

Regulation of Financial Advisors - Implementation of Dodd-Frank Act

The basic premise is that financial advisors in the municipal bond market are unregistered and an unregulated, untaxed area offends some. This is not to say that there are not problems, although the biggest scandals have all involved regulated persons acting as advisors (often a banker acting with an underwriting or counterparty role in the same transaction).

Some aspects about regulation that are certain:

1. The Municipal Securities Rulemaking Board (MSRB) is in charge, with oversight by the Securities and Exchange Commission.
2. All advisory firms must register.
3. Fees are assessed annually to support regulation. Currently very low.
4. The rules are to apply to all advisory personnel and any persons associated with the firms.
5. Rule G-17 applies to all underwriters and financial advisors. It will likely be the basis for many disciplinary procedures.

“In the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.”

The MSRB comments note that Rule G-17 applies even in the absence of fraud. In particular, failure to disclose material information is highlighted. In light of various court and regulatory actions about lack of disclosure on pensions and other post employment benefits obligations (OPEB), it can be expected that advisors just like bankers will get more detailed in discussing disclosure with clients (due diligence).

Ancillary to these rules is the increase in recordkeeping. In an era where “paperless is better” is the watchword, Speer Financial is now having to make a record of all client contacts and keep files of all work product. Financial advisors are to be audited, and need to have ready records. As someone who never paid attention to the amount of time spent answering questions or helping a client, this is a new world. It seems necessary to justify to an outsider that our clients are correct in believing that we provided services and that those services were beneficial.

Other aspects of regulations that are proposed include the following:

1. Transaction fees. The MSRB has proposed that a fee be paid by the advisor to the MSRB on every transaction. Ultimately this is an additional cost of issuance to the governmental issuer. Such charges are already paid by underwriters, who build this regulatory cost into their fees.
2. Pay to play rules. Such a rule (Rule G-37) already applies to some extent to bankers and underwriters. Campaign contributions to persons running for office are limited to persons for which the banker can vote and this amount is capped. The same rule essentially is to apply to advisors and is enlarged to apply to referenda campaigns. This is a new area and one which will surprise many municipal officials in the next election cycle. Apparently only attorneys, especially bond counsel, and engineers will be able to contribute.