

Engineers and the Municipal Advisor Registration Requirement

Engineering firms have recently found themselves in the difficult position of assessing whether new Securities and Exchange Commission (SEC) rules apply to their activities and therefore necessitate registration as “municipal advisors” with the SEC and the Municipal Securities Rulemaking Board (MSRB).

Background of Municipal Advisor Registration Requirement

Amid concerns about the largely unregulated and unsupervised municipal securities market, municipal security losses during the 2008 financial crisis and allegations of unsavory business activities on behalf of some municipal market participants, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) required “a range of municipal financial advisors to register with the SEC and comply with regulations issued by the MSRB.” Under new rules adopted by the SEC, it is unlawful for any company or individual to provide certain financial advice to, or on behalf of, or to solicit municipal entities or certain other persons without first becoming a municipal advisor registered with the SEC.

The municipal advisor definition is broad and includes activities that ensnare many entities that have not historically considered themselves municipal advisors, such as engineering firms. A municipal advisor is defined as:

A person (who is not a municipal entity or an employee of a municipal entity) that provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues; or undertakes a solicitation of a municipal entity. (15 U.S.C. 78o-4(e)(4))

The definition expressly excludes, among other things, “engineers providing engineering advice.”

Although municipal advisors were required to register with the SEC and MSRB by Oct. 1, 2010, the SEC did not adopt final rules interpreting the statutory language and implementing a permanent registration regime until September 2013. In the SEC’s

final rules, the commission nominally clarified the exception for engineers and stated that an engineer is excepted from the definition of municipal advisor “to the extent that the engineer is providing engineering advice.” More important, it provided several pages of interpretative guidance regarding what the SEC deems permissible/impermissible activities for engineers. Subsequent to the final rules, the SEC also published additional guidance regarding the municipal advisor rules in the form of frequently asked questions. The SEC has extended the effective date of the new rules to July 1, 2014; however, the temporary rules (as well as rules enacted by Dodd-Frank) already require registration if an entity is engaged in activities triggering municipal advisor registration status.

Engineering Firms and Advice

Engineering firms that are not registered as municipal advisors need to be vigilant not to provide “advice” regarding municipal securities or to limit activities that involve advice so that they fall within the exceptions. The SEC has indicated that “advice” includes “advice with respect to the structure, timing, terms, and other similar matters concerning [municipal] financial products or issues” as well as:

A recommendation that is particularized to the specific needs, objectives, or circumstances of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues, based on all the facts and circumstances. (Securities Exchange Act Release No. 70462 (Sept. 20, 2013), 78 FR 67468, 67479 (Nov. 12, 2013))

The SEC has excluded from “advice”:

The provision of general information that does not involve a recommendation regarding municipal financial products or the issuance of municipal securities, including with respect to the structure, timing, terms or other similar matters concerning such financial products or issues. (17 CFR § 240.15Ba1-1(d)(1)(ii))

Information and conversations about financing of projects can inadvertently, and easily, morph into “advice” about issuance of municipal securities, so firms should be very careful about the content of their oral and written statements. Likewise, firms must avoid providing advice when they are asked pointed questions by



a municipal entity, because even if a firm does not provide express advice, the SEC has warned that it will deem “implicit recommendations” to also constitute impermissible “advice.”

Independent Registered Municipal Advisors

Although persons are prohibited from providing certain “advice” to municipal entities without registering as a municipal advisor, engineers and others are exempt from registration if they provide advice to a municipal entity regarding municipal securities and the municipal entity has an “independent registered municipal advisor” (Independent Municipal Advisor Exception). An independent registered municipal advisor is a “municipal advisor registered pursuant to section 15B of the [Exchange] Act and the rules and regulations thereunder and that is not, and within at least the past two years was not, associated... with the person seeking to rely on [the exception].” In order to rely on this exception, the engineering firm must receive a written representation from the municipal entity that the municipal entity has an independent registered municipal advisor and that the entity will rely on the advice of such advisor, among other things. As long as the conditions of the Independent Municipal Advisor Exception are met, engineers can provide certain advice without triggering the municipal advisor registration requirement.

Requirements for Interactions with Municipal Entities

When engineering firms meet with municipal entities regarding financing options, even generally, the engineering firms must make certain oral disclosures to the municipal entity regarding their role and what it may and may not provide to them. Like-

wise, when engineering firms provide any written materials to a municipal entity, the materials must include certain disclosures intended to clarify the roles of the parties.

Compliance with The Municipal Advisor Rules

Violation of municipal advisor rules is avoidable; however, many engineering firms may not think that the rules apply to them. Likewise, municipal entities may not be fully aware of the rules and may ask their engineering firms to engage in activities that would deem them municipal advisors under the new rules. Therefore, engineering firms should not rely on municipal entities to set the permissible boundaries.

Due to the broad exclusion when a municipal entity has an independent municipal advisor, it would not be surprising if some firms, as a matter of practice, require that a municipal entity have an independent municipal advisor prior to agreeing to a work on a project to avoid accidentally running afoul of the municipal advisor registration requirements.

This area is still evolving, and we expect that questions will continue to arise both before and after the final rules become effective. The Commission has been receptive to concerns raised by the industry, and it is possible that additional interpretative guidance will be issued as new concerns are raised.

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