

RBC confirms U.S. subpoena over auction-rate securities

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Royal Bank of Canada was one of a number of financial institutions subpoenaed in the United States in connection with auction-rate securities, the bank confirmed yesterday.

The \$330-billion (U.S.) market for auction-rate securities collapsed this year as a result of the liquidity crunch, leaving many American investors stuck with frozen securities.

The Wall Street Journal reported yesterday that Citigroup Inc. is negotiating with federal regulators to settle allegations it wrongly told customers the securities were safe and liquid. Citigroup could wind up buying back more than \$5-billion of the securities from investors and paying a fine of up to \$100-million, the newspaper reported.

Late last month, New York Attorney-General Andrew Cuomo launched a multibillion-dollar securities fraud lawsuit against UBS AG, alleging it was falsely selling and marketing auction-rate securities as safe. He further alleged that as the market for the securities began to collapse, the bank's top executives quickly sold \$21-million of their personal holdings of auction-rate securities while continuing to market them.

"UBS is not alone in this scheme," Mr. Cuomo had told reporters. "There are other institutions which participated, but UBS is a major player."

His office has reportedly subpoenaed dozens of companies since beginning its investigation.

"I can confirm that RBC Capital Markets Corp., along with others, were subpoenaed back in April," Royal Bank spokeswoman Beja Rodeck said in an e-mail yesterday.

Veritas Investment Research analyst Ohad Lederer wrote in a note to clients this week: "We don't know how badly [RBC] will get stung by its involvement in the auction-rate securities market. The facts are few, we admit, but combined with a pinch of imagination and a dash of conjecture, it is not a stretch to see how the issue could adversely weigh on Royal's U.S. strategy and/or results."

The bank's inventory of auction-rate securities built up from a negligible balance to \$3.7-billion in the weeks leading up to a decision in early February by a number of U.S. banks to withdraw their support for the market (which precipitated the collapse), Mr. Lederer noted. And RBC has already taken a \$212-million writedown on its securities, and has disclosed that it is a "remarketing agent" for a program of \$21.3-billion, of which \$20.2-billion is student loans.

Mr. Lederer said he assumes elevated funding costs are to blame for most of Royal's writedown.