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Pair of U.S. Senators Urges Disclosure on Bond Markups.

(Reuters) – Municipal and corporate bond dealers would have to tell investors how much they charge to cover their compensation under bipartisan legislation currently in the U.S. Senate to end secret price markups.

The proposal, quietly introduced earlier this year by Virginia Democratic Senator Mark Warner and Oklahoma Republican Senator Tom Coburn, comes as momentum is growing among U.S. securities regulators to bring more transparency to the combined $13 trillion-plus municipal and corporate bond markets.

This week, executives from Charles Schwab met with federal lawmakers, Securities and Exchange Commission officials and other regulators to advocate for requiring disclosure on municipal bond markups.

"It's very opaque and somewhat confusing to investors," said Peter Crawford, a senior vice president at Charles Schwab.

"One of the things we have found in this over-the-counter market is the degree of price difference from one dealer to the next can be significant."

Most individual investors, the $3.7 trillion municipal bond market's backbone, are in the dark about how much dealers add to prices in trades.

Complicating matters, regulation on compensation is hazy. Currently, dealers must disclose if they act as agents facilitating trades but not if they act as principals in the trades. For most trades in the municipal market, then, dealers are "riskless principals," purchasing securities from their customers and immediately reselling them to other dealers.

Crawford, whose firm levies a flat charge of $1 per bond transaction to customers, said Charles Schwab has studied the lack of disclosure for about seven years.

The brokerage analyzed a California general obligation bond with a 5.25 percent coupon bond offered by five different dealers on its trading platform. It found the prices ran from $120.938 to $124.10, which meant on a $10,000 trade there was a $316.40 difference in prices.

The current federal push on dealer compensation in the municipal market began two years ago, when a comprehensive SEC report found individual investors pay more for bonds than institutions because they lack information, specifically about markups and markdowns.

In recent months the call for change has grown louder, with SEC Republican Commissioner Michael Piwowar saying in January retail investors must be given a better sense of markups.

Last month, his fellow SEC Republican Commissioner Daniel Gallagher said "'riskless principal' is basically just a fancy name for 'agency,'" and disclosing markups and markdowns "would enable customers to assess the fairness of the execution prices."

Meanwhile, the two self-regulatory organizations helping the SEC oversee the bond markets are focusing on the issue.

The Municipal Securities Rulemaking Board is currently taking steps that may lead to new rules on riskless principal transactions. At the same time the Financial Industry Regulatory Authority is "reviewing" the issue for corporate bonds, Richard Ketchum, its head, told reporters last month.

Crawford said this was the firm's first visit to Washington policymakers about markups, which was inspired by Piwowar's comments.

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