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SEC Chair Clayton Raises New Concern About Muni Disclosure.

Securities and Exchange Commission Chair Jay Clayton raised a new concern about the state of secondary market disclosure in the muni market, on the same day that the Municipal Securities Rulemaking Board announced a step aimed at addressing another of Clayton's worries.

Clayton raised the concern during his introductory remarks to kick off Monday's meeting of the SEC's Fixed Income Market Structure Advisory Committee. Clayton, who has previously said he is worried about muni investors relying on stale financial disclosures, said Monday that he has heard of a trend of issuers being advised that information they supply on EMMA is subject to more scrutiny under federal anti-fraud laws than information provided to the market in other ways.

"I have significant questions about this advice," said Clayton, expressing doubt that it was correct in terms of "either law or policy."

Clayton said he has asked the SEC's Office of Municipal Securities to create a legal bulletin on the topic, and said he believes that continuing disclosure in the muni market is an important focus.

"This is an important topic, particularly for our main street investors," Clayton said.

Clayton first raised the issue of stale financial reporting late last year, touching off debate over issuers' responsibilities. The Municipal Securities Rulemaking Board announced Monday that it has voted to file with the SEC a proposal to enhance EMMA with new features to emphasize the timing of issuers' annual financial disclosures.

The subject was also on tap for FIMSAC's discussion, where talk focused on disclosure practices and the experiences of investors in seeking the information they feel they need to make informed decisions about whether or not to buy particular bonds.

Kendel Taylor, director of finance for the city of Alexandria, Virginia, said it takes until August to get all of the financial data for Alexandria's fiscal year ending June 30. The city still posts it in November, which she said she considers a fairly quick turnaround.

Investor panelists said states and large cities tend to be the most sluggish disclosures, as well as very small issuers. Not-for-profit healthcare and some parts of the education sector disclose much more quickly, the investors said.

Tom McLoughlin, a managing director at UBS, said that market conditions right now are such that issuers don't see an impact on their cost of borrowing when they don't do a good job on disclosure.

"There's no penalty for not disclosing right now, because there's a complete imbalance between supply and demand," McLoughlin said.

FIMSAC also discussed a preliminary recommendation from FIMASAC's Municipal Securities

Transparency Subcommittee regarding certain principal transactions with advisory clients seeking to liquidate bond positions.

Section 206(3) of the Advisers Act makes it unlawful for any investment adviser acting as principal for his/her own account to sell any security to or purchase any security from a client without disclosing to the client in writing before the completion of the transaction the capacity in which the investment adviser is acting and obtaining the consent of the client. The disclosure and consent is required on a transaction-by-transaction basis.

The recommendation is aimed at improving market liquidity by allowing broker-dealers registered as investment advisers to act as a principal with regard to client positions so long as the dealer enters a “blind bid,” meaning that there is no “last look” at competing bids.

MSRB Chief Market Structure Officer John Bagley said that the subcommittee’s discussion of this recommendation became wrapped up in the consideration of the practice of “pennying,” about which the MSRB may produce rulemaking. Pennying occurs when a firm takes a “last look” and then marginally outbids its competitors to purchase a security for its own account. The practice is believed by some to hurt market liquidity.

Bagley said the decision was made to move forward with the recommendation because it would be subject to the SEC’s rulemaking process, which would provide an opportunity for fulsome comment.

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