WSJ: SEC Fines Brokerages Over Sale of Puerto Rico Bonds.

The Securities and Exchange Commission fined 13 brokerage firms for improperly selling junk-rated Puerto Rico bonds in increments below $100,000, the agency's first action under a rule designed to protect mom-and-pop municipal-bond investors from high-risk debt.

Firms including Riedl First Securities Co. of Kansas and TD Ameritrade were among those that agreed to settle SEC charges that they sold portions of the U.S. commonwealth's $3.5 billion March bond offering that were smaller than the $100,000 minimum, the agency said. The firms didn't admit or deny the SEC's findings and agreed to pay fines that range from $130,000 for Riedl to $54,000 for J.P. Morgan Securities, a unit of J.P. Morgan Chase & Co., and Lebenthal & Co.

Other firms fined by the SEC include Charles Schwab & Co. and UBS AG. Representatives for Riedl and J.P. Morgan declined to comment. A spokeswoman for Schwab said the firm canceled the trades when alerted and is reviewing its procedures. A representative of TD Ameritrade said the firm agreed to the settlement without admitting or denying the allegations. The other firms either declined to comment or didn't immediately respond to a call or email seeking comment.

"These firms violated a straightforward investor protection rule that prohibits the sale of muni bonds in increments below a specified minimum," said LeeAnn Gaunt, chief of the SEC's Municipal Securities and Public Pensions Unit. "We conduct frequent surveillance of trading in the municipal-bond market and will penalize abuses that threaten retail investors."

The SEC and other regulators have been moving to protect the small investors who make up the bulk of the $3.7 trillion municipal-bond market, which the SEC described in a 2012 report as "illiquid and opaque." That has included fining Kansas, New Jersey and Illinois for failing to note underfunded pension obligations in disclosures to bond investors.

The agency's move comes during a rally in the municipal bond market, which has posted its longest string of monthly positive returns in more than two decades, according to Barclays PLC data. Debt sold by U.S. cities and states returned 8.32% through the end of October, including price increases and interest payments, outpacing gains in blue-chip U.S. stocks, corporate debt and Treasurys.

Investors, led by retail investors purchasing the debt through mutual funds, have poured about $18.2 billion into municipal-bond funds this year, after withdrawing about $43.38 billion in the same period of 2013, according to Lipper.

Among the beneficiaries of the rally have been issuers of low-rated debt, including Puerto Rico, which in March sold $3.5 billion in junk-rated debt to investors including hedge funds with an 8% coupon. The $100,000 minimum was listed in the official statement and established to protect individual investors from the risks of noninvestment-grade debt, which includes default, not being able to sell the bonds quickly or interest-rate spikes that cause prices to decline, the SEC said. The bonds were rated double-B-plus at the time by Standard & Poor's Ratings Services.

The agency said enforcement officials observed some of the sales in their surveillance of the municipal-bond market and subsequently identified 66 transactions in which dealer firms sold the bonds in units smaller than $100,000, in violation of the rule. The SEC's order against Riedl, which received the largest fine, says its transactions fell below the minimum 28 times. J.P. Morgan and Lebenthal went below the minimum once each, according to the SEC.

"This signals yet a larger presence of the SEC in the day-to-day workings of the municipal-bond market," said Matt Fabian, managing director at research firm Municipal Market Advisors. "This was a very high-profile transaction, massive and widely covered in the media. And the problems…were widespread and widely discussed."

The following is a complete list of firms fined: Charles Schwab & Co., Hapoalim Securities USA, Interactive Brokers LLC, Investment Professionals Inc., J.P. Morgan Securities, Lebenthal & Co., National Securities Corporation, Oppenheimer & Co., Riedl First Securities Co. of Kansas, Stifel Nicolaus & Co., TD Ameritrade, UBS Financial Services, and Wedbush Securities.

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