# Bond Case Briefs

*Municipal Finance Law Since 1971*

---

## Reuters: U.S. Municipal Bond Trade Markups Face New Regulatory Scrutiny.

(Reuters) – The compensation that dealers receive in U.S. municipal bond trades is once again in regulators' crosshairs, with a member of the Securities and Exchange Commission saying on Monday that he is investigating how to give investors more information about markups.

SEC Commissioner Michael Piwowar, a Republican sworn in last August, is calling for retail investors to have a better sense of dealer markups – or compensation – in "riskless principal transactions."

Most individual investors are in the dark about how much dealers add to prices in trades.

In its sweeping report on the $3.7 trillion municipal bond market released more than a year ago, the SEC recommended requiring dealers to disclose markups, saying the lack of information put individual investors at a disadvantage. Since then, the commission has fallen quiet on the issue.

Regulation is hazy on dealer compensation. Dealers must disclose their remuneration if they act as agents facilitating trades, but not if they act as principals in the trade. For most trades in the municipal bond market, dealers are "riskless principals" purchasing securities from their customers and immediately reselling them to other dealers.

Piwowar told a meeting of the U.S. Chamber of Commerce that he asked the commission's municipal securities office "to work with me to develop a few proposals to improve how the fixed-income markets operate," highlighting markups as an area of concern.

Piwowar took an in-depth look at dealer compensation when he worked at the SEC as an economist, and his academic research on markups was frequently cited in the commission's 2012 report.

"We engaged in a lot of conversations with the dealers and the dealers were saying things like 'we commit capital to this market,'" he told reporters after the meeting.

"But we started looking at the data and a lot of these transactions look like they might be riskless principal transactions where the dealers aren't actually committing any capital," he said. "If they simply mark it up from where they bought it at, they don't have to disclose what the markup is."

Recording the markup would "enable investors to have better information," he added.

Piwowar did not give details about the proposals, or when they might be released.

In recent years, federal regulators have expressed concerns that individual investors, the "mom and pop" buyers that support the municipal bond market, do not have adequate information about the debt they use for income. An investigation by the Government Accountability Office concluded that those investors often paid more for bonds than banks and other institutions because of this lack of information.

The SEC enforces the rules for the market written by the Municipal Securities Rulemaking Board, a self-regulatory organization made up of banks, issuers and advisers. But FINRA, or the Financial Industry Regulatory Authority, has traditionally overseen markups and fined banks for not dealing fairly with their customers when they have tacked on excessive amounts. In one case in 2011, FINRA fined a bank for markups as large as 8.49 percent. Typically, they are closer to 2 percent.

“When you think about the number of securities in the market, the number of participants, the number of issuers, the spreads in these markets – I really think we can get more bang for our buck in terms of our resources and helping retail investors understand these markets better,” Piwowar said.

He added that the coming flood of retiring baby boomers and current uneasiness about the direction of interest rates should inspire deeper consideration of pricing.

WASHINGTON Mon Jan 27, 2014 2:51pm EST