, withdrawal from registration, consent to service of process, and books and records requirements. In addition to Form MA for municipal advisor firms and sole proprietors, Form MA-I would be required for all municipal advisor individuals, including those employees of municipal advisor firms who engage in municipal advisory activities on behalf of their firms.

Fiduciary Duty. The Dodd-Frank Act amends Section 15B(c)(1) of the Exchange Act to provide that municipal advisors have a fiduciary duty to

their municipal clients.¹¹ Entities that fall within the definition of "municipal advisor" already are subject to this statutory fiduciary duty, whether or not they have registered with the SEC as municipal advisors; the SEC has not yet provided guidance on what fiduciary status will mean for municipal advisors, but the MSRB has requested comment on draft Rule G-36 concerning municipal advisors' fiduciary duty, and on a draft interpretive notice under Rule G-36. The draft Rule and proposed interpretive notice provide that the fiduciary duty shall include a duty of loyalty and a duty of care, and discuss the contours of these duties, including a requirement of disclosure and consent in the case of material conflicts of interest.¹²

Other MSRB Rules. The MSRB also has proposed a supervisory rule, a "pay-to-play" prohibition, a fair-dealing interpretation, and amendments to its gifts and gratuities rule, all of which would apply to municipal advisors.¹³ A number of MSRB rules already apply to municipal advisors¹⁴, including Rule G-17 regarding fair dealing.¹⁵

¹ Dodd-Frank Act Section 975(a)(1)(B); 15 U.S.C. 78o-4(a)(1)(B).

² Exchange Act Section 15B(e)(8) defines "municipal entity" as "any State, political subdivision of a State, or municipal corporate instrumentality of a State, including (A) any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (B) any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (C) any other issuer of municipal securities." In its release proposing a permanent registration rule, the SEC notes that the definition includes, but is not limited to, public pension funds, local government investment pools and other state and local governmental entities or funds, and participant-directed investment programs or plans such as 529, 403(b), and 457 plans; it would also include charter schools. *Registration of Municipal Advisors*, Exchange Act Release No. 34-63576, 22-23 (Dec. 20, 2010) ("Proposing Release").

³ Exchange Act Section 15B(e)(10) defines "obligated person" as "any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities." Obligated persons may include conduit borrowers such as private universities, non-profit hospitals, and private corporations. Proposing Release, n.86. The proposed rules would provide further interpretation of the term.

⁴ Dodd-Frank Act Section 975(e); 15 U.S.C. 78o-4(e)(4)(A).

⁵ Proposing Release at 20-21.

⁶ Proposing Release at 32.

⁷ Dodd-Frank Act Section 975(e); 15 U.S.C. 78o-4(e)(4)(C).

⁸ Proposing Release.

⁹ "Associated municipal advisor professional" is defined as any associated person of a municipal advisor who is: (A) primarily engaged in municipal advisory activities; (B) engaged in the solicitation of municipal entities or obligated persons; (C) a supervisor of any persons described in (A) or (B); (D) a supervisor of any person described in (C) up through and including the Chief Executive Officer or similarly situated official designated as responsible for the day-to-day conduct of the municipal advisor's municipal advisory activities; or (E) a member of the municipal advisor's executive or management committee, or a similarly situated official, if any. The definition excludes any associated person whose functions are solely clerical or ministerial, and is derived from the definition of "municipal finance professional" in MSRB Rule G-37.

¹⁰ Proposing Release (above at n.2).

¹¹ Dodd-Frank Act Section 975(c)(2).

¹² MSRB Notice 2011-14 (Feb. 14, 2011).

¹³ MSRB Notices 2011-28 (May 25, 2011), 2011-04 (Jan. 14, 2011), 2011-13 (Feb. 14, 2011), and 2011-16 (Feb. 22, 2011).

¹⁴ See www.msrb.org/MSRB-For/Municipal-Advisors/MSRB-Rules.aspx.

¹⁵ See also MSRB Notice 2011-13 (Feb. 14, 2011).

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