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FINRA Notice Highlights Confusion.

A Financial Industry Regulatory Authority notice has highlighted what some market participants say is confusion among broker-dealers on whether they would have to register as municipal advisors in some instances.

Late last week FINRA sent out a notice reminding its members to register as MAs if they engage in investment-related activities with their clients. FINRA regulates broker-dealer firms, and under the Securities and Exchange Commission's MA registration rule advice about investing the proceeds of municipal bonds is a muni advisory activity in most instances.

"Recent FINRA examinations have found that some member firms are engaged in investment-related activities with municipal clients, but have not registered as municipal advisors and do not have reasonably designed supervisory systems and controls to determine whether they are required to register as municipal advisors," FINRA said.

The Securities Industry and Financial Market Association said the FINRA notice highlighted the complexities of MA activity rules.

"We appreciate the FINRA reminder, and it highlights the complexities of compliance with this rule set," said Leslie Norwood, a managing director, associate general counsel and head of municipals at SIFMA.

However, the industry doesn't see it as a frequent issue.

An MA who did not want to be named said they hadn't seen a lot of registered broker-dealers participate in unregistered MA activities compared to the early days of Dodd-Frank.

The Dodd-Frank Act required those acting as MAs to register with the Securities and Exchange Commission and the Municipal Securities Rulemaking Board and was intended to mitigate problems involving financial intermediaries providing unregulated advice.

"The question that people ought to ask themselves is, is my firm registered for that type of activity, am I individually registered?" the MA said. They said if that is a no, then they need to find what exemption they are relying on.

Crossover could occur when broker-dealers go to market with a new transaction or the investment of municipal bond proceeds.

The Government Finance Officers Association has said that due to the SEC's MA rule, brokers may be considered MAs if they provide advice on investments or bonds proceeds to governments.

If the funds are identifiable as municipal bond proceeds, that broker-dealer would need to have a registered MA involved. The one exemption for that would be if an investment adviser was involved, they said.

Also, broker-dealers need to check to see when opening a new brokerage account whether funds in that account could be co-mingled between bond proceeds and non-bond proceeds. With bond proceeds, broker-dealers would have to comply with MA rules because they're providing advice on municipal products or investments, they said.

"The enforcement is good in giving people a reminder and helping to provide some further indication of the types of activities that people may cross into either knowingly or unknowingly and put themselves in peril around registration," they said.

Robert Zondag, CFO and managing partner at American Deposit Management Co., an independent MA firm, has not seen registered broker-dealers participating in unregistered MA activities, but said there is confusion around MA activities since it's still fairly new compared to other municipal roles.

Zondag said FINRA could have put out the notice to address members already registered in other roles such as broker dealers and investment advisors and not as MAs.

The National Association of Municipal Advisors said FINRA's notice was useful so professionals can understand MA activities in determining if they should register.

"NAMA has been increasingly concerned, in general, with professionals who provide MA services but who are not registered," said Susan Gaffney, NAMA executive director. "While we have seen evidence of this in the non-BD space, this release again highlights this important issue."

Rod Kanter, partner at law firm Bradley, said he hasn't seen many broker-dealers cross the line to unregistered MA activity. However, he said it wasn't unusual for FINRA to put out such notices.

"It's not uncommon for regulatory and similar bodies to alert the market when they spot behavior that they disagree with before taking more aggressive action," Kanter said.

The notice happened shortly before MSRB Rule G-40, on advertising by MAs, went into effect Friday. Rule G-40 is a milestone because it will formally regulate MA advertising for the first time, requiring among other things that advertisements not be misleading and prohibiting MAs from using client testimonials in an advertisement.

"Social media is new for everyone and so it's a matter of understanding the different types of social media your firm might use and what the new requirements are," Zondag said. "It's going to be a new landscape for all firms trying to understand how to best use the new technologies and make sure they comply with the rules."

By Sarah Wynn

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