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**CREDIT MARKETS**

# NASD Settles Overcharge Claims

## Merrill Lynch, UBS Are Among Firms To Pay Fines and Make Restitution

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The National Association of Securities Dealers settled cases with eight Wall Street firms over allegations the companies overcharged investors who bought and sold municipal bonds.

**Merrill Lynch & Co., Charles Schwab Corp.,** Edward Jones, **Morgan Stanley,** Prudential Equity Group, **UBS** AG's UBS Financial Services Inc. unit, **Wachovia Corp.**'s Wachovia Securities LLC unit and First Trust Portfolios LP, all agreed to pay fines and restitutions without admitting or denying allegations.

The total financial penalties added up to about \$610,000, with \$200,666 being paid by UBS, \$118,680 by First Trust Portfolios, \$109,527 by Merrill and \$60,869 by Schwab. Other firms paid smaller amounts.

While the penalties are small compared with other regulatory fines in recent years, the matter represents one of the largest cases to date that regulators have brought about pricing discrepancies in the \$23 trillion bond market. Bonds, unlike many stocks, are traded over the counter between dealer firms that take proprietary positions and make money by collecting a spread between their buying and selling prices instead of collecting a commission.

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[See real-time commentary](#)<sup>1</sup> covering releases, events, and flows affecting the Treasury market, from Briefing.com.

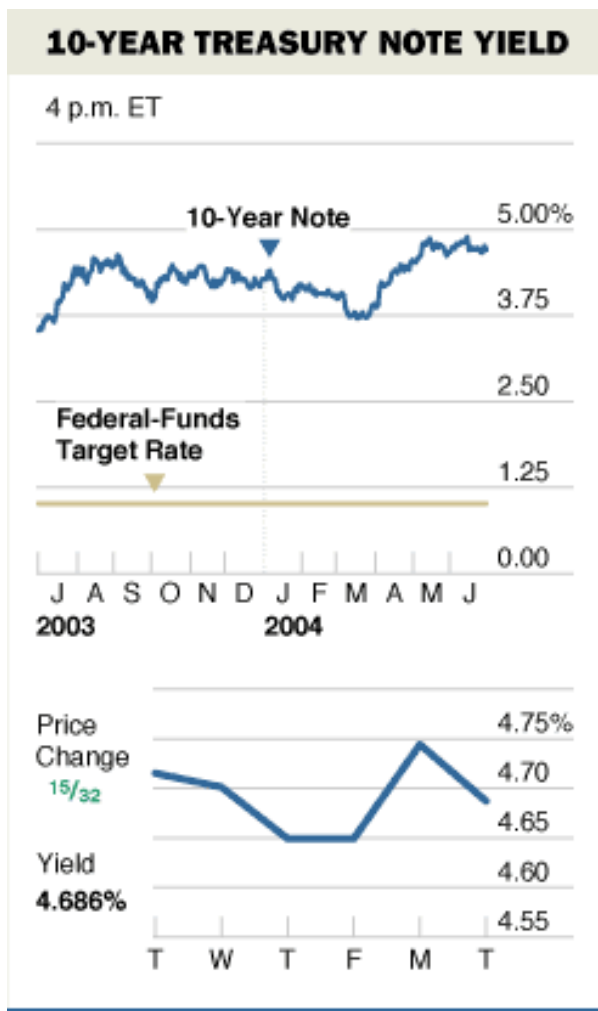
**AUCTION RESULTS**

Here are the results of the Treasury auction of four-week bills. All bids are awarded at a single price at the market-clearing yield. Rates are determined by the difference between that price and the face value.

Applications	\$24,122,113,000
Accepted bids	\$9,000,125,000
Accepted noncompetitively	\$40,634,000
Accepted frgn noncomp	\$0
Auction price (Rate)	99.910 (1.155%)
Coupon equivalent	1.174%
Bids at market-clearing yld accepted	89.56%
Cusip number	912795QV6

The bills are dated July 1 and mature July 29.

The cases also come several months before more up-to-the-minute pricing information is due to be made available to bond investors. The bond market has grown in recent years as nervous stock investors have shifted cash to bonds, just as Americans growing older allocated a larger portion of their investments to bonds.



The \$2 trillion municipal-bond market is a haven for individual investors, mostly because of the tax benefits they provide. But in recent years, the market has come under scrutiny from regulators who said it isn't transparent enough. These critics said prices investors paid when buying and selling bonds differed widely on the same day, even when there was no major news or market activity.

The NASD investigated bond-trading activity and found problems in the way municipal bonds were priced. The NASD didn't find that dealers took "unfair profits" in dealing with customers, but said firms also failed to take reasonable steps to get fair prices for customers.

The NASD identified about 60 trades in an arbitrarily selected period in 2002 and 2003 in which investors sold bonds at below market prices. The bonds were later resold by dealers hours or days later at prices from 6% to more than 100% greater than where investors had sold them.

In one trade at UBS, an investor received about \$81,250 for Beaver County, Pa., industrial-developments bonds with a par value of \$200,000. NASD alleged that other trades after the initial sell order established the true market value of the bonds at \$155,820, nearly \$75,000 more than the investor received

for them.

The investigation now turns to the interdealer brokers who participated in many of the trades. NASD officials declined to comment on this phase of the investigation, but said that they had other cases they were working on with interdealer brokers as well as brokerage firms that sold both municipal and corporate bonds.

"This is an area we're very much focused on," said Barry Goldsmith, head of enforcement at NASD, the main regulatory body for brokerage firms.

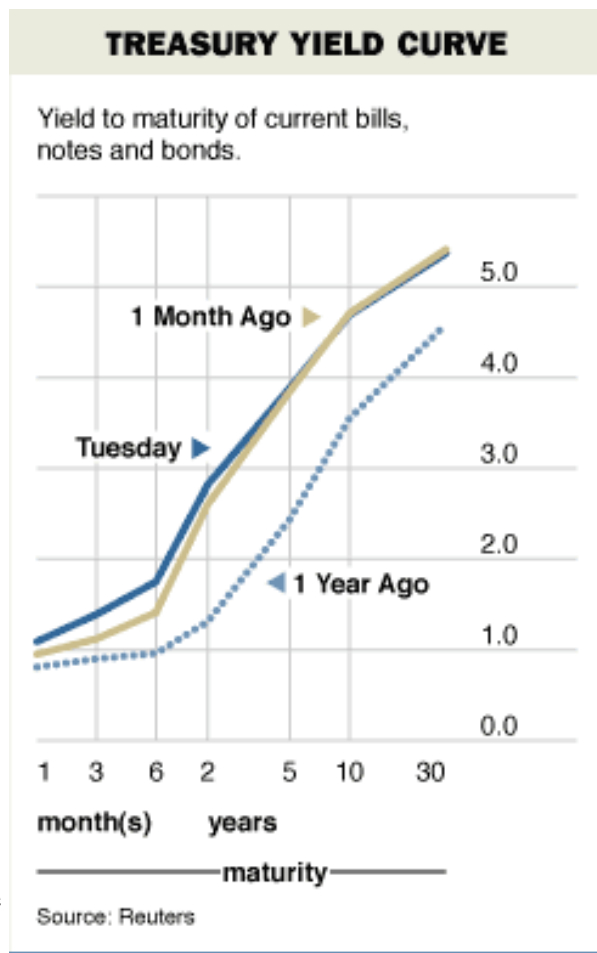
Schwab released a statement saying it supports "efforts to enhance the municipal market's efficiency related to retail customer pricing." UBS said it had changed its procedures and reimbursed investors involved in the case. Prudential, which is paying penalties of \$17,306, said it has also paid restitution to the investors involved in the transactions. Spokesmen for Merrill and Morgan Stanley declined to comment, as did representatives of Edward Jones and Wachovia Securities, which are paying penalties of \$25,181 and \$39,486 respectively. Representatives for First Trust couldn't be reached for comment.

The settlement comes as lawmakers and regulators increase their scrutiny of the bond market, especially in corporate and municipal bonds. The Securities and Exchange Commission recently opened an investigation into conduct of auctions in the \$200 billion auction-rate debt market.

### Treasury Bonds

Treasuries ended higher despite a strong consumer-confidence report, as investors focused mostly on today's Federal Reserve policy meeting. The market dipped briefly on news that the Conference Board's consumer-confidence index jumped to 101.9 for June from 93.1 in May, well above an expected 95 level. But analysts noted that yields already had risen in recent months as the market priced in Fed tightening, and some believe bonds are now fairly valued for a series of gradual rate increases.

At 4 p.m., the benchmark 10-year note was up 15/32 point, or \$4.69 per \$1,000 face value, at 100 16/32. Its yield fell to 4.686% from 4.743% Monday, as yields move inversely to prices. The 30-year bond's price was up 22/32 point at 100 3/32 to yield 5.368%, down from 5.417% Monday.



--Brian Blackstone contributed to this article.

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