



MUNICIPAL SECURITIES REGULATION AND ENFORCEMENT

2024 MID-YEAR REVIEW

In the first half of 2024, the Financial Industry Regulatory Authority (FINRA) issued several fines and suspensions against participants in the municipal market, including for violations of its registration, reporting, disclosure, and testing requirements. The Securities and Exchange Commission (SEC) moved forward with litigation against municipal advisors for breaching their fiduciary duties and other federal securities law violations, including failure to register with the SEC and Municipal Securities Rulemaking Board (MSRB).

For its part, the MSRB continued to aim for more consistency in dealer regulations, amending MSRB Rule G-27 to harmonize certain supervision requirements with FINRA rules. The MSRB also amended Rule G-12 to facilitate the move for municipal securities transactions to a one-day settlement cycle, commonly referred to as “T+1,” and proposed shortening the reporting time for dealer transactions to the MSRB from 15 minutes to one minute.

At the end of June, the U.S. Supreme Court issued two important opinions. One eliminated the deference given to the SEC’s interpretations of federal securities laws, including possibly the SEC’s authority to adopt Rule 15c2-12. The second opinion requires the SEC to file its enforcement actions seeking civil penalties in federal court.

The individual was previously subject to a FINRA disciplinary action in 2016 for willfully failing to timely update his Uniform Application for Securities Industry Registration - Form U4, to disclose several tax liens, leading to the individual’s statutory disqualification from registration in 2017. In November 2018, his firm filed a Uniform Termination Notice for Securities Industry Registration - Form U5, terminating the individual’s registration, but later filed a Membership Continuance Application (MC-400) seeking to permit his re-association with the firm.

Despite the individual’s knowledge that he was not permitted to associate with the firm or transact in municipal securities while the MC-400 was pending, between May 2020 and May 2021, FINRA alleged that

FINRA ENFORCEMENT ACTIONS

Unregistered Dealer Fined

On January 4, 2024, the former president and chief compliance officer of a now-defunct Georgia-based investment firm agreed to settle charges with FINRA for a matter in which FINRA alleged that he acted as an unregistered dealer in violation of Article III, Section 3 of FINRA’s bylaws, FINRA Rules 1210 and 2010, and MSRB Rules G-2 and G-4.

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he used the login credentials and email addresses of other registered representatives at the firm to conduct municipal securities business, including discussing and recommending transactions to customers, communicating with firm vendors about trade corrections, and using the firm's systems to effect trades.

As part of the settlement, the individual agreed to accept a suspended fine of \$20,000 and an 18-month suspension from associating with any FINRA member firm. The fine only applies if the individual, who is now retired, attempts to re-join the industry.

A copy of the Letter of Acceptance, Waiver, and Consent can be found [here](#).

Firm Fined over NTBC Indicator

On January 5, 2024, a large full-service brokerage firm settled charges with FINRA alleging that it failed to include the Non-Transaction Based Compensation indicator (the NTBC Indicator) when reporting its municipal securities transactions to the MSRB's Real-Time Transaction Reporting System (RTRS), in violation of MSRB Rule G-14.

MSRB Rule G-14 requires broker-dealers to report information about purchases and sale transactions for municipal securities "promptly, accurately, and completely," requiring the inclusion of the NTBC Indicator for customer trades that do not include a mark-up, mark-down or commission. The requirement, which went into effect in 2016, was intended to improve price transparency by distinguishing between transaction prices that include some form of transaction-based dealer compensation and those that do not.

FINRA alleged that, from July 2016 to July 2021, the firm excluded the NTBC Indicator for all transactions in non-managed accounts (totaling 91,059 accounts) due to errors in the design of the firm's electronic transaction reporting system. FINRA also alleged that the firm violated MSRB Rule G-27 concerning supervisory procedures since, between July 2016 and December 2023, "the firm's supervisory system, including its written supervisory procedures, was not reasonably designed to ensure compliance with RTRS reporting requirements because the firm lacked any supervisory reviews or written procedures relating to the [NTBC Indicator]."

In December 2023, the firm took steps to enhance its systems and procedures by adopting and implementing a quarterly supervisory review for the accurate reporting of the NTBC Indicator.

As part of the settlement, the firm agreed to a censure and a \$100,000 fine. A copy of the Letter of Acceptance, Waiver, and Consent can be found [here](#). FINRA previously censured and fined the same firm \$350,000 in April 2022 for violations of FINRA Rules 6730(a), 3110(a), and 2010 relating to Trade Reporting and Compliance Engine (TRACE) reporting.

Firm Fined for Trade Confirmation Failures

On January 19, 2024, FINRA fined a New York-based broker dealer for its failure to disclose mark-up and mark-down information on retail customer confirmations, in violation of MSRB Rule G-15 and FINRA Rules 2232 and 2010, as well as for violations of MSRB Rule G-27 and FINRA Rules 3110 and 2010 concerning supervision.

Trade confirmations are designed to protect investors by alerting them to potential conflicts of interest with their broker-dealers and providing them the means to verify the terms of their transactions. MSRB Rule G-15 and FINRA Rule 2232 require each broker-dealer, at or before the completion of a transaction in municipal securities, to send the customer a written confirmation that includes the dealer's mark-up or mark-down for the transaction (expressed as both a total dollar amount and as a percentage of the prevailing market price). A violation of FINRA Rule 2232 is also a violation of FINRA Rule 2010.

FINRA alleged that, between June 2020 and August 2021, the firm provided retail customer confirmations that failed to include such information for 793 transactions in municipal securities as well as 344 transactions in corporate or agency debt securities. The firm failed to include any information related to mark-ups or mark-downs for most of the affected retail customer confirmations. In some instances, the firm included the dollar amount on the mark-up or mark-down but did not include other information such as a percentage of the prevailing market price. The disclosure failures allegedly arose from a coding issue related to orders that were placed over the phone with the firm's clearing company. Additionally, from at

least June 2020 to September 2021, FINRA alleged that the firm did not have any policies or procedures in place regarding the disclosures required on retail customer confirmations, and the firm did not conduct any review of retail customer confirmations to confirm they included the requisite disclosures.

The settlement resulted in a \$100,000 fine and a censure. A copy of the Letter of Acceptance, Waiver, and Consent can be found [here](#).

Firm Fined for Rule G-37 Violations

On January 29, 2024, FINRA fined and censured a New York-based, veteran-owned investment bank \$30,000 for failing to timely file Form G-37 reports disclosing the extent of its underwriting base, as well as for violations of MSRB Rule G-27 concerning supervision.

The purpose and intent of MSRB Rule G-37 is to ensure that the high standards and integrity of the municipal securities markets are maintained; to prevent misconduct; and to protect investors, municipal entities, and the public interest. MSRB Rule G-37 requires broker-dealers in municipal securities to send to the MSRB, by the last day of the month following the end of each calendar quarter, a Form G-37 that discloses contributions made to issuer officials and/or bond ballot campaigns, payments made to political parties, and a list of issuers with which the broker-dealer has engaged in the municipal securities business during the prior calendar quarter.

FINRA alleged that the firm filed 14 Form G-37 reports between one and 645 days late and filed eight Form G-37 reports that omitted 60 municipal underwritings for which the firm acted in a managerial capacity. Additionally, the firm allegedly failed to maintain procedures regarding the process for identifying and compiling information required to be reported on the Form G-37, such as assigning someone the responsibility to maintain a record of reportable information, identifying the sources from which reportable information should be collected, and providing for a review of the Form G-37 reports to ensure the accuracy of their content before filing. Instead, FINRA alleged that the firm's compliance department relied on a spreadsheet of municipal underwritings prepared by the

firm's municipal underwriting department, which at times omitted certain underwritings required to be reported.

FINRA's findings with respect to Rule G-37 related solely to the timing of the filings and completeness of required information for issuers with which the firm had done business in the prior quarter. FINRA did not find that the firm failed to report any political contributions that required disclosure. Similarly, FINRA's findings related to the firm's alleged violation of MSRB Rule G-27 on supervision did not identify deficiencies specific to the firm's process for monitoring and tracking political contributions, rather FINRA faulted the firm for failing to effectively supervise its municipal securities activities only with regard to disclosing the extent of its underwriting base.

A copy of the Letter of Acceptance, Waiver, and Consent can be found [here](#).

FINRA Fines Broker-Dealer for Processing and Settlement Violations

FINRA censured and fined a broker-dealer \$1.6 million in February 2024 for repeatedly failing to abide by MSRB Rule G-12 in connection with the processing and settling of municipal securities transactions and related supervisory failures under MSRB Rule G-27.

According to a February 15, 2024, FINRA [announcement](#), the broker-dealer allegedly failed to close out 239 inter-dealer municipal securities transactions from December 2016 through August 2021 and to promptly take physical possession or control of 247 municipal securities that were short more than 30 calendar days from January 2016 through August 2021. According to FINRA, MSRB Rule G-12(h) requires that failed inter-dealer municipal securities transactions be canceled or closed out no later than 20 calendar days after settlement date.

FINRA noted in its February 15, 2024, announcement that the disciplinary action was "the first disciplinary action in which FINRA has charged a firm with violating the close-out requirements of Municipal Securities Rulemaking Board (MSRB) Rule G-12(h) and related supervisory failures." The broker-dealer consented to FINRA's findings without admitting or denying the charges.

FINRA Fines and Suspends Broker Over Testing Violation

On March 28, 2024, FINRA fined and suspended a former municipal securities representative for allegedly accessing study materials while taking a MSRB qualification examination administered by FINRA, in violation of MSRB Rule G-3(f) and FINRA Rule 2010. The matter was referred to FINRA by the testing company that proctors MSRB and FINRA qualification exams.

MSRB Rule G-3(f) provides that associated persons may not engage in any activity inconsistent with a qualification exam's "purpose as a test of the qualification of persons taking such examination" nor "knowingly sign a false certification concerning any such qualification examination." FINRA Rule 2010 requires that associated persons, in the conduct of their business, "observe high standards of commercial honor and just and equitable principles of trade."

FINRA alleged that the individual possessed and had access to study materials located in the test center restroom during a lengthy unscheduled break. As part of the settlement, he agreed to a \$5,000 fine and 18-month suspension from the industry. The representative is no longer an employee of their firm.

A copy of the Letter of Acceptance, Waiver, and Consent can be found [here](#).

FINRA Fines Broker-Dealer for Failing to Ensure Fair Pricing in Corporate and Muni Bond Transactions

In March 2024, a broker-dealer agreed to pay a \$90,000 fine and \$44,927.83 plus interest in restitution after FINRA found the firm charged unfair prices across municipal and corporate bond trades and, in doing so, violated FINRA Rules 2121 and 2010 and MSRB Rules G-30 and G-17. According to the [Letter of Acceptance, Waiver, and Consent](#) (AWC), the broker-dealer allegedly charged customers unfair prices on 62 corporate bond transactions and six municipal bond transactions between June 2020 and March 2023. In addition, the AWC adds that the firm failed to maintain a supervisory system, including written supervisory procedures reasonably designed to achieve

compliance with its fair pricing obligations under FINRA Rules 3110 and 2010 and MSRB Rule G-27. The broker-dealer accepted and consented to the findings by FINRA in the AWC without admitting or denying them in addition to agreeing to pay the above sanctions.

DOJ ENFORCEMENT

Trader Found Guilty of Securities and Wire Fraud Relating to Treasury Securities

On February 7, 2024, a Chicago federal jury returned a guilty verdict against an individual at a broker-dealer firm on one count of securities fraud and three counts of wire fraud.

The U.S. Attorney's Office February 8, 2024, announcement notes that, according to evidence presented at trial, the defendant worked as the head of fixed income trading for a broker-dealer in Chicago and in 2019, the defendant engaged in unauthorized speculative trading in U.S. Treasury bonds using his employer's trading accounts, causing more than \$30 million in losses to the employer and its counterparties. The defendant allegedly attempted to disguise the trades and losses with fake off-setting trades through another clearing firm, which appeared profitable.

In addition to fraudulent trading, the defendant was convicted of embezzling thousands of dollars from his employer from 2017 to 2019 by falsifying books and records in order to create fake commissions. As a result of the fraud, the broker-dealer declared insolvency.

LITIGATION UPDATES

Final Judgment Entered Against Municipal Advisor

On January 30, 2024, a final consent judgment was entered against a municipal advisor and the municipal advisor's managing partner in an SEC action that had been ongoing for more than five years.

The SEC alleged that the municipal advisor and managing partner breached their fiduciary duties to the municipal issuer by not vetting the underwriter of its bonds or recommending an alternative underwriter, and also by not providing the requisite information and advice necessary for the municipal issuer to properly price the bonds. In its complaint, the SEC noted the municipal issuer “is a small, unsophisticated issuer which had never issued bonds.”

Without admitting or denying the SEC’s allegations, the municipal advisor and its managing partner consented to entry of a final judgment by which the municipal advisor was ordered to pay disgorgement in the amount of \$25,000 and the municipal advisor and managing partner to pay civil penalties in the amounts of \$30,000 and \$20,000, respectively. The SEC’s litigation release can be found [here](#).

Summary Judgement Granted in Favor of SEC in Action Against Charter School Municipal Advisors

On April 15, 2024, a court granted partial summary judgment in favor of the SEC on claims that municipal advisors to two charter schools violated their fiduciary duties, among other violations. The court noted “[a]s first-time issuers of municipal bonds, these schools sought Defendants’ help in structuring a deal with a bank underwriter to raise the funds at the lowest cost possible.”

The court found that the municipal advisors violated federal securities laws by engaging in a fee-splitting arrangement with an underwriter, being dually employed as a municipal advisor and underwriter, and failing to register as a municipal advisor. The court also found that the municipal advisors’ lack of disclosure to their charter school clients regarding the municipal advisors’ registration status and dual employment was a violation of the fiduciary duty standards set forth in Section 15B(c) (1) of the Exchange Act and MSRB Rule G-42. As there is limited case law regarding a municipal advisor’s fiduciary duties, the court looked to precedent regarding investment advisers’ fiduciary duties, which require “utmost good faith, and full and fair disclosure of all material facts, as well as an affirmative obligation to employ reasonable care to avoid misleading their clients.”

The court also found the municipal advisors violated their fair dealing obligations under MSRB Rule G-17, as well as Section 15B(c)(1) of the Exchange Act, which prohibits any acts in contravention of any MSRB Rule. The SEC’s litigation release can be found [here](#).

U.S. Supreme Court Issues Decision Affecting SEC Rulemaking and Enforcement

On June 28, 2024, the U.S. Supreme Court overruled *Chevron U. S. A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837, which required courts to defer to administrative agency interpretations of the statutes implemented by the agency. The result is that federal courts will not have to provide Chevron deference to the SEC’s interpretations of federal securities laws, including the SEC’s interpretation of its statutory authority to adopt Rule 15c2-12. Some municipal issuers and market professionals have criticized this Rule as an overstep of the SEC’s congressional mandate to prevent fraudulent, manipulative, and deceptive practices especially in light of the so-called “Tower Amendment.” The Supreme Court decision does not mean the SEC’s interpretations will not be considered, only that the courts will conduct an independent legal analysis. A copy of the opinion can be found [here](#).

The Supreme Court also ruled that the SEC will be required to bring fraud actions in federal court, which provides the defendant a right to a trial by jury, rather than using in-house proceedings. Ballard Spahr’s [Securities Enforcement and Corporate Governance Litigation](#) Group alert on this opinion can be found [here](#) and copy of the opinion can be found [here](#).

MSRB RULEMAKING

MSRB Proposes Rule G-14 and G-12 Amendments

On January 12, 2024, the MSRB filed its proposed Rule G-14 and Rule G-12 amendments to shorten the amount of time for dealer transaction reporting to the MSRB from fifteen minutes to one minute. The MSRB states that “[t]he proposed rule change is intended to bring about greater market transparency through more timely disclosure and dissemination of information to market participants and market-supporting vendors so that the information

better reflects current market conditions on a real-time basis, while carefully balancing the considerations raised by commenters throughout the rulemaking process.” reporting information by municipal issuers.

The SEC received 25 comments on the proposed rule changes, which can be found [here](#). Several of the commenters questioned the benefit of shortening reporting time versus the burden of compliance.

A copy of the MSRB’s SEC filing can be found [here](#).

MSRB Amends Rule G-12

On February 7, 2024, the Securities and Exchange Commission (the Commission) [approved](#) the MSRB’s proposed amendment to MSRB Rule G-12 (on uniform practice). The amendment is contained in a new section (k) of the rule (Rule G-12(k)) and had a compliance date of May 28, 2024. Rule G-12(k) will promote the completion of allocations, confirmations, and affirmations by the end of the trade date for municipal securities transactions between institutional customers. Rule G-12(k) is intended to facilitate the move for municipal securities transactions to a one-day settlement cycle (commonly referred to as T+1) and aligns with the same-day allocation, confirmation, and affirmation process for equities and corporate bonds required by Rule 15c6-2 under the Exchange Act.

Rule G-12(k)(ii) provides two options dealers may use to comply with the rule to meet the same-day allocation, confirmation, and affirmation standard for regular-way transactions in municipal securities. Under the first option, dealers may enter into a written agreement with the relevant parties to ensure completion of the allocation, confirmation, affirmation, or any combination thereof, for the transaction as soon as technologically practicable and no later than the end of the day on the trade date in such form as necessary to achieve settlement of the transaction. Under the second option, dealers are required to establish, maintain, and enforce written policies and procedures reasonably designed to ensure completion of the allocation, confirmation, and affirmation for the transaction as soon as technologically practicable and no later than the end of the day on the trade date. Specific requirements for each option are further described under Rule G-12(k).

MSRB Amends Rule G-27 Consistent with FINRA Rules

In May 2024, the MSRB amended Rule G-27 to permit FINRA-member dealers to designate an associated person’s private residence where supervisory activities take place as a residential supervisory location (RSL) if certain conditions are met, similar to amendments recently adopted by FINRA to Rule 3110. The MSRB also amended Rule G-27 to allow FINRA-member dealers to meet their internal inspection obligations remotely for a period of time in conformity with FINRA’s remote inspections pilot program. The purpose of the amendments is to modernize dealer regulations and promote consistent application of rules that apply to dealers who are subject to both MSRB and FINRA regulatory authority.

Under the G-27 RSL amendments, a dealer has the option to treat an associated person’s private residence where certain supervisory activities are conducted as a non-branch location. Rather than annual inspections, RSLs would be subject to inspections on a regular periodic schedule. Under the amendments, there are 10 conditions that must be met for designating an associated person’s private residence as an RSL that include requirements for recordkeeping and supervision as well as restrictions on the number of associated persons conducting business at the location, the availability of the location to the public, customer meetings, sales activities, and the handling of customer funds. Under the amendments, there are six conditions that make a location ineligible to designate as an RSL, including, for example, a person at the location being statutorily disqualified or subject to a regulatory investigation. Dealers were allowed to start using the RSL designation beginning on June 1, 2024. Dealers must provide a first list of designated RSLs to FINRA by October 15, 2024.

Regarding the G-27 remote inspections amendments, the MSRB’s amendments include the conditions and requirement to allow dealers to opt into FINRA’s remote inspections pilot program (Pilot Program). FINRA’s Pilot Program allows FINRA-member firms to meet their inspection obligation of qualified branches remotely. Under the amendments, dealers must develop a reasonable risk-based approach for utilizing remote inspections and are also required to conduct a risk assessment for each office or location.

The factors in the risk assessment must be documented and include the dealer's size, organizational structure, scope of business activities, number and location of the dealer's offices, the nature and complexity of the products and services offered by the dealer, the volume of business done, the number of associated persons assigned to a location, the disciplinary history of municipal securities representatives or associated persons, and any indicators of irregularities or misconduct. Among other requirements, dealers choosing to participate in FINRA's Pilot Program must have in place written supervisory procedures for remote inspections that are "reasonably designed to detect and prevent violations of, and achieve compliance with, applicable securities laws and regulations, including applicable MSRB rules."

The MSRB's Rule G-27 amendments do not apply to dealers who are non-FINRA members, including bank dealers. A link to the MSRB notices can be found [here](#) and [here](#).

CONCLUSION

While the MSRB continues to modernize its rules, FINRA has looked to enforce rules protecting the retail customer. We expect the enforcement actions related to municipal advisor rules and registration to continue. The consequences to municipal bond market enforcement actions resulting from the Supreme Court's decisions to limit the SEC's ability to bring enforcement actions in-house and strike down Chevron deference remain to be seen, but it is likely defendants will test the SEC's authority more frequently in federal court.

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