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Gallagher: Mandate GASB Standards, Possibly By Linking to Tax-Exempts.

WASHINGTON - Securities and Exchange Commission member Daniel Gallagher is calling for Congress to mandate that municipal issuers use Governmental Accounting Standards Board standards, possibly as a condition for their bonds to be tax-exempt.

Gallagher issued the call at the Financial Industry Regulatory Authority's Fixed Income Conference in New York City on Tuesday, continuing to build on his track record as the SEC's most outspoken voice on munis.

He also said Congress could grant the SEC authority to recognize GASB standards, as it does for FASB benchmarks, as an alternative to requiring issuers use them as a condition of their bonds' tax-exempt status.

The Republican commissioner said that too many issuers are not adhering to GASB standards for accounting for pension liabilities, leading some to be able to "hide the yawning chasm in their balance sheets" created by overly ambitious projections of pension investment returns.

"According to the most recent information I could locate, just over two-thirds of the 30,000 or so largest state and local municipal issuers use GASB standards," Gallagher said. "Data were not available for the extent to which an additional 20,000 smaller municipal issuers use GASB standards, but I would hazard a guess that their rate of compliance with GASB is lower than the larger issuers."

Issuers are not currently required to adhere to GASB standards, but must do so in order to get a "clean audit" from their auditors. Also if they say they are using GASB standards, they must do so. "We need a legislative fix to mandate the use of GASB standards for municipal issuers — whether it is a grant of authority to the Commission to recognize GASB standards as they do the [Financial Accounting Standards Board's] or as a condition placed on the bonds' exempt status," Gallagher continued. "This should help drive better transparency for investors in the muni market."

Gallagher has said repeatedly that he is worried about bond exposure to muni pension and other post-employment benefit (OPEB) liabilities. The SEC's enforcement division has also taken action on this front. Most recently, the commission charged Kansas for understating bond exposure to its pension liabilities, the third state the commission has charged for pension reporting problems.

He also said he is pleased that a number of firms have been meeting with SEC to discuss ways to facilitate electronic trading, after he called on SEC last year to engage with market participants and other interested parties to "develop creative solutions to increase liquidity in the secondary fixed income markets."

Gallagher also touched on other issues in the muni market, repeating some of his past passionate calls for improved transparency for retail investors in the secondary market. Gallagher applauded FINRA and the Municipal Securities Rulemaking Board for their introduction late last year of joint proposals to require dealers acting in a principal capacity to disclose to investors a "reference price"

of the same security traded that same day. He said in a December interview that he would have liked the rule to be more similar to a true disclosure of the dealer's markup, but added on Tuesday that the proposals are a positive step.

He also praised the enforcement division's work in the muni space, pointing to the SEC's enforcement action in Harvey, Ill. and saying he supports SEC efforts to bar access to the market for muni officials or cities that don't follow the rules. Last summer, the SEC secured an emergency order to stop a bond offering by the city based on evidence that the proceeds were to be fraudulently diverted with some of those sums directed to pay the city's comptroller and muni adviser, Joseph Letke. In December, the city agreed to a settlement in which it agreed to stay out of the markets for as many as three years. The SEC also won a judgment against Letke, along with a bar against participating in future muni offerings.

"This case was an outstanding use of agency resources, and I fully support prohibiting municipalities that cannot or will not comply with the law from accessing the securities markets, as well as pursuing the culpable officials who perpetrate the fraud," Gallagher said.

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