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[SEC's Gallagher Sounds Calls For Pension, OPEB 'Disclosure Baseline'](#)

WASHINGTON – Securities and Exchange Commission member Daniel Gallagher said Thursday that pension and other post-employment benefit liabilities need to be made more transparent for investors, and argued for a universal “disclosure baseline” that all cities should use.

Gallagher, who has been outspoken on his interest in the muni market and who told The Bond Buyer last year that he had taken a “blood oath” to keep the SEC’s attention on munis, made the remarks at the Municipal Securities Rulemaking Board’s 1st Annual Municipal Securities Regulator Summit here. The summit was a non-public event open to regulatory officials and staff from the SEC, MSRB, Financial Industry Regulatory Authority, and others, an MSRB spokeswoman said.

Recent accounting standard reforms undertaken by the Governmental Accounting Standards Board have improved transparency for investors in municipal securities, Gallagher said, but take a step back by doing away with the annual required contribution and a need for more OPEB transparency remains.

“The ARC was the amount plan sponsors had to pay to amortize unfunded liabilities over a maximum 30-year period,” Gallagher said. “Every plan was required to disclose the ARC, and so it was a well-defined, easy-to-use measuring stick to determine whether plan sponsors were meeting their funding obligations. While I understand the need to divorce the technical nature of accounting for pension promises from the political nature of funding those pension promises through the state budgetary process, removing the ARC will diminish transparency on this important issue.”

Gallagher said he hopes GASB will revisit its standards again in time, but added that supplemental disclosure could be a help for investors more immediately. Municipalities should value and disclose their total liabilities using a risk-free discount rate such as the treasury yield curve, Gallagher suggested. They should then calculate and disclose a baseline plan contribution equal to the amount actuarially necessary to fully fund the plan.

“Investors would then be able to readily compare financials calculated using GASB standards and disclosures about the current level of plan funding against this common baseline,” he said. “Entities would be free to explain to investors why the differences exist.”

Gallagher also spoke about three steps muni regulators can take in the near future to improve the secondary market — requiring disclosure of riskless principal markups, improving post-trade price transparency, and adopting a best execution rule.

Commissioner Michael Piwowar has also made public comments recently about plucking some of this “low hanging fruit” that would not require radical overhauling of the market or legislative action.

Riskless principal transactions occur when a dealer almost simultaneously buys and sells securities, thereby taking on little or no risk that the market will move against the firm during that short time.

The SEC's comprehensive 2012 report on the municipal market recommends the MSRB consider requiring dealers to disclose to customers any markups or markdowns on these transactions.

"Given that 'riskless principal' is basically just a fancy name for 'agency,' there is no real reason to perpetuate this dichotomy," Gallagher said. "Disclosure of the markup or markdown in riskless principal transactions would enable customers to assess the fairness of the execution prices."

The MSRB should consider amending its Rule G-15 on confirmation to require this disclosure, he said.

Gallagher said the fixed income markets are a mystery to most investors, and drew a Hollywood comparison to what the bond market looks like.

"Maybe a good approximation of today's debt markets are the scenes from the equity markets of 25 years ago as portrayed in 'The Wolf of Wall Street,' he said. "Although I do hope there is a lot less fraud, and at least a little less debauchery, than what was depicted in that film. It is still common for investors to place corporate and municipal bond trades by calling their broker for a quote, without much insight as to whether they are receiving best execution and a fair price."

The MSRB has already proposed a best execution rule that would require broker-dealers to use "reasonable diligence" to obtain the best price for a customer based on prevailing market conditions, and is also exploring options for improving both pre and post-trade transparency on its EMMA website.

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