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Stakeholders

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July 1, 2024

Category

Fair Practice

Affected Rules

[Rule G-27](#)

MSRB Amends Rule G-27 to Allow Dealers to Conduct Remote Inspections, Consistent with Recent FINRA Amendments

Overview

On May 30, 2024, the Municipal Securities Rulemaking Board (“MSRB”) filed with the U.S. Securities and Exchange Commission (“Commission”)¹ a proposed rule change to amend MSRB Rule G-27, on supervision, to permit certain brokers, dealers, and municipal securities dealers (“dealers”) that are members of the Financial Industry Regulatory Authority (“FINRA”) to fulfill their internal inspection obligations under Rule G-27(d) remotely for a specified period. The amendment is designed to conform the MSRB’s supervision rule to FINRA’s recently approved supervisory requirements under FINRA Rule 3110 Supplementary Material .18 creating a remote inspections pilot program (the “FINRA Pilot Program”).²

The MSRB’s proposed rule change was filed for immediate effectiveness with an operative date of July 1, 2024, to coincide with the operative date of the FINRA Pilot Program.

Summary of Amendment

The amendment to Rule G-27 allows certain dealers the option to participate in the FINRA Pilot Program to help ensure a coordinated regulatory approach to dealer supervision and enable FINRA to more efficiently inspect those dealers that are subject to both self-regulatory

¹ [File No. SR-MSRB-2024-05.](#)

² See Exchange Act Release No. 98982 (November 17, 2023), 88 FR 82464 (November 24, 2023).



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organizations' rules. Dealers that are FINRA members will have the option to fulfill their office inspection obligation under Rule G-27 remotely for a pilot period, if certain conditions are met. The amendment would not apply to dealers that are not members of FINRA, including bank dealers.³

The FINRA Pilot Program establishes a voluntary, three-year remote inspections pilot program to allow eligible FINRA-member firms the option to fulfill their inspection obligation of qualified branch offices, including offices of supervisory jurisdiction and non-branch locations remotely, without an on-site visit to such offices or locations, subject to specified terms. Proposed Supplementary Material .05 of MSRB Rule G-27 would provide eligible dealers with the flexibility to opt into the FINRA Pilot Program to fulfill their office inspection obligations under MSRB Rule G-27(d) by conducting inspections of eligible offices of municipal supervisory jurisdiction ("OMSJ"), branch offices, and non-branch locations remotely without an on-site visit to such locations, subject to certain conditions and criteria.

The amendments to Rule G-27 containing the conditions and requirements for dealers wishing to opt into the FINRA Pilot Program are summarized below:

Rule G-27 Supplementary Material .05(a) details the scope of the amendment and mirrors the scope of the FINRA Pilot Program under FINRA Rule 3110.18(a). Rule G-27 Supplementary Material .05(a) permits dealers the option to avail themselves of the FINRA Pilot Program for the required inspections of OMSJs, branch offices, and non-branch locations, in accordance with Rule G-27(d). Rule G-27 Supplementary Material .05(a) lists the applicable dates of participation in a remote inspection pilot program as July 1, 2024, through June 30, 2027.

Rule G-27 Supplementary Material .05(b) outlines the requirement for dealers to undertake a risk assessment in order to participate in the FINRA Pilot Program.

Rule G-27 Supplementary Material .05(b)(1) provides that a dealer may elect to conduct an inspection remotely, without an on-site visit for an office or location, when the dealer reasonably determines that the purposes of Rule G-27 Supplementary Material.05 can be accomplished in a remote manner. Prior to electing a remote inspection, rather than an on-site inspection, the

³ A bank dealer is defined under MSRB Rule D-8 as a municipal securities dealer which is a bank or a separately identifiable department or division of a bank. The MSRB will consider at a later date whether or not to extend the ability to conduct remote office inspections to bank dealers after giving due consideration to how to operationalize such initiative.

dealer would be required to develop a reasonable risk-based approach to using remote inspections and conduct and document a risk assessment for an office or location. The risk assessment must document the factors considered, including, among other things, 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 (*i.e.*, "red flags"). The risk assessment also must take into account any higher-risk activities that take place at, or higher-risk associated persons that are assigned to, that office or location.

Rule G-27 Supplementary Material .05(b)(2) lists additional factors that a dealer must take into consideration when conducting a risk assessment for remotely inspecting an office or location, including:

- i. the volume and nature of customer complaints;
- ii. the volume and nature of outside business activities, particularly investment-related;
- iii. the volume and complexity of products offered;
- iv. the nature of the customer base, including vulnerable adult investors;
- v. whether associated persons are subject to heightened supervision;
- vi. failures by associated persons to comply with the dealer's written supervisory procedures; and
- vii. any recordkeeping violations.

Rule G-27 Supplementary Material .05(c) lists eligibility exclusions and conditions for dealers wishing to participate in the FINRA Pilot Program at the firm and location level.

Rule G-27 Supplementary Material .05(c)(1) lists the firm level requirements. A dealer is ineligible from participation in the FINRA Pilot Program if the dealer is not a FINRA member or becomes ineligible from conducting remote inspections under the prescribed firm-level ineligibility criteria under FINRA Rule 3110.18(f)(1). In addition, a dealer must satisfy appropriate recordkeeping and surveillance and technology standards.

The dealer's recordkeeping system must meet the following criteria:

- i. The dealer must have a recordkeeping system to make, maintain, and preserve such records required to be made, maintained and preserved under applicable securities laws and regulations, including

- applicable MSRB rules, and the dealer's written supervisory procedures under Rule G-27(c);
- ii. the records must not be physically or electronically maintained and preserved at the office or location subject to the remote inspection; and
- iii. the dealer must have prompt access to any records made by an office or location participating in the FINRA Pilot Program.

The dealer must determine that its surveillance and technology tools are appropriate to supervise the types of risks presented by each such remotely supervised office or location. The tools may include but are not limited to:

- i. firm-wide tools such as electronic recordkeeping systems, electronic surveillance of e-mail and correspondence, electronic trade blotters, regular activity-based sampling reviews and tools for visual inspections;
- ii. tools specifically applied to such office or location based on the activities of associated persons, products offered, restrictions on the activity of the office or location (including holding out to customers and handling of customer funds or securities); and
- iii. system security tools such as secure network connections and effective cybersecurity protocols.

G-27 Supplementary Material .05(c)(2) lists the location-level requirements that each office or location must satisfy in order to be eligible for a remote inspection under the FINRA Pilot Program. A dealer will not be eligible to conduct remote inspections of any office or location during the FINRA Pilot Program if such office or location becomes ineligible for remote inspection under FINRA's prescribed location-level eligibility criteria under FINRA Rule 3110.18(g)(1). In addition, the following conditions must be met:

- i. electronic communications (*e.g.*, e-mail) are made through the dealer's electronic system;
- ii. the associated person's correspondence and communications with the public are subject to the dealer's supervision in accordance with Rule G-27(e); and
- iii. no books or records of the dealer required to be made, maintained, and preserved under applicable securities laws and regulations, including applicable MSRB rules, and the dealer's own written supervisory procedures under Rule G-27(c) are physically or electronically maintained and preserved at such office or location.

Rule G-27 Supplementary Material .05(d) requires dealers electing to participate in the FINRA Pilot Program to establish, maintain, and enforce

written supervisory procedures regarding 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. At a minimum, these procedures must address:

- i. the methodology, including technology, that may be used to conduct remote inspections;
- ii. the factors considered in the risk assessment made for each applicable office or location pursuant to paragraph (b) of Rule G-27 Supplementary Material .05; and
- iii. the use of other risk-based systems employed generally by the dealer to identify and prioritize for review those areas that pose the greatest risk of potential violations of applicable securities laws and regulations, including applicable MSRB rules.

Rule G-27 Supplementary Material .05(e) requires dealers to maintain an ongoing review of the activities and functions occurring at all offices and locations, whether or not the dealer conducts inspections remotely. In addition, a dealer's use of remote inspections of an office or location will be subject to the same standards for review as for other offices or locations under Rule G-27, in addition to the standards set forth in Rule G-27 Supplementary Material .05, and when a dealer's remote inspection of an office or location identifies any red flags, the dealer may need to impose additional supervisory procedures for that office or location or may need to provide for more frequent monitoring of that office or location, including potentially a subsequent on-site visit on an announced or unannounced basis.

Rule G-27 Supplementary Material .05(f) requires dealers electing to conduct remote inspections under the FINRA Pilot Program to maintain and preserve centralized records for each year of participation. These records must separately identify:

- i. all offices or locations that were inspected remotely; and
- ii. any offices or locations for which the dealer determined to impose additional supervisory procedures or more frequent monitoring, as provided in paragraph (e) of Rule G-27 Supplementary Material.05. A dealer's documentation of the results of a remote inspection for an office or location must identify any additional supervisory procedures or more frequent monitoring for that office or location that were imposed as a result of the remote inspection, including whether an on-site inspection was conducted at such office or location.

Rule G-27 Supplementary Material .05(g) requires dealers participating in the FINRA Pilot Program to comply with FINRA requirements with respect to the collection and submission of specified data and information, and in the manner and format determined by FINRA. Dealers shall also establish, maintain and enforce written policies and procedures that are reasonably designed to comply with any specified data and information collection and transmission requirements prescribed by FINRA. These requirements with respect to data and information collection and submission, as well as with respect to the related written policies and procedures, are set forth in FINRA Rule 3110.18(h).

Rule G-27 Supplementary Material .05(h) states that dealers who are eligible and wish to participate in the FINRA Pilot Program must make their election to participate in the FINRA Pilot Program in the manner and format as prescribed in FINRA Rule 3110.18(i).

Rule G-27 Supplementary Material .05(i) states that any dealer that fails to satisfy the conditions of Rule G-27 Supplementary Material .05 and requirements set forth by FINRA related to the timely collection and submission of data and information, shall no longer be eligible to conduct inspections remotely and must conduct on-site inspections of each office and location on the required cycle in accordance with Rule G-27(d).

Questions concerning this filing may be directed to Bri Joiner, Senior Director, Frank Mazzarelli, Director, or Justin Kramer, Assistant Director, Market Regulation, at (202) 838-1500.

May 31, 2024

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Text of Amendment*

Rule G-27: Supervision

(a) - (g) No Change.

Supplementary Material

.01 - .03 No Change.

* Underlining indicates new language; strikethrough denotes deletions.

.04 Reserved.

.05 Remote Inspections Pilot Program

(a) Scope. This Supplementary Material establishes the standards by which a dealer may participate in the Remote Inspections Pilot Program of a registered securities association of which it is a member (“Pilot Program”) with respect to the required inspection of offices of municipal supervisory jurisdiction, municipal branch offices and non-branch locations by dealers pursuant to paragraphs (d)(i)(A), (B) and (C) of Rule G-27. This Supplementary Material shall cover the required inspections of such offices or locations for a period of three years starting on July 1, 2024 and expiring on June 30, 2027 (“Pilot Period”). If this Supplementary Material is not amended to allow dealers to continue to participate in the Pilot Program with respect to their municipal securities activities should a registered securities association extend the Pilot Period or make permanent the Pilot Program, this Supplementary Material will automatically sunset on June 30, 2027, after which dealers will not be able to participate in the Pilot Program with respect to their municipal securities activities.

(b) Risk Assessment

(1) Review Standards. Subject to the requirements of this Supplementary Material, each dealer obligated to conduct an inspection of an office or location during the Pilot Period pursuant to, as applicable, paragraphs (d)(i)(A), (B) or (C) of Rule G-27, may elect to conduct the applicable inspection remotely, without an on-site visit for an office or location, when a dealer reasonably determines that the purposes of this Supplementary Material can be accomplished by conducting such required inspection remotely. Prior to electing a remote inspection for an office or location, rather than an on-site inspection, a dealer must first develop a reasonable risk-based approach to using remote inspections, and conduct and document a risk assessment for that office or location. The assessment must document the factors considered, including, among other things, 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 (i.e., “red flags”), and must take into account any higher-risk activities that take place at, or higher-risk associated persons that are assigned to, that office or location. A dealer or its office or location that is ineligible for remote inspections, pursuant to paragraph (c) of this Supplementary Material, must conduct an on-site inspection of that office or location on the applicable schedule under section (d) of Rule G-27. Notwithstanding this Supplementary Material, a dealer shall remain subject to the other requirements of section (d) of Rule G-27.

(2) Other Risk Assessment Factors. In conducting the risk assessment of each office or location in accordance with paragraph (b)(1) of this Supplementary Material, a dealer shall consider, among other things, the following factors in making its risk assessment for remotely inspecting an office or location:

(A) the volume and nature of customer complaints;

(B) the volume and nature of outside business activities, particularly investment-related;

(C) the volume and complexity of products offered;

(D) the nature of the customer base, including vulnerable adult investors;

(E) whether associated persons are subject to heightened supervision;

(F) failures by associated persons to comply with the dealer's written supervisory procedures; and

(G) any recordkeeping violations.

In addition, dealers should conduct on-site inspections or make more frequent use of unannounced, on-site inspections for high-risk offices or locations, or where there are red flags, and supervisory systems must take into consideration any red flags when determining whether to conduct a remote inspection of an office or location.

(c) Eligibility Exclusions and Conditions

(1) Firm-Level Requirements

(A) With respect to firm-level requirements, a dealer shall not be eligible to conduct remote inspections of any of its offices or locations in accordance with this Supplementary Material if (i) the dealer is not a member of a registered securities association or (ii) at any time during the Pilot Period such dealer becomes ineligible to conduct remote inspections under the prescribed firm-level ineligibility criteria of such registered securities association.

(B) During the period that a dealer is participating in the Pilot Program, the dealer must satisfy the following conditions to be eligible to conduct remote inspections of any of its offices or locations in accordance with this Supplementary Material:

(i) Recordkeeping System.

(a) The dealer must have a recordkeeping system to make, maintain, and preserve such records required to be made, maintained and preserved under applicable securities laws and regulations, including applicable Board rules, and the dealer's written supervisory procedures under Rule G-27(c);

(b) The records must not be physically or electronically maintained and preserved at the office or location subject to the remote inspection; and

(c) The dealer must have prompt access to any records made by an office or location participating in the Pilot Program.

(ii) Surveillance and Technology Tools. The dealer must determine that its surveillance and technology tools are appropriate to supervise the types of risks presented by each such remotely supervised office or location. The tools may include but are not limited to:

(a) firm-wide tools such as electronic recordkeeping systems, electronic surveillance of e-mail and correspondence, electronic trade blotters, regular activity-based sampling reviews and tools for visual inspections;

(b) tools specifically applied to such office or location based on the activities of associated persons, products offered, restrictions on the activity of the office or location (including holding out to customers and handling of customer funds or securities); and

(c) system security tools such as secure network connections and effective cybersecurity protocols.

(2) Office or Location Requirements

(A) With respect to office or location requirements, a dealer shall not be eligible to conduct remote inspections of any office or location in accordance with this Supplementary Material if at any time during the Pilot Period such office or location becomes ineligible for remote inspection under the prescribed location-level eligibility criteria of a registered securities association of which it is a member.

(B) As part of the requirement to develop a reasonably designed risk-based approach to using remote inspections, and the requirement to conduct and document a risk assessment, during the period that a dealer is participating in the Pilot Program, a specific office or location of the dealer must satisfy the following conditions to be eligible for remote inspections in accordance with this Supplementary Material:

(i) electronic communications (e.g., e-mail) are made through the dealer's electronic system;

(ii) the associated person's correspondence and communications with the public are subject to the dealer's supervision in accordance with Rule G-27(e); and

(iii) no books or records of the dealer required to be made, maintained, and preserved under applicable securities laws and regulations, including applicable Board rules, and the dealer's own written supervisory procedures under Rule G-27(c) are physically or electronically maintained and preserved at such office or location.

(d) Written Supervisory Procedures for Remote Inspections. Consistent with a dealer's obligation under Rule G-27(c), a dealer that elects to participate in the Pilot Program must establish, maintain, and enforce written supervisory procedures regarding remote inspections that are reasonably designed to detect and prevent violations of, and achieve compliance with, applicable securities laws and regulations, including applicable Board rules. Reasonably designed procedures for conducting remote inspections of offices or locations must address, among other things:

(1) the methodology, including technology, that may be used to conduct remote inspections;

(2) the factors considered in the risk assessment made for each applicable office or location pursuant to paragraph (b) of this Supplementary Material; and

(3) the use of other risk-based systems employed generally by the dealer to identify and prioritize for review those areas that pose the greatest risk of potential violations of applicable securities laws and regulations, including applicable Board rules.

(e) Effective Supervisory System. The requirement to conduct inspections of offices and locations is one part of the dealer's overall obligation to have an effective supervisory system. Therefore, the dealer must maintain its ongoing review of the activities and functions occurring at all offices and locations, whether or not the dealer conducts inspections remotely. A dealer's use of remote inspection of an office or location will be subject to the same standards for review as for other offices or locations under Rule G-27 in addition to the standard set forth in this Supplementary Material. Where a dealer's remote inspection of an office or location identifies any red flags, the dealer may need to impose additional supervisory procedures for that office or location or may need to provide for more frequent monitoring of that office or location, including potentially a subsequent on-site visit on an announced or unannounced basis.

(f) Documentation Requirement. A dealer must maintain and preserve a centralized record for each period constituting a Pilot Year, within the meaning of the Pilot Program and as defined by a registered securities association. The record must separately identify:

(1) all offices or locations that were inspected remotely; and

(2) any offices or locations for which the dealer determined to impose additional supervisory procedures or more frequent monitoring, as provided in paragraph (e) of this Supplementary Material. A dealer's documentation of the results of a remote inspection for an office or location must identify any additional supervisory procedures or more frequent monitoring for that office or location that were imposed as a result of the remote inspection, including whether an on-site inspection was conducted at such office or location.

(g) Data and Information Collection Requirement. Dealers that elect to participate in the Pilot Program and are not excluded under any of the firm-level requirements under paragraph (c)(1) of this Supplementary Material must comply with the requirements of a registered securities association, of which they are a member, with respect to the collection and submission of specified data and information, and in the manner and format determined by the registered securities association.

Such dealers shall establish, maintain and enforce written policies and procedures that are reasonably designed to comply with any specified data and information collection, and transmission requirements prescribed by a registered securities association of which they are a member.

(h) Election to Participate in Remote Inspections Pilot Program. Dealers eligible for participation in the Pilot Program by not having been excluded under any of the firm-level requirements under paragraph (c)(1) of this Supplementary Material shall make their election, in the manner and format as prescribed by a registered securities association, of which they are a member, to participate in the Pilot Program in accordance with this Supplementary Material. Dealers that elect to withdraw from subsequent Pilot Years (i.e., Pilot Year 2, Pilot Year 3, and Pilot Year 4, if applicable) shall withdraw in the manner and format as prescribed by a registered securities association of which they are a member.

(i) Failure to Satisfy Conditions. A dealer that fails to satisfy the conditions of this Supplementary Material, including the requirements specified by a registered securities association of which it is a member, related to the timely collection and submission of data and information shall be ineligible to participate in the Pilot Program with respect to its municipal securities activities and must conduct on-site inspections of each office and location on the required cycle in accordance with Rule G-27(d).