

# MSRB REPORTS

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Municipal Securities Rulemaking Board

November 1987

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## Board Elects Hearty Chairman; Comerford Vice Chairman

James B.G. Hearty has been elected Chairman of the Board and Terrence E. Comerford, Vice Chairman. Mr. Hearty is Managing Director of the Bank of Boston, Boston, Massachusetts and Mr. Comerford is Managing Director of PaineWebber Inc., San Francisco, California. The new officers began their one-year terms on October 1, 1987.

Mr. Hearty is in charge of all fixed income underwriting, trading and sales at the Bank of Boston. Prior to joining the bank in 1977, he was a portfolio assistant at Bankers Trust Company in New York for a year and an agent for Northwestern Mutual Life Insurance Company in Boston for three years. Mr. Hearty graduated from Williams College.

Mr. Comerford is a Senior Investment Banker at Paine-Webber Inc. He joined Blythe & Company, Inc., a securities firm that later merged with PaineWebber, in 1957. Mr. Comerford also serves on the Technical Advisory Committee of the California Debt Advisory Commission. He received an M.B.A. from Northwestern University.

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### Calendar

October 13	—	Effective date of G-12 and G-15 on confirmation disclosure requirements
October 14	—	Effective date of G-34 on CUSIP numbers for secondary market securities
	—	Effective date of G-8 on delivery of official statements
	—	Effective date of G-19 on suitability requirements
January 10	—	Comments due on G-12 and G-15 on BEO securities
Pending	—	G-12 and G-15 on delivery of interchangeable securities
	—	G-32 on sole underwriting period

## From the Chairman

The Board begins its new year in the wake of events that have shaken the municipal securities market. We all have been affected profoundly by the 1986 tax legislation, higher interest rates, reduced profitability, and the contraction of the dealer community. In addition, the controversy surrounding escrowed-to-maturity bonds has disrupted an important segment of the industry. We also await the results of the SEC's investigations into the WPPSS default and certain alleged arbitrage bonds.

The Board is fully aware of these issues and has been working to resolve problems in the structure of the municipal securities industry. These problems share a common factor: the timing and flow of information to market participants. Obvious examples of flaws in the market are the failure of Board rule G-32 to effect the dissemination of official statements and the recent escrowed-to-maturity controversy.

Resolving these problems will not be easy. Simply amending or adding MSRB rules may not ensure that the right information reaches the market at the time it is most useful. The Board will be exploring various solutions and is committed to taking whatever actions are necessary. Toward these ends, the Board will be working closely with the SEC as well as the Public Securities Association, the Government Finance Officers Association and other industry trade groups.

Devising efficient and effective solutions, however, is impossible without *your* thoughtful participation. As the Board puts its suggestions forward, I urge you to examine their impact on all market participants and to convey your views to the Board or to any one of its members listed in this issue of *MSRB Reports*.

**James B.G. Hearty**  
MSRB Chairman, 1987-1988

## Board Members 1987 to 1988

### Bank Representatives

**James B.G. Hearty, Managing Director**  
*Bank of Boston* ..... Boston  
(617) 434-4800

**Eric N. Keber, Managing Director**  
*Bankers Trust Company* ..... New York  
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**G. Timothy Lane, Executive Vice President**  
*Barnett Banks, Inc.* ..... Jacksonville  
(904) 791-7602

**W. Graham Lynch, Senior Vice President**  
*Wachovia Bank & Trust Company, Inc.* ... Winston-Salem  
(919) 770-4611

**John W. Rowe, Executive Vice President**  
*Center Bank, N.A.* ..... St. Louis  
(314) 554-6424

### Public Representatives

**Thomas H. Locker, Comptroller**  
*Orange County* ..... Orlando  
(305) 236-5690

**Leslie Nelman, Vice President**  
*Farmers Insurance Group* ..... Los Angeles  
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**Carroll M. Perkins, Associate General Manager**  
*Salt River Project* ..... Phoenix  
(602) 236-5400

**Elizabeth A. Roistacher, Professor of Economics**  
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(212) 772-4098

**Richard S. West, President**  
*American Syndicate Advisors* ..... Boston  
(617) 357-9110

### Securities Firm Representatives

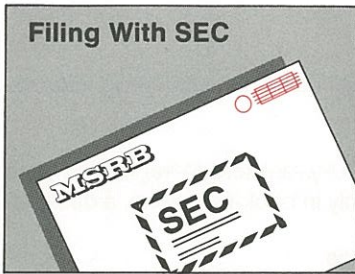
**W.J. Turner L. Cobden, Senior Vice President and Manager**  
*Smith Barney, Harris Upham & Co., Inc.* ..... New York  
(212) 698-3452

**Terrence E. Comerford, Managing Director**  
*PaineWebber Inc.* ..... San Francisco  
(415) 954-5999

**Michael E. Dougherty, President**  
*Dougherty, Dawkins, Strand & Yost, Inc.* ..... Minneapolis  
(612) 341-6016

**David J. Master, Executive Vice President**  
*Boettcher & Company, Inc.* ..... Houston/Denver  
(713) 226-5700

**Thomas Sexton, Managing Director**  
*First Boston Corporation* ..... New York  
(212) 909-3656



**Route to:**

- Manager, Muni. Dept.
- Underwriting
- Trading
- Sales
- Operations
- Public Finance
- Compliance
- Training
- Other \_\_\_\_\_

**Delivery of Interchangeable Securities: Rules G-12 and G-15**

**Amendments Filed**

**The amendments would**

- permit interchangeable securities to be delivered in either bearer or registered form, unless the parties agree to a specific form of delivery;
- eliminate the one-day reclamation provision for interchangeable securities delivered in registered form; and
- eliminate the requirement to designate a security as being in registered form on inter-dealer and customer confirmations.

On October 6, 1987, the Board filed with the Securities and Exchange Commission proposed amendments to rule G-12 on uniform practice and rule G-15 on confirmation, clearance and settlement of transactions with customers.<sup>1</sup> The proposed amendments would permit deliveries of securities issuable in either bearer or registered form (interchangeable securities) to be in either form, unless the parties agree to a specific form of delivery. The proposed amendments also would eliminate the one-day reclamation provision in rule G-12(g)(iii)(A)(4) for securities delivered in registered form, and the requirement in rules G-12(c)(vi)(B) and G-15(a)(iii)(B) to designate a security as being in registered form on confirmations. The Board has requested that the SEC delay the effectiveness of the proposed amendments for a period of six months following the date of SEC approval to give dealers a chance to make necessary computer changes and to educate personnel.

**Background**

Many issues of municipal securities issued prior to the effective date of the Tax Equity and Fiscal Responsibility Act of 1982

(TEFRA) permit holders to choose registered or bearer certificates. At that time, the municipal securities market primarily was composed of bearer issues, and the Board's good delivery rule, rule G-12(e), reflected the expectation that inter-dealer deliveries of municipal securities would be in bearer form. Specifically, rule G-12(e)(vi)(A), on inter-dealer deliveries, provides:

Delivery of securities which are issuable in both bearer and registered form shall be in bearer form unless otherwise agreed by the parties; *provided, however*, that delivery of securities which are required to be in registered form in order for interest thereon to be exempt from Federal income taxation shall be in registered form.

In addition, rule G-12(g)(iii)(A)(4), on reclamation, permits a dealer to reclaim interchangeable securities within one business day of their delivery if they are delivered in registered form and were not identified as such at the time of trade.

In March 1987, the Public Securities Association requested that the Board reconsider the presumption in favor of bearer certificates contained in rule G-12(e) and permit deliveries of securities of interchangeable issues to be made in either bearer or registered form, unless the parties specifically agree otherwise. In June 1987, the Board published for comment proposed amendments to rules G-12 and G-15.<sup>2</sup>

**Summary of Comments**

The Board received 18 comments on the proposed amendments, with a majority of commentators supporting the proposed amendments.<sup>3</sup> Most commentators stated that the presumption in favor of bearer certificates in the Board's rules, which was adopted prior to the TEFRA requirement for registered securities, is inconsistent with today's registered environment and the use of automated clearance and settlement systems.

The commentators in favor of the proposed amendments

**Questions about this notice may be directed to Harold L. Johnson, Assistant General Counsel.**

<sup>1</sup> SEC File No. SR-MSRB-87-12. Comments on the amendments should be filed directly with the Commission and should refer to the filing number.

<sup>2</sup> *MSRB Reports*, vol. 7, no. 3 (June 1987) at 9.

<sup>3</sup> Thirteen of the commentators supported the draft amendments, while five opposed them. The comments are available for inspection at the Board's offices.

stated that the amendments would result in cost savings for the industry.<sup>4</sup> Some commentators noted that the amendments would allow depositories to convert interchangeable securities on deposit from bearer to registered form and thereby minimize the costs and risks of housing certificates, clipping coupons, monitoring calls and other details of processing bearer certificates. A number of the commentators stated that the proposed amendments would reduce failed transactions and permit additional transactions to be settled by book-entry rather than by more expensive physical delivery. The majority of the commentators argued that customers would benefit from the proposed amendments because of the better call notification, prompt interest payments and the relative safety from theft or loss offered by registered certificates.

The commentators opposing the proposed amendments noted that some customers continue to request delivery of bearer certificates and expressed concern that the proposed amendments would make it more difficult to provide bearer certificates to these customers.<sup>5</sup> The Board believes, however, that investors generally have become more comfortable with registered securities as nearly all new issue activity since July 1, 1983, TEFRA's effective date, has been in registered form. The Board urges dealers to educate their customers about the benefits of registration over the next six months.

### Summary of Amendments

The proposed amendments would eliminate the presumption in favor of bearer securities in rules G-12(e)(vi)(A) and G-15(c)(iv)(A) and would permit deliveries of interchangeable securities to be in either bearer or registered form, unless there is an agreement between parties on a specific form of delivery. The proposed amendments also would eliminate the one-day reclamation provision in rule G-12(g)(iii)(A)(4) for interchangeable securities delivered in registered form. Finally, since deliveries could be made in either registered or bearer form and since a dealer may not know the form of the security prior to delivery, the amendments would eliminate the requirement in rules G-12(c)(vi)(B) and G-15(a)(iii)(B) to designate a security as being in registered form on confirmations.

October 6, 1987

### Text of Proposed Amendments\*

#### Rule G-12. Uniform Practice

- (a) through (b) No change.
- (c) *Dealer Confirmations.*
  - (i) through (v) No change.
  - (vi) In addition to the information required by paragraph (v)

above, each confirmation shall contain the following information, if applicable:

- (A) No change.
- (B) if the securities are "~~fully registered,~~" "~~registered as to principal only,~~" or available only in book-entry form, a designation to such effect;
- (C) through (l) No change.
- (d) No change.
- (e) *Delivery of Securities.* The following provisions shall, unless otherwise agreed by the parties, govern the delivery of securities:

- (i) through (v) No change.
- (vi) *Form of Securities.*
  - (A) *Bearer and Registered Form.* Delivery of securities which are issuable in both bearer and registered form ~~shall~~ may be in bearer form unless otherwise agreed by the parties; *provided, however,* that delivery of securities which are required to be in registered form in order for interest thereon to be exempt from Federal income taxation shall be in registered form.

- (B) No change.
- (vii) through (xvi) No change.
- (f) No change.
- (g) *Rejections and Reclamations.*

- (i) through (ii) No change.
- (iii) *Basis for Reclamation and Time Limits.* A reclamation may be made by the receiving party or a demand for reclamation may be made by the delivering party if, subsequent to delivery, information is discovered which, if known at the time of the delivery, would have caused the delivery not to constitute good delivery, provided such reclamation or demand for reclamation is made within the following time limits:

- (A) Reclamation or demand for reclamation by reason of the following shall be made within one business day following the date of delivery:

- (1) through (3) No change.
- ~~(4) not good delivery because securities (which are issuable in both bearer and registered form) were delivered in registered form and were not identified as such at the time of trade.~~
- (B) through (D) No change.
- (iv) through (vi) No change.
- (h) through (l) No change.

#### Rule G-15. Confirmation, Clearance and Settlement of Transactions with Customers

- (a) *Customer Confirmations.*
  - (i) through (ii) No change.
  - (iii) In addition to the information required by paragraphs (i) and (ii) above, each confirmation to a customer shall contain the following information, if applicable:
    - (A) No change.
    - (B) if the securities are "~~fully registered,~~" "~~registered as to principal only,~~" or available only in book-entry form, a designa-

<sup>4</sup> Even some of the commentators opposing the proposed amendments acknowledged the cost savings that the proposed amendments would provide.

<sup>5</sup> Delays in the transfer of registered securities, the possibility of transfer fees and relative ease of transferring bearer securities are cited by the commentators as reasons for the investor preference for bearer certificates.

\* Underlining indicates new language; strike-through indicates deletions.

tion to such effect;

(C) through (J) No change.

(iv) through (ix) No change.

(b) No change.

(c) *Deliveries to Customers.* Except as provided in section (d) below, a delivery of securities by a broker, dealer, or municipal securities dealer to a customer or to another person acting as agent for the customer shall, unless otherwise agreed by the parties or otherwise specified by the customer, be made in accordance with the following provisions:

(i) through (iii) No change.

(iv) *Form of Securities.*

(A) *Bearer and Registered Form.* Delivery of securities which are issuable in both bearer and registered form shall may be in bearer form unless otherwise agreed by the parties; *provided, however,* that delivery of securities which are required to be in registered form in order for interest thereon to be exempt from Federal income taxation shall be in registered form.

(B) No change.

(v) through (xii) No change.

(d) through (e) No change.



**Route to:**

- Manager, Muni. Dept.
- Underwriting
- Trading
- Sales
- Operations
- Public Finance
- Compliance
- Training
- Other \_\_\_\_\_

**Confirmation Disclosure of Book-Entry-Only Securities: Rules G-12 and G-15**

**Comments Requested**

The Board requests comments on draft amendments deleting the requirement in the rules that dealers designate on confirmations securities that are available only in book-entry form.

Rules G-12(c) and G-15(a) set forth the information that must appear on inter-dealer and customer confirmations, respectively. The Board is considering deleting the requirement in the rules to designate on confirmations securities that are available only in book-entry form.

In recent years, a number of issuers have begun to issue municipal securities in book-entry-only form. In these issues, the issuer deposits one "global" certificate for each maturity of the issue at a securities depository registered with the Securities and Exchange Commission. Physical certificates are not available to investors. Ownership positions and transactions in the issue among the depository's members are recorded in the depository's records. Investors that are not depository participants maintain ownership positions through securities firms, banks or clearing agents that are depository members.<sup>1</sup> In addition to these issues, some municipal securities are available only by book-entry on the books of a custodian other than a registered securities depository.

Rules G-12(c)(vi)(B) and G-15(a)(iii)(B) currently state that, if

the securities in a transaction are fully registered, registered as to principal only or available only in book-entry form, the confirmation must designate this fact. On October 6, 1987, the Board filed with the Securities and Exchange Commission amendments to the rules that, among other things, would delete the requirement to designate securities as fully registered or registered as to principal only.<sup>2</sup>

**Summary of Draft Amendments**

The Board is seeking comments on draft amendments to rules G-12(c)(vi) and G-15(a)(iii) that would delete the requirement to designate securities as book-entry-only on confirmations.<sup>3</sup> The Board questions whether the book-entry form of securities is a major factor in investment decisions, requiring disclosure on customer confirmations.<sup>4</sup> With regard to inter-dealer transactions, the Board notes that securities professionals are assumed to know the securities which they are trading, including the book-entry-only nature of certain issues.<sup>5</sup> Since a designation of book-entry-only form on an inter-dealer confirmation does not assist in identifying the particular security that is the subject of the transaction, the Board believes that it may be unnecessary to continue to require this information on inter-dealer confirmations.<sup>6</sup>

The Board requests comment from interested persons on the draft amendments. The Board would welcome comment on

**Comments on the matters discussed in this notice should be submitted not later than January 10, 1988, and may be directed to Harold L. Johnson, Assistant General Counsel. Written comments will be available for public inspection.**

<sup>1</sup> The Depository Trust Company (DTC) estimates that approximately 23 percent of the principal amount of long-term municipal securities issued in the first six months of 1987 was issued in book-entry-only form at DTC.

<sup>2</sup> These amendments also would allow securities issuable in both registered and bearer form to be delivered in either form. See this issue of *MSRB Reports* at 5-7.

<sup>3</sup> The draft amendments would delete this requirement both for issues that are book-entry-only through registered securities depositories and those that are book-entry-only through other custodians.

<sup>4</sup> Book-entry-only form does not affect the credit risk or interest payment features of a security and tends to reduce the risk of loss, theft and inadequate call notification for individual investors. Dealers nevertheless should alert customers who may be unfamiliar with such issues or who may expect physical delivery that an issue is book-entry-only.

<sup>5</sup> For inter-dealer transactions, the items of information that must be exchanged by securities professionals at the time of trade are governed by contract law and essentially are those items necessary adequately to identify the security that is the subject of the contract. Delivery of book-entry-only securities does not provide a right of reclamation unless the availability of physical certificates was a specific condition of the trade.

<sup>6</sup> The Board is unaware of any issue for which the book-entry-only feature is necessary to distinguish the issue from other similar issues.

whether there is a need for confirmation disclosure of book-entry-only form and the purpose, if any, which such disclosure serves.

October 30, 1987

**Text of Draft Amendments\***

**Rule G-12. Uniform Practice**

- (a) through (b) No change.
- (c) *Dealer Confirmations*
  - (i) through (v) No change.
  - (vi) In addition to the information required by paragraph (v) above, each confirmation shall contain the following information, if applicable:
    - (A) No change.
    - ~~(B) if the securities are available only in book-entry form, a~~

- ~~designation to such effect;~~
- (C) through (I) Renumbered (B) through (H).
- (d) through (I) No change.

**Rule G-15. Confirmation, Clearance and Settlement of Transactions with Customers**

- (a) *Customer Confirmations*
  - (i) through (ii) No change.
  - (iii) In addition to the information required by paragraphs (i) and (ii) above, each confirmation to a customer shall contain the following information, if applicable:
    - (A) No change.
    - ~~(B) if the securities are available only in book-entry form, a designation to such effect;~~
    - (C) through (J) Renumbered (B) through (I).
    - (iv) through (ix) No change.
- (b) through (e) No change.

\* Strike-through indicates deletions.



**Route to:**

- Manager, Muni Dept.
- Underwriting
- Trading
- Sales
- Operations
- Public Finance
- Compliance
- Training
- Other \_\_\_\_\_

## Disclosure of Uncertain Tax Status of Market Discount Securities: Rule G-17

### Interpretation

The Board advises dealers to disclose to customers, at or before the time of trade, the current uncertain tax consequences of purchases of municipal securities at a market discount.

### Rule G-17. Disclosure of Uncertain Tax Status of Market Discount Securities

The Municipal Securities Rulemaking Board has received inquiries concerning the application of Board rules to transactions in municipal securities sold at a market discount. H.R. 3545, recently passed by the House of Representatives, if enacted into law, would require purchasers of discounted securities to realize yearly taxable income.

The pending legislation would apply to "market discount" securities purchased after October 13, 1987. The bill has not

been acted on by the Senate and is not the law. The proposed retroactive effective date of the provision, however, has created some uncertainty concerning the tax consequences to customers who are purchasing market discount securities.

The Board is of the view that while this bill is pending, under rule G-17, on fair dealing, dealers should disclose to customers, at or before the time of trade, that the tax consequences of purchases, made on or after October 13, 1987, of municipal securities at a market discount are uncertain.<sup>1</sup> The uncertain tax status and the duty to disclose it apply to "tax swaps" involving market discount securities as well as to other sales of market discount securities to customers. Customers also should be alerted to the potential effect on the market value of such securities if the proposed provision is enacted into law.

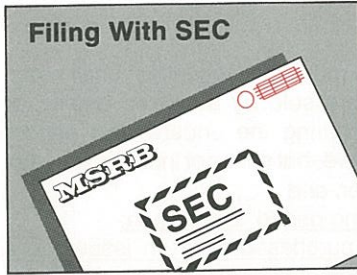
With respect to confirmation disclosure, Board rule G-15(a) contains no specific requirement for dealers to disclose on confirmations the uncertain tax consequences of a transaction. The Board notes that a dealer has the discretion to include such information in the description area of the confirmation if the dealer deems this advisable. Confirmation disclosure, however, does not excuse the duty of a dealer to explain material facts about a transaction to a customer at or before the time of trade.

*MSRB Interpretation of November 11, 1987, by Angela Desmond, General Counsel.*

<sup>1</sup> Rule G-17 provides:

In the conduct of its municipal securities business, each broker, dealer and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest or unfair practice.





**Route to:**

- Manager, Muni. Dept.
- Underwriting
- Trading
- Sales
- Operations
- Public Finance
- Compliance
- Training
- Other \_\_\_\_\_

**Sole Underwriting Period: Rule G-32**

**Amendment Filed**

The proposed amendment would define the underwriting period for sole underwriters.

On October 5, 1987, the Board filed with the Securities and Exchange Commission a proposed amendment to rule G-32 on disclosures on connection with new issues. The amendment would define the "underwriting period" in new issue distributions made by sole underwriters (sole underwritings) and thus would identify the transactions that are subject to the requirements of rule G-32. The amendment will become effective upon approval by the Commission. Persons wishing to comment on the amendment should comment directly to the Commission.<sup>1</sup>

**Background**

Rule G-32 requires all dealers selling new issue municipal securities during the underwriting period to deliver a copy of the official statement for the issue, if one will be prepared, to each customer no later than settlement with the customer.<sup>2</sup> The underwriting period is defined to begin with the first submission to a syndicate of an order for the purchase of the securities or the purchase of such securities from the issuer, whichever first occurs. The underwriting period ends when the issuer delivers the securities to the syndicate or the syndicate no longer retains an unsold balance of the securities, whichever last occurs. This definition is designed to ensure that a sufficient number of investors receive new issue disclosures.<sup>3</sup>

The Board has interpreted rule G-32 to apply to sole

underwritings notwithstanding the use of the term "syndicate" in the definition of underwriting period and has stated that the number of underwriters is irrelevant to the purposes of the rule.<sup>4</sup> The definition of underwriting period for syndicated underwritings, however, is not appropriate for sole underwritings because a sole underwriter may retain portions of an issue in its inventory long after the delivery of the issue by the issuer and completion of the initial reoffering.

**Summary of Amendment**

The amendment would define the underwriting period for sole underwritings to begin upon the first submission of an order for the issue or the purchase of the issue from the issuer by the underwriter, whichever first occurs. It would define the underwriting period to end when both of the following two conditions are met: (1) the issuer delivers the securities to the underwriter; and (2) the underwriter no longer retains an unsold balance of the securities or 21 calendar days elapse after the first submission of an order to the underwriter, whichever first occurs.

**Summary of Comments**

In March 1987, the Board solicited comments on the proposed amendment and received three comment letters.<sup>5</sup> The two commentators who addressed the substance of the proposed rule change generally supported it.<sup>6</sup> One commentator suggested the underwriting period for sole and syndicated underwritings end five business days following the "initial street settlement date" to make it easier for dealers that are not

**Questions about this notice may be directed to Harold L. Johnson, Assistant General Counsel.**

<sup>1</sup>SEC File No. SR-MSRB-87-13. Comments filed with the Commission should refer to the file number.

<sup>2</sup>For negotiated issues, certain underwriting information also must be provided in writing. If an official statement in final form is not prepared by or on behalf of the issuer, an official statement in preliminary form, if any, must be sent to the customer with a notice that no final official statement is being prepared. The rule also makes certain disclosure delivery requirements for inter-dealer transactions to facilitate the availability of official statements on new issues.

<sup>3</sup>All dealers selling new issue securities during the underwriting period, including those dealers that are not underwriters for the issue, are subject to the requirement of rule G-32 to deliver new issue disclosures to customers.

<sup>4</sup>MSRB Interpretation of April 18, 1979, by Mark K. Sisitsky, *MSRB Manual* (CCH) para. 3656.15 at 5253.

<sup>5</sup>*MSRB Reports* Vol. 7, No.2 at 17-18 (March 1987). The comment letters are available for inspection at the Board's Offices.

<sup>6</sup>One commentator apparently misunderstood the term "underwriting period" to relate to a deadline for delivery of official statements to customers rather than a determination of the transactions subject to rule G-32. The proposed amendment does not alter the requirement that new issue disclosure documents be delivered to a customer no later than settlement of the transaction.

underwriters to determine when the underwriting period ends. The Board believes that the proposed rule change and the definition of underwriting period for syndicated underwritings provide adequate objective criteria for dealers to determine their obligations under rule G-32. Another commentator suggested replacing the 21-day period in the proposed rule change with a 30-day period. The Board, however, concluded that the 21-day period provides the appropriate balance between the disclosure objectives of rule G-32 and the burdens on dealers to comply with the rule.

October 6, 1987

**Text of Proposed Amendment\***

**Rule G-32. Disclosure in Connection with New Issues**

(a) through (b) No change.

(c) *Definition of New Issue Municipal Securities and Official Statement.*

For purposes of this rule, the following terms have the following meanings:

(i) ~~¶~~The term "new issue municipal securities" shall mean securities of an issue that are sold by a broker, dealer, or municipal securities dealer during the underwriting period, ~~defined in rule G-11 of the Board,~~ but shall not include issues of tax-exempt commercial paper. ~~and~~

(ii) The term "underwriting period" shall mean:

(A) for securities purchased from an issuer by a syndicate, the period defined in paragraph (a)(ix) of rule G-11, on sales of new issue municipal securities during the underwriting period; and

(B) for securities purchased from an issuer by one broker, dealer or municipal securities dealer, the period commencing with the first submission to the broker, dealer or municipal securities dealer of an order for the purchase of the securities or the purchase of such securities from the issuer, whichever first occurs, and ending at such time as the following two conditions both are met: (1) the issuer delivers the securities to the broker, dealer or municipal securities dealer, and (2) the broker, dealer or municipal securities dealer no longer retains an unsold balance of the securities purchased from the issuer or 21 calendar days elapse after the date of the first submission of an order for the securities, whichever first occurs.

~~(ii)~~ renumbered (iii) No change.

\* Underlining indicates new language; strike-through indicates deletions.

## Notice of Approval



## Route to:

- Manager, Muni. Dept.
- Underwriting
- Trading
- Sales
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- Compliance
- Training
- Other \_\_\_\_\_

## CUSIP Numbers for Secondary Market Securities: Rule G-34

### Amendments Approved

The amendments require dealers to apply for new CUSIP numbers for secondary market securities that have one CUSIP number but are no longer a single, fully fungible group of securities.

On October 14, 1987, the Securities and Exchange Commission approved amendments to rule G-34 on CUSIP numbers and the dissemination of initial trade date information.<sup>1</sup> The amendments require dealers to apply for new CUSIP numbers for secondary market securities that are assigned a CUSIP number which no longer designates a single, fully fungible group of securities. The amendments became effective upon approval by the Commission.

### Background

Rule G-34 requires dealers to apply to the Board or its designee for new CUSIP numbers in certain specified circumstances.<sup>2</sup> Section (a) of the rule requires any dealer that acquires a new issue of municipal securities, as a principal or agent, to apply for the assignment of CUSIP numbers to the new issue.<sup>3</sup> If the new issue will be used to refund an outstanding issue of municipal securities in such a manner that securities previously assigned one CUSIP number are refunded to more than one date or price, the dealer also must apply for new CUSIP numbers for the outstanding issue. Section (b) of rule G-34 requires any dealer that acquires or arranges for a transferable instrument altering the security or source of payment for part of a maturity of an outstanding issue to apply for new CUSIP numbers for the securities that are subject to the transferable instrument when traded with the instrument attached.<sup>4</sup>

Dealers and the automated clearance and settlement sys-

tems depend upon CUSIP numbers to identify municipal securities and the usefulness of the CUSIP numbering system to identify securities is diminished if the same CUSIP number is assigned to two or more types of securities having different features. Several circumstances not specifically addressed by rule G-34, however, such as secondary market insurance obtained by customers or remarketed securities, may cause secondary market securities previously having identical features no longer to be fungible.

### Summary of Amendments

The amendments require a dealer to apply for new CUSIP numbers in connection with the sale or offering of any secondary market municipal securities that are assigned a CUSIP number that no longer designates securities that are identical with respect to certain specified features. These features, which also are used to determine CUSIP number assignment for new issues, are listed in rule G-34(a)(i)(A). They are:

- (1) complete name of issue and series designation, if any;
- (2) interest(s) rates and maturity date(s);
- (3) dated date;
- (4) type of issue (e.g., general obligation, limited tax or revenue);
- (5) type of revenue, if the issue is a revenue issue;
- (6) details of all redemption provisions;
- (7) name of any company or other person in addition to the issuer obligated, directly or indirectly, with respect to the debt service on all or part of the issue; and
- (8) any distinction(s) in the security or source of payment of the debt service on the issue.

The amendments require a dealer applying for new CUSIP numbers for secondary market securities to provide the CUSIP

**Questions about the amendments may be directed to Harold L. Johnson, Assistant General Counsel.**

<sup>1</sup> SEC Release No. 34-25020.

<sup>2</sup> The Board has designated the CUSIP Service Bureau to receive these applications.

<sup>3</sup> The CUSIP numbers must be obtained on or prior to the date of sale of the issue. The rule also requires any dealer serving as a financial advisor to the issuer of a competitive issue to be responsible for ensuring that CUSIP numbers are assigned to the issue.

<sup>4</sup> Such instruments include insurance with respect to debt service on the issue, put or tender options, letters of credit or guarantee or any similar devices.

number previously assigned to the securities and other information necessary to ensure the appropriate CUSIP number assignment to the securities. The amendments apply only if the secondary market securities are eligible for CUSIP number assignment. The CUSIP Service Bureau is expanding the types of municipal securities eligible for CUSIP number assignment and the Board urges dealers to contact the Service Bureau to determine the CUSIP eligibility of secondary market securities.

October 14, 1987

### Text of Amendments\*

#### Rule G-34. CUSIP Numbers and Dissemination of Initial Trade Date Information

(a) No change.

(b) *Secondary Market Securities.*

~~(i) Except as otherwise provided in this section (b),~~ Each municipal securities broker, dealer or municipal securities dealer who that, in connection with a sale or an offering for sale of part, but not all, of an outstanding maturity of an issue of municipal securities, acquires or arranges for the acquisition of a transferable instrument applicable to such part which alters the security or source of payment of such part shall apply in writing to the Board or its designee for the assignment of a CUSIP number which will be used to designate the part of the outstanding maturity of the issue which is the subject of the instrument when traded with the instrument attached. Such instruments shall include (A) insurance with respect to the payment of debt service on such portion, (B) a put option or tender option, (C) a letter of credit or guarantee, or (D) any other similar device. This paragraph (i) shall not apply with respect to any part of an outstanding maturity of an issue of municipal securities with respect to which a CUSIP number that is applicable to such part when traded with an instrument which alters the security or source of payment of such part has already been assigned.

(ii) Each broker, dealer or municipal securities dealer, in

connection with a sale or an offering for sale of part of a maturity of an issue of municipal securities which is assigned a CUSIP number that no longer designates securities identical with respect to all features of the issue listed in items (1) through (8) of subparagraph (a)(i)(A) of this rule, shall apply in writing to the Board or its designee for a new CUSIP number or numbers to designate the part or parts of the maturity which are identical with respect to items (1) through (8) of subparagraph (a)(i)(A).

~~(ii)(iii) The municipal securities broker, dealer or municipal securities dealer shall make the application required under this section (b) as promptly as possible, and shall provide to the Board or its designee: information sufficient to identify~~

(A) the previously assigned CUSIP number;

(B) all information on the features of the maturity of the issue listed in items (1) through (8) of subparagraph (a)(i)(A) of this rule and documentation of the features of such maturity sufficient to evidence the basis for CUSIP number assignment; and,

(C) if the application is based on an instrument affecting the source of payment or security for a part of a maturity of an issue, information on and to describe the nature of the instrument acquired, including the name of any party obligated with respect to debt service under the terms of such instrument. The municipal securities broker or municipal securities dealer also shall provide and documentation sufficient to evidence the basis for number assignment and nature of the instrument acquired.

~~(iii) The provision of this section (b) shall not apply with respect to any part of an outstanding maturity if an issue of municipal securities with respect to which a CUSIP number that is applicable to such part when traded with an instrument which alters the security or source of payment of such part has already been issued.~~

(c) No change.

(d) *Eligibility.* The provisions of this rule shall not apply to an issue of municipal securities (or for the purpose of section (b) ~~the any part of an outstanding maturity of an issue when traded with an instrument which alters the security or source of payment of such part~~) which does not meet the eligibility criteria for CUSIP number assignment.

\* Underlining indicates new language; strike-through indicates deletions.



**Route to:**

- Manager, Muni. Dept.
- Underwriting
- Trading
- Sales
- Operations
- Public Finance
- Compliance
- Training
- Other \_\_\_\_\_

**Miscellaneous Technical Amendments: Rules G-8, G-12 and G-15, and G-19**

**Amendments Approved**

The technical amendments to

- rule G-8 require dealers to maintain records of all deliveries of disclosure documents required under rule G-32;
- rules G-12 and G-15 correct certain cross-references regarding confirmation disclosure requirements; and
- rule G-19 prohibits a dealer from effecting a transaction for a discretionary account unless the dealer determines that it is suitable.

On October 13, 1987, the Securities and Exchange Commission approved miscellaneous technical amendments to rules G-12 and G-15 on good delivery,<sup>1</sup> and on October 14, 1987, the Commission approved miscellaneous technical amendments to rule G-8 on books and records<sup>2</sup> and rule G-19 on suitability.<sup>3</sup> The amendments became effective upon approval by the Commission.

Rule G-8(a)(xiii) requires dealers to make and keep records of all deliveries of disclosure documents required under rule G-32. The technical amendments to rule G-8(f) require dealers complying with SEC rule 17a-3, which does not incorporate the rule G-8(a)(xiii) recordkeeping requirements, to make and keep records of deliveries of official statements as required by rule G-8(a)(xiii).

Rules G-12(e) and G-15(c) specify the requirements for physical deliveries of securities on inter-dealer and customer transactions, respectively. In 1986, the Board amended rules G-12(c)(vi) and G-15(a)(iii) to require a disclosure on the confirmation if securities are subject to federal taxation or the federal

alternative minimum tax. The amendments revise the good delivery rules, correcting the cross-references in rules G-12(e) and G-15(c) to these confirmation provisions, and conform the securities description required on the delivery ticket by rules G-12(e) and G-15(c) with the descriptions required on confirmations.

Rule G-19 was amended in 1985 to prohibit a professional from recommending a transaction in municipal securities unless the professional has reasonable grounds to believe, and does believe, that the recommendation is suitable for the customer in light of information available from the issuer of the security. Rule G-19(d)(ii) on discretionary accounts was not, however, cross-referenced to this requirement. The amendment to rule G-19(d)(ii) prohibits dealers from effecting a transaction in municipal securities for a discretionary account unless the dealer first determines that the transaction is suitable in terms of both customer and issuer information. In addition, rule G-19(d)(ii) references subparagraph (c)(ii)(B), which permits a dealer to recommend a transaction in municipal securities when information about the customer is not known or furnished. In keeping with past Board interpretations, the amendment to rule G-19 prohibits a dealer from effecting a transaction with or for a discretionary account unless the professional first makes an affirmative determination of the suitability of the transaction for a customer.

**October 14, 1987**

**Texts of Amendments\***

**Rule G-8. Books and Records to Be Made by Municipal Securities Brokers and Municipal Securities Dealers**

(a) through (e) No change.

(f) *Compliance with Rule 17a-3.* Municipal securities brokers and municipal securities dealers other than bank dealers which

**Questions about these amendments may be directed to Diane G. Klinke, Deputy General Counsel or Harold L. Johnson, Assistant General Counsel.**

<sup>1</sup> SEC Release No. 34-25017.

<sup>2</sup> SEC Release No. 34-25002.

<sup>3</sup> SEC Release No. 34-25021.

\* Underlining indicates new language; strike-through indicates deletions.

are in compliance with rule 17a-3 of the Commission will be deemed to be in compliance with the requirements of this rule, provided that the information required by subparagraph (a)(iv)(D) of this rule as it relates to uncompleted transactions involving customers; paragraph (a)(viii); paragraph (a)(xi); and paragraph (a)(xii); and paragraph (a)(xiii), shall in any event be maintained.

(g) No change.

#### Rule G-12. Uniform Practice

(a) through (d) No change.

(e) *Delivery of Securities*. The following provisions shall, unless otherwise agreed by the parties, govern the delivery of securities:

(i) No change.

(ii) *Securities Delivered*.

(A) All securities delivered on a transaction shall be identical as to the information set forth in subparagraph (E) of paragraph (c)(v) and, to the extent applicable, the information set forth in subparagraphs (A) and ~~(E)~~ (E) of paragraph (c)(vi). All securities delivered shall also be identical as to the call provisions and the dated date of such securities.

(B) No change.

(iii) *Delivery Ticket*. A delivery ticket shall accompany the delivery of securities. Such ticket shall contain the information set forth in subparagraphs (A), (B), (D) (except in the case of transactions in zero coupon, compound interest and multiplier securities, in which case the maturity value shall be shown), (E) through (H), (M) and (N) of paragraph (c)(v) and, to the extent applicable, the information set forth in subparagraphs (A) through ~~(E)~~ (I) of paragraph (c)(vi) and shall have attached to it an extra copy of the ticket which may be used to acknowledge receipt of the securities.

(iv) through (xvi) No change.

(f) through (l) No change.

#### Rule G-15. Confirmation, Clearance and Settlement of Transactions with Customers

(a) through (b) No change.

(c) *Deliveries to Customers*. Except as provided in section (d) below, a delivery of securities by a broker, dealer, or municipal

securities dealer to a customer shall, unless otherwise agreed by the parties or otherwise specified by the customer, be made in accordance with the following provisions:

(i) *Securities Delivered*.

(A) All securities delivered on a transaction shall be identical as to the information set forth in subparagraph (E) of paragraph (a)(i) and, to the extent applicable, the information set forth in subparagraphs (A) and ~~(E)~~ (E) of paragraph (a)(iii). All securities delivered shall also be identical as to the call provisions and the dated date of such securities.

(B) No change.

(ii) *Delivery Ticket*. A delivery ticket shall accompany the delivery of the securities. Such ticket shall contain the information set forth in subparagraphs (A), (B), (D) (except in the case of transactions in zero coupon, compound interest and multiplier securities, in which case the maturity value shall be shown), (E) through (H), (L) and (N) of paragraph (a)(i) and, to the extent applicable, the information set forth in subparagraphs (A), ~~(B), (C), and~~ through (E) through and (G) through ~~(H)~~ (J) of paragraph (a)(iii).

(iii) through (xii) No change.

(d) through (e) No change.

#### Rule G-19. Suitability of Recommendations and Transactions; Discretionary Accounts

(a) through (c) No change.

(d) *Discretionary Accounts*. No broker, dealer or municipal securities dealer shall effect a transaction in municipal securities with or for a discretionary account

(i) except to the extent clearly permitted by the prior written authorization of the customer and accepted in writing by a municipal securities principal or municipal securities sales principal on behalf of the broker, dealer or municipal securities dealer; and

(ii) unless the broker, dealer or municipal securities dealer first determines that the transaction is suitable for the customer as set forth in paragraphs (c)(i) and (c)(ii)(A) of this rule or unless the transaction is specifically authorized by the customer.

(e) No change.

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