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NEWS RELEASE

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FINRA Issues Guidance to Investors Caught in ARS Auction Failures

Washington, D.C. — The Financial Industry Regulatory Authority (FINRA) today spelled out the options available to investors holding unexpectedly illiquid auction rate securities (ARS) because of recent developments in the credit market that have resulted in many ARS auctions failures.

The FINRA Investor Alert [Auction Rate Securities: What Happens When Auctions Fail](#) does not endorse any particular course of action by ARS investors, but does explain the alternatives open to them.

Investors who purchase ARS are typically seeking a cash-like investment that pays a higher yield than money market mutual funds or certificates of deposit. There are generally two types of ARS - bonds with long-term maturities (20 to 30 years) and preferred shares with a cash dividend. The interest on the bonds and the dividends on the preferred stock shares are variable. Those variable rates are set through auctions for a specified, short term usually measured in days - seven, 14, 28 or 35. These auctions provide the primary source of liquidity to ARS investors who wish to sell their investments. But due to recent developments in the credit market - including downgrades in the credit ratings of bond issuers and bond insurers - a significant number of auctions have failed, because there have been more sellers than buyers. As a result, some investors who counted on immediate access to their funds by selling at auction have been forced to hold on to their ARS.

"If you need your money in a hurry, loss of liquidity is a financial hardship," said John Gannon, FINRA's Senior Vice President for Investor Education. "We want investors who have been affected by the recent auction failures to know what options are available to them."

The first thing ARS investors should do is read the offering documents for their investments carefully to determine if the issuer has made provisions in anticipation of illiquidity and failed auctions. Some issuers of bonds or preferred shares may have reserved the right to convert the ARS into a fixed or variable rate security, or to call the instrument at a certain price.

ARS investors who cannot liquidate their holdings because of failed auctions have several options open to them, including:

Continuing to Hold. If you have no need to access the money invested in the ARS immediately, you may want to consider holding until the next auction, which usually will be less than a month away. Typically, when an auction fails, investors receive an interest rate or dividend set above market rates until the next auction.

Selling in the Secondary Market. You may wish to consider selling in the secondary market to a third party. Also, although your brokerage firm is not required to purchase your ARS in the secondary market, it may be willing to do so. Your broker owes you a duty to obtain best execution, but you should keep in mind that selling outside of the auction process may make it harder to determine if you are getting a fair value, and may result in your getting a lower price. In addition, you need to factor in the costs or fees not associated with an auction sale.

Borrowing on Margin. Some firms are offering to lend customers money to help them meet their cash flow needs. Be aware that the interest rate charged on these loans may exceed the yield you're getting on the

underlying security. Also, borrowing against a tax-exempt security (some auction rate bonds, such as those issued by municipalities, may offer tax advantages) may cause you to lose the ability to deduct some or all of the margin loan interest from your taxes. To learn more about the risks of margin trading, see the FINRA Investor Alert [Investing with Borrowed Funds: No "Margin" for Error](#).

Liquidating Other Investments. If you have immediate cash needs, you might also consider selling other securities in your portfolio. When weighing this option, be sure to consider factors such as the total transaction costs you would incur, whether the sale would trigger adverse tax consequences and how the liquidation would impact the balance of your portfolio.

Investors who have a problem related to ARS that their brokerage firm did not resolve satisfactorily can file a complaint online at FINRA's [Investor Complaint Center](#).

To receive FINRA's Investor Alerts and other important investor information via email, sign up for FINRA's [Investor News](#).

FINRA, the Financial Industry Regulatory Authority, is the largest non-governmental regulator for all securities firms doing business in the United States. Created in 2007 through the consolidation of NASD and NYSE Member Regulation, FINRA is dedicated to investor protection and market integrity through effective and efficient regulation and complementary compliance and technology-based services. FINRA touches virtually every aspect of the securities business—from registering and educating all industry participants to examining securities firms; writing and enforcing rules and the federal securities laws; informing and educating the investing public; providing trade reporting and other industry utilities; and administering the largest dispute resolution forum for investors and registered firms. For more information, please visit our Web site at www.finra.org.

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