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SEC Panel Focuses on Price Transparency for Retail Investors.

Securities and Exchange Commission commissioners and market participants at an SEC fixed-income roundtable Tuesday wrestled with how to improve the transparency of municipal bond trading and prices, particularly for retail investors.

Speaking on the first panel, which focused on the current structure of the municipal market, market participants said price transparency for retail trades remains a daunting challenge. Panelists included dealers, financial advisors, alternative-trading system executives and academics. Many noted that the relative lack of transparency makes dealing with smaller retail customers frustrating and more-costly.

Carnegie Mellon professor Burton Hollifield, who studies the muni market, said the market remains opaque but clear trends emerge when looking at retail vs. institutional trading. “There is much more price dispersion in retail-sized trades than in institutional-sized trades,” he told fellow panelists.

SEC Commissioner Elisse Walter stressed the SEC doesn’t want to impose an equity structure on the muni market, but rather wants to make it more efficient and fairer to retail investors. She said there is “somewhat of an evolution” with more investors not just buying and holding, but selling munis for various reasons.

“The more I look at it, the more concerns I have about fairness in this market,” Walter said. “Do we need to take another look at how valuation appears on a statement?”

Ric Edelman, chairman and chief executive officer at advisory firm, Edelman Financial Services, said retail investors are being lied to by brokers because they do not realize yields are negotiable and their monthly statements don’t accurately reflect the actual price of their munis. Often a statement will value a muni at a premium, but an investor will only be able to sell it at a discount.

“We have huge education and disclosure problems within the industry,” Edelman said, adding that typical retail investors like retirees are not familiar with the nuances of the market. “They have no idea what they’re doing and how the game works.”

But other panelists took umbrage with Edelman’s remarks, pointing to the huge challenge of pricing such a diverse market and arguing that brokers make their best efforts to supply accurate statements.

“It’s not totally accurate that that exists at every firm,” said Larry Bowden, executive vice president

and director of fixed income sales and trading at Stephens Inc. Bowden said brokers at his firm do a lot of research on pricing, especially when they get varying prices from pricing services. He said brokers at his firm "are in there fighting for their customers."

"We do go to a lot of effort to try and get the statements as accurate as we can," he added.

"It's not the bond's price that's the problem, it's the yield," said Robert Auwaerter, principal and head of the fixed income group at The Vanguard Group Inc. "Pricing bonds in the municipal market is definitely an art not a science," primarily because most muni bonds, unlike corporate bonds, have call features that allows issuers to call them before maturity.

Some panelists had suggestions for improving price transparency.

Joseph Hemphill 3d, chief executive officer at Regional Brokers Inc., said he sees about 27% of bid-wanteds — bids solicited for bonds when it is not clear what the bonds are worth — actually trading. That means more than 70% of bid information from those bonds winds up unavailable.

Tom Vales, chairman and CEO at TMC Bonds LLC, said his ATS sees about 3,000 bid-wanteds on a daily basis, only about 20% of which trade.

"What if we could aggregate?" Hemphill asked. For bid-wanted bonds, investors typically seek bids through their brokers who in turn seek bids through ATS' and broker's brokers.

Hemphill said ATS' and brokers' brokers have been talking about pulling the data on bid-wanteds together and making it available, both to the Municipal Securities Rulemaking Board and to trading desks. That could change the game and relieve some of the frustration around third-party evaluations of a security, he said.

A later panel addressing improvements to the market covered much of the same ground, but some participants worried that additional information would be useless to many retail investors.

"An individual investor without some guide along the way won't be able to process that," said Brad Winges, head of Piper Jaffray fixed income sales, trading and underwriting.

John Bonow, chief executive officer at The PFM Group suggested finding a way to tie CUSIP numbers to similar credits, since many small issuers come to market so rarely. He also said retail investors should have access, possibly through the MSRB's EMMA website, to a forward-looking calendar where they can see a particular bond issue coming to market and tell their brokers, "I want a piece of it."

SEC officials and the panelists agreed that EMMA system is a great resource, but said that a greater effort is needed to make retail investors, not just municipal market professionals, aware of it. Walter suggested "a public-private partnership" approach and asked, "How can we put the most effective educational campaign together?"

The MSRB has said it will focus on enhancing and promoting EMMA in the coming year.

On the second panel, MSRB executive director Lynnette Kelly added that the MSRB's work on a possible best execution rule is difficult because it poses conundrums such as how to mandate determine the best interdealer market for a given security.

"It's a multi-year process," she said.

Meanwhile, Gallagher and several other panelists worried that if interest rates begin to rise again, there will be “Armageddon” for investors who will see the value of the low-coupon bonds the hold drop. Gallagher said bondholders’ concerns may be compounded since they’ve learned they may not have priority rights in bankruptcy proceedings such as those in California.

Bowden said investors should be careful not to hold all 30-year bonds, and should ladder the maturities of their bonds so that as some are redeemed they can purchase bonds with higher interest rates.

Besides Walter, commissioners David Gallagher and Luis Aguilar also sat in for the SEC. New SEC chair Mary Jo White appeared at the beginning of the discussion, but departed after opening statements. Aguilar expressed disappointment in the composition of the two muni panels, noting that the participants contained few retail investors, only two women and nobody of color.

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