Bond Case Briefs

Municipal Finance Law Since 1971

MSRB's Kelly Highlights Concerns For Retail Muni Investors.

WASHINGTON – The Municipal Securities Rulemaking Board is helping the Securities and Exchange Commission's Investor Advocate identify products and practices in the municipal market that could hurt retail investors.

In a recent letter responding to a request from SEC Investor Advocate Rick Fleming, MSRB executive director Lynnette Kelly said the timeliness of continuing disclosures, the lack of bank loan disclosures, and trades below the minimum denomination are three main areas of concern for the board. Kelly also sent the letter to Jessica Kane and Rebecca Olsen in the SEC's office of municipal securities and Stephen Luparello in the SEC's division of trading and markets.

Fleming's office is tasked with protecting investors and works with the SEC and relevant self-regulatory organizations like the MSRB to "encourage reforms designed to benefit investors in the municipal securities markets," according to its website.

Fleming said he requested information from the MSRB as part of his research for his December report to Congress that looks back at the fiscal year and evaluates the progress of his recommendations. The letter details the most problematic products and practices for investors, based on the office's communications with officials of organizations like the MSRB, SEC, and Financial Industry Regulatory Authority. Not everyone responds with a letter like Kelly did, he said.

Kelly said an MSRB report published last May on issuers' timing of annual financial disclosures shows that for the last five years investors and the general public have had to wait an average of 200 calendar days after the end of the relevant fiscal year to see the "valuable information" in issuers' audited financial statements, submitted on EMMA. Annual financial information submissions also lagged, coming in an average of 188 days after the end of the applicable fiscal year, according to the report.

The MSRB has promoted its tools and resources to help issuers understand their disclosure obligations and to make the disclosures timelier, Kelly said. Issuers now have access to a free, automated email reminder service that helps them file periodic financial disclosures on schedule. As of Oct. 30, about 7,500 municipal entities have taken advantage of the service, she told Fleming.

The use of bank loans in the muni market has also drawn market participants' attention. The Federal Deposit Insurance Corp., in its Oct. 21 "Call and Thrift Financial Report Data" found that the issuance of bank loans to state and local governments increased to $192.3 billion in the fourth quarter of 2014, from $96.7 billion in the fourth quarter of 2012 for FDIC-regulated banks.

"Bank loan executions have far exceeded bank loan disclosures," Kelly said in her letter.

Municipal entities with bank loans do not currently have to disclose them under Rule 15c2-12 of the Securities and Exchange Act of 1934, which outlines disclosure obligations for issuers that want firms to underwrite their bonds. However, the MSRB has encouraged the practice and on Aug. 18

made it easier for entities to disclose their loans through EMMA. The board also sent a letter to the SEC in January encouraging the commission to re-examine issuers' obligations under 15c2-12, particularly regarding bank loans. Market groups, like the National Federation of Municipal Analysts, have also published best practices papers encouraging bank loan disclosure.

If such disclosures aren't made voluntarily , potential investors may not know about an issuer's total outstanding debt until they see another public offering from the issuer or audited annual financial statements, Kelly said. The EMMA website shows that only 130 bank loan disclosure documents have been submitted to the EMMA system since 2012, according to the letter.

"Delayed or undisclosed debt-like obligations could result in an investor's inability to assess in a timely manner the loan's impact on an issuer's credit profile and could inadvertently distort valuation of an issuer's bonds in both the primary and secondary markets," Kelly said. "The MSRB believes that the timely disclosure by municipal bond issuers of additional debt and debt-like obligations is essential to foster market transparency and to ensure a fair and efficient municipal market."

The final concern is making sure parties to a transaction are complying with the minimum denomination for muni offerings, which is listed in official statements and designed to prevent retail investors from buying unsuitable bonds. The minimum denomination is generally set at $5,000 but can sometimes be $100,000 or more, which is generally out of range for a retail investor. MSRB Rule G-15 in part prohibits dealers from making customer transactions below the designated denomination.

Kelly also said the MSRB is monitoring trade disclosures to see whether dealers are providing all material information about a security at the time of trade. While it is unclear whether dealers are complying with the obligation, it would "pose a significant risk to the retail investor" if they were not, "resulting in the investor possibly acting on incomplete information and executing a transaction that is unsuitable," she said.

The MSRB is pursuing initiatives to promote price transparency in the market that will benefit retail investors, the letter said. The self-regulator most recently introduced a proposal that would require dealers acting as principals to disclose markups and markdowns on transactions with retail customers. Comments on the proposal are due to be submitted by Dec. 11.

THE BOND BUYER

BY JACK CASEY

NOV 25, 2015 9:30am ET

Copyright © 2026 Bond Case Briefs | bondcasebriefs.com