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FINRA to Start Examining New Muni Markup Rule Compliance.

WASHINGTON - The Financial Industry Regulatory Authority is going to immediately begin examinations of firms' compliance with markup disclosure rules, with early returns indicating minor speed bumps in the implementation of those landmark requirements, regulatory officials said Tuesday.

Cindy Friedlander, the senior director of fixed income regulation within FINRA's Regulatory Operations group, said during a panel at FINRA's annual conference that the regulator will not wait to begin examining firms' compliance with the markup disclosure requirements that took effect less than two weeks ago.

Amendments to Municipal Securities Rulemaking Board rules G-15 on confirmation and G-30 on prices and commissions require dealers as of May 14 to disclose their markups and markdowns on certain transactions in the confirmations they send to retail customers. Dealers had hoped for a compliance extension, but didn't get it.

Under the rules, dealers initially must look at their contemporaneous trades of the same muni with other dealers or customers to establish a presumption of prevailing market price. If that data is unavailable, they must make a series of other successive considerations.

They must look at contemporaneous trades of the muni in interdealer trades, then trades of the muni between other dealers and institutional investors, then trades on alternative trading systems or other electronic platforms. Further down the waterfall, dealers can look at contemporaneous trades of similar securities.

Markup disclosures must be given as a total dollar amount and a percentage of the prevailing market price.

"We will be examining firms immediately," Friedlander said. "We are going to be very careful to take into account firms' good faith efforts to comply with the rules."

Michael Post, MSRB general counsel, said the board has been discussing how compliance with the markup rule has gone over the first week or so.

"What we've heard is that things have gone relatively smoothly," Post said, acknowledging that there have been reports of some hiccups. "It's a relief that the issues that people are encountering are things that they think that they can address."

Post reserved some measure of caution about his remarks, realizing that a firm experiencing a significant compliance failure might be hesitant to admit that to the MSRB.

Peg Henry, a deputy general counsel at Stifel Financial (SF) in St. Louis, said she has spent a lot of time on the trading floor recently and has asked traders in the past couple of days how things are

going with markup disclosure.

“The responses I got ranged from ‘not bad’ to ‘so far so good’ to ‘it is what it is,’” she said.

Henry said her firm has experienced some issues, such as the fact that it works with several vendors in its day-to-day business that don’t standardize how they report information. She also added that the size of the markup that needs to be reported on a trade could seemingly be affected by a trade of the same security that occurs later in the day.

“There are situations that have arisen just in the first week that have created problems for us,” she said. “We’ve developed workarounds, but the workarounds are very labor intensive.”

Post said that firms can choose to calculate the prevailing market price of a security earlier in the day if it chooses, so it can disclose the markup before another transaction occurs that could muddy the waters.

Ivonia Slade, an assistant director in the Securities and Exchange Commission’s Public Finance Abuse Unit, said her group is going to remain focused on topics it has acted on over the past several years, such as offering fraud that occurs when issuers make misleading statements in their bond documents. She highlighted the SEC’s focus on enforcing the fiduciary duty requirements of municipal advisors.

“Our focus has been on making sure that they’re meeting those obligations,” she said.

The FINRA conference began May 21 and concludes May 23.

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