MSRB REPORTS

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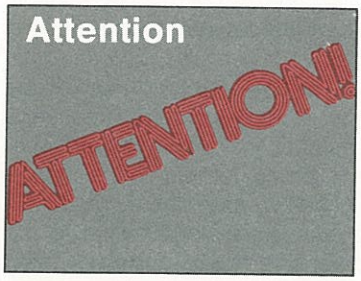

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Registration of Municipal Securities

Review of Rules G-8, G-12, G-15, and G-24

On July 1, 1983 certain provisions of the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") regarding the registration of new issues of municipal securities become effective. These provisions essentially require that most new issues of long-term municipal securities which are issued on or after that date must be issued solely in registered form.[1] Under the provisions of TEFRA, securities which are issued in bearer form in violation of this requirement would be subject to several penalties, including, among others, the loss of the tax exemption of the interest paid on the securities and the loss of eligibility for capital gains treatment of any gain derived from the sale or redemption of the securities.

Subsequent to the passage of TEFRA the Board undertook a review of those provision of its rules relating specifically to transactions in registered securities, to ensure that these requirements were appropriate in light of the municipal securities industry's transition to the generalized use of securities in registered form. As a result of this review the Board has adopted amendments to certain of its rules to facilitate the trading and clearance of registered registered securities. With respect to other provisions, the Board is satisfied that the existing rules will continue to be appropriate after the July 1, 1983 effective date of the registration requirement.

The Board believes that it would be helpful for the municipal securities industry to publish a summary of these rules at this time. Accordingly, set forth below is a review of the Board rules or pending amendments having specific application to transactions in registered securities.

The rules summarized below are those which make specific reference to registered municipal securities. Other rules which do not specifically refer to registered securities are, of course, equally applicable to transactions in such securities, unless it is clear that, by their terms, they do not apply.

Rule G-8. Recordkeeping

Board rule G-8 sets forth certain requirements concerning the records to be made and kept by municipal securities brokers and dealers regarding their municipal securities activities. Rule G-8(a)(i) requires, among other matters, that the records of original entry ("blotters") must indicate that a transaction involves registered securities, if this is the case. Rule G-8(a)(iv)(A) requires dealers to make a record of "municipal securities in transfer." Such record must set forth the description and the aggregate par value of the securities, the name in which registered, the name in which the securities are to be registered, the date sent out for transfer, the address to which sent for transfer, former certificate numbers, the date returned from transfer, and new certificate numbers.

Rule G-12. Uniform Practice

Board rule G-12 sets forth certain provisions regarding practices to be followed by municipal securities brokers and dealers in confirming, clearing, and settling inter-dealer transactions in municipal securities.

Confirmations (Rule G-12(c))

Rule G-12(c) (vi) requires that inter-dealer confirmations indicate if the securities involved in the transaction are fully registered or registered as to principal. The rule also requires that any unusual certificate denominations to be delivered on a transaction (*i.e.*, denominations other than those permitted under rule G-12(e)(v)) must be specified on the confirmation.

Questions or comments concerning these rules may be directed to Donald F. Donahue, Deputy Executive Director.

Denominations (Rule G-12(e)(v))

Rule G-12(e)(v) states that registered securities certificates are in "good delivery" form if they are in denominations of multiples of $1000 par value up to and including $100,000 par value; for example, if a dealer effects a transaction for $54,000 par value securities, such dealer may deliver a

[1]TEFRA exempts from the registration requirement securities which mature in one year or less from the date of issuance, securities which are "not of a type offered to the public," and certain securities which are sold to non-U.S. nationals and are payable outside the United States.

single certificate of $54,000 par value. Certificates in other denominations (*e.g.*, a single certificate representing $500,000 par value securities) may not be delivered unless this is agreed upon at the time of trade and specified on the inter-dealer confirmation.

Registered vs. Bearer Form (Rule G-12(e)(vi))

Rule G-12(e)(vi) states that

> [d]elivery of securities which are issuable in both bearer and registered form shall be in bearer form unless otherwise agreed by the parties.

Therefore, if secutities are available solely in registered form (as is the case with mortgage revenue securities issued after 1981 and will be the case for most municipal securities issued on or after July 1, 1983), a delivery of registered securities may not be rejected.

Delivery of Registered Securities: General Standards (Rule G-12(e)(xiv))

Rule G-12(e)(xiv) sets forth requirements governing the delivery of registered securities. Subparagraphs (A) and (B) of this provision set forth requirements relating to the completion of assignments and of separate "bond powers" attached to the securities, respectively, and subparagraph (C) requires the attachment of a release of a power of attorney, if necessary for delivery purposes. Subparagraph (D) of this provision specifies that

> [e]ach assignment, endorsement, alteration and erasure shall bear a guarantee acceptable to the transfer agent or registrar.

Delivery of Registered Securities: Form of Registration (Rule G-12(e)(xiv))

Currently pending amendments to subparagraphs (E) and (F) of rule G-12(e)(xiv)[2] will, when effective, require that, to be deliverable on an inter-dealer transaction without any specification at the time of trade, securities must be registered in the name of one of the following four types of persons:

- an individual or individuals;
- a nominee;
- an individual or individuals acting in a fiduciary capacity; or
- a municipal securities broker or municipal securities dealer whose signature is on file with the transfer agent (if the municipal securities broker or dealer is not a national exchange member firm, a statement attesting to the filing of the signatures must be placed on the assignment).

Securities with some other form of registration, on which documents in addition to the completed assignment (*e.g.*, corporate resolutions and a certificate of incumbency) are necessary for transfer purposes, would, under the amendments to subparagraph (F), be considered to be in "legal form," and would not be deliverable unless it was specified at the time of trade that securities in "legal form" would be delivered.

Delivery of Registered Securities: Interest Payments (Rule G-12(e)(xiv))

Subparagraphs (G) and (H) of rule G-12(e)(xiv) govern the payment of interest checks on deliveries of registered securities. Subparagraph (G) specifies that deliveries on transactions settling after the record date but prior to the interest payment date (or other deliveries on which the recipient will be unable to have the securities transferred prior to the record date) must be accompanied by a currently dated check for the amount of interest due. Subparagraph (H) imposes a similar standard in the case of deliveries of registered securities which are in default on interest payments.

Reclamation (Rule G-12(g))

Rule G-12(g)(iii)(A)(4) permits reclamation on an inter-dealer transaction for a period of one business day following the delivery date if registered securities are delivered on a transaction on which bearer securities are due. Since most municipal securities issued on or after July 1, 1983 will be available solely in registered form, this reclamation provision will not be applicable; this is currently the case with mortgage revenue securities issued after 1981.

A currently pending amendment to rule G-12(g)(iii)(C)(2)[3] will provide, when effective, that reclamation may be made for a period of eighteen months in the event of

> refusal to transfer or deregister by the transfer agent due to presentation of documentation in connection with the transfer or deregistration which the transfer agent deems inadequate.

Close-Out (Rule G-12(h))

Rule G-12(h) sets forth a procedure for the close-out of an uncompleted transaction by the purchasing dealer. This rule has recently been amended[4] to provide that, in the event that the securities involved in the transaction which is the subject of the close-out notice have been submitted for transfer, the time periods specified in the close-out notice are extended for a period of ten business days. This extension is available only with respect to the first close-out notice issued on a transaction, and only if the notice is not retransmitted. Further, the time extension provision is subject to a "sunset" date, and will not be available on any notice of close-out initiated on or after January 1, 1985.

Rule G-15. Customer Confirmations

Rule G-15(c) requires that customer confirmations indicate if the securities involved in the transaction are fully registered or registered as to principal. The rule also requires that, if registered securities certificates in denominations other than denominations which are multiples of $1000 par value up to and including $100,000 par value are to be delivered on the transaction, the denominations to be delivered must be specified on the confirmation.

[2]The amendments were filed on May 9, 1983; *see MSRB Reports*, v. 3, n. 3 (May 1983), pp. 7–9. The Board has requested that the effectiveness of the amendments be delayed for 60 days following the date of Commission approval.

[3]The amendments were filed on May 9, 1983; *see MSRB Reports*, v. 3, n. 3 (May 1983), pp. 7–9. The Board has requested that the effectiveness of the amendments be delayed for 60 days following the date of Commission approval.

[4]*See* June 7, 1983 Notice of Approval of Amendments to Close-Out Procedures.

Rule G-24. Use of Ownership Information

Among other matters, rule G-24 states that, if a municipal securities broker or dealer has access to confidential information regarding the ownership of municipal securities obtained from an issuer when acting in an agency or fiduciary capacity for the issuer, such broker or dealer is prohibited from using such information in the conduct of its municipal securities activities unless the issuer consents to such use. The Board notes that this provision would apply to information obtained by a person associated with a municipal securities broker or dealer who acts as the issuer's agent (*e.g.*, as bond registrar or transfer agent) with respect to an issue of registered securities.

June 27, 1983

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Notice of Approval

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Rule G-12

Amendments Approved on Close-Out Procedures

On June 6, 1983, the Securities and Exchange Commission approved certain amendments to the procedures set forth in rule G-12(h) for closing out uncompleted transactions between dealers. The amendments, which are described more fully below, (1) permit use of the close-out procedure on certain reclaimed transactions, (2) provide for an extension of close-out deadlines in certain circumstances where securities have been submitted for transfer, and (3) delete a requirement for the attachment of a contra-confirmation to a notice of close-out. The amendments were effective upon approval by the Commission. The text of the amendments follows this notice.

The provisions of the amendments are as follows:

- **The amendments permit the initiation of a close-out procedure on certain transactions reclaimed after the ninetieth business day following the original settlement date.** Prior to approval of the amendments, the provisions of rule G-12(h)(i)(E) specified that a close-out notice could not be issued on a transaction after the ninetieth business day following the settlement date. However, the provisions of rule G-12(g) permit reclamations to be made for up to eighteen months after delivery for certain specified reasons, and indefinitely for other specified reasons. Therefore, the previous rule did not permit a reclaiming dealer to use the close-out procedure to ensure completion of the reopened contract, if the reclamation occurred more than ninety business days after the settlement date.

The Board believes that the use of the close-out procedure would promote more expeditious resolution of transactions which have been reopened as a result of a reclamation. Accordingly, the amendments make the close-out procedure available, for a short period of time, in the event that a transaction is reopened due to a reclamation of securities, for certain specified reasons, after the ninetieth business day following the settlement date. The amendments permit the purchaser to initiate a close-out procedure with respect to such a transaction, in accordance with the provisions of the rule, for a period of fifteen business days following the date of reclamation. The amendments also provide that such a procedure would be an initial procedure for purposes of the timing provisions specified in subparagraph (h)(i)(A).

This provision of the amendments would apply, however, only if the delivery had been reclaimed pursuant to the provisions of subparagraphs (g)(iii)(C) or (g)(iii)(D) of rule G-12[1] If the reclamation has been made for some other reason (*e.g.*, securities with mutilated coupons, or missing the legal opinion, both grounds for reclamation under subparagraph (g)(iii)(A)), the provision of the amendments would not apply, and a close-out could not be initiated with respect to the reclaimed transaction after the ninetieth business day following the settlement date. Since the time periods for reclamations for other reasons are relatively brief, the Board does not believe that additional time for initiation of a close-out procedure is warranted.

- **The amendments permit the selling dealer receiving a close-out notice which it does not retransmit to obtain an extension of time if the securities owed on the transaction are in transfer.** Previously, the close-out rule had provided an extension of time only in the event that a close-out notice is retransmitted by the selling dealer first receiving it, and no extension had been provided based specifi-

Questions or comments concerning the amendments or the close-out rules generally may be directed to Donald F. Donahue, Deputy Executive Director.

[1]Subparagraph (g)(iii)(C) of rule G-12 currently provides that reclamation may be made within 18 months of a delivery for any of the following reasons:
(1) irregularity in delivery, including, but not limited to, delivery of the wrong issue (*i.e.*, issuer, coupon rate or maturity date), duplicate delivery, delivery to the wrong party or location, or over delivery;
(2) refusal to transfer or deregister by the transfer agent due to a lack of documentation required by paragraph (e)(xiv) of the rule; or
(3) information pertaining to the description of the securities was inaccurate for either of the following reasons:
(i) information required by subparagraph (c)(v)(E) of the rule was omitted or erroneously noted on a confirmation, or
(ii) information material to the transaction but not required by subparagraph (c)(v)(E) of the rule was erroneously noted on a confirmation.
Subparagraph (g)(iii)(D) provides that reclamation of a delivery may be made without any time limitation for either of the following reasons:
(1) the security delivered is reported missing, stolen, fraudulent or counterfeit; or
(2) a notice of call for less than the entire issue of securities was published on or prior to the delivery date and the securities were not identified as "called" at the time of trade.

cally on the reason for the selling dealer's failure to deliver. However, as a result of the passage of the registration requirement contained in the Tax Equity and Fiscal Responsibility Act of 1982,[2] and as a result of the Board's concern that undue delays in the transfer process may become a more significant factor in the municipal clearance process during the initial period following the effectiveness of that requirement, the Board has concluded that it would be appropriate to alter the close-out process to take into account this substantial change in the manner in which the industry will be clearing securities and to provide additional time to permit the transfer process to be accomplished.

Accordingly, the amendments provide that, if the selling dealer receiving an initial notice of close-out from the originating purchaser has submitted the securities which it is failing to deliver to be transferred, the selling dealer may delay the delivery deadline and the execution period specified on the notice for ten business days by advising the purchaser of the reason for its failure to deliver. The selling dealer must advise the purchaser of the reason for its failure to deliver by telephone not later than the close of business on the business day following its receipt of the telephone notice of close-out from the purchaser; the selling dealer must confirm this notice in writing, sent return receipt requested not later than the following business day, including in such notice a statement of the dates of the new delivery deadline and the new execution period, as extended by the seller's action.

This time extension, however, would be available only to the selling dealer first receiving the notice of close-out from the originating purchaser. If the notice of close-out is retransmitted to another dealer, and this third dealer is the party which has submitted the securities for transfer, the third dealer would not be able to invoke an additional time extension attributable to the fact that the securities are being transferred. The Board notes that the retransmittal of the close-out notice itself causes a five business day extension of the dates involved in the procedure, and the Board believes that providing an additional ten-day extension would unduly delay the close-out procedure and harm the purchaser's interests in accomplishing a timely completion of the contract.

The amendments also provide that this time extension for securities in transfer shall be available only on close-outs initiated prior to January 1, 1985. The Board is of the view that, as more efficient transfer mechanisms become available on a wider range of municipal issues, there will be less need for additional time on a close-out procedure. The Board believes that a "sunset" date of January 1, 1985 provides sufficient time for municipal market participants to develop and ensure the adoption of efficient transfer mechanisms on most municipal issues.

- **The amendments delete the requirement that a copy of the contra-dealer's confirmation be attached to close-out notices.** The previous rule had required that a dealer issuing or retransmitting a close-out notice must attach to such notice a copy of the contra-confirmation of the transaction sent by the dealer who is receiving the close-out notice. The Board has concluded that this requirement is no longer necessary. Since the relevant information regarding the transaction is required to be specified both in the telephone and the written close-out notice, and since a dealer receiving a telephone notice of close-out must proceed based on such telephone notice, not awaiting receipt of the written notice, the requirement to attach the contra-confirmation to the written notice does not appear to provide significant assistance in identifying the related transactions to the dealer receiving the notice. Accordingly, the amendments delete the requirement for attachment of a copy of the contra-confirmation.

June 7, 1983

Text of Amendment*

Rule G-12. Uniform Practice

(a) through (g) No change.

(h) Close-Out. Transactions which have been confirmed or otherwise agreed upon by both parties but which have not been completed may be closed out in accordance with this section, or as otherwise agreed by the parties.

(i) Close-Out by Purchaser. With respect to a transaction which has not been completed by the seller according to its terms and the requirements of this rule, the purchaser may close out the transaction in accordance with the following procedures:

(A) Notice of Close-Out. If the purchaser elects to close out a transaction in accordance with this paragraph (i), the purchaser shall, not earlier than the fifth business day following the settlement date, notify the seller by telephone of the purchaser's intention to close out the transaction. The purchaser shall state that unless the transaction is completed by a specified date and time, which shall not be earlier than the close of the tenth business day following the date the telephonic notice is given (the fifth business day, in the case of a second or subsequent notice), the transaction may be closed out in accordance with this section at any time during the period of time, which shall not be more than five business days, specified by the purchaser for such purpose. The purchaser shall immediately thereafter send, return receipt requested, a written notice of close-out to the seller. Such notice shall contain the information specified in item (1) of subparagraph (C) below. ~~and shall be accompanied by a copy of the seller's confirmation of the transaction to be closed out or other written evidence of the contract between the parties.~~

[2]The Tax Equity and Fiscal Responsibility Act, as subsequently amended, contained a provision essentially requiring that most new issues of municipal securities issued after June 30, 1983 must be made available solely in registered form. The Act exempts from the registration requirement securities which mature in one year or less from the date of issuance, securities which are "not of a type offered to the public," and certain securities which are sold to non-U.S. nationals and are payable outside the United States.

*Underlining indicates new language; broken line indicates deleted text.

(B) (1) Retransmittal. [as in current rule—no substantive change.]

(2) Transfer of Securities. If a selling dealer receiving an initial notice of close-out which has not been retransmitted has submitted the securities owed on the transaction to the registrar or transfer agent for transfer, the selling dealer may, upon notice to the purchaser, extend the dates for close-out by ten business days. The selling dealer must provide such notice by telephone, not later than the first business day following its receipt of the telephone notice of close-out, and must immediately thereafter send, return receipt requested, a written confirmation of such notice, stating the dates for close-out as extended due to such notice. The provisions of this item (2) of subparagraph (B) shall not apply to any notice of close-out initiated on or after January 1, 1985.

(C) and (D) No change.

(E) Close-Out Not Completed. If a close-out pursuant to a notice of close-out is not completed in accordance with the terms of the notice and the provisions of this rule, the notice shall expire. Additional close-out notices may be issued, provided that a close-out procedure with respect to a transaction may not be initiated later than the ninetieth business day following the settlement date of such transaction, regardless of the number of close-out notices issued. Notwithstanding the foregoing, in the case of a transaction on which a delivery of securities has been reclaimed pursuant to the provisions of subparagraphs (g)(iii)(C) or (g)(iii)(D) of this rule and which remains uncompleted, the purchaser may initiate one or more close-out procedures with respect to such transaction at any time during a period of fifteen business days following the date of reclamation. The first such procedure shall be considered an initial procedure for purposes of subparagraph (A) above.

(F) and (G) No change.

(i) through (l) No change.

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Rule G-11

Amendments Approved Which Provide Exemptions for Qualified Note Syndicates

On May 31, 1983, the Securities and Exchange Commission approved amendments to rule G-11 on syndicate practices. The amendments provide an exemption from certain of the rule's disclosure requirements, under specified circumstances, for members and managers of "qualified note syndicates." A "qualified note syndicate" is defined as a syndicate formed for the purpose of purchasing and distributing new issues of municipal securities that mature in less than two years. In addition, the new issue must be purchased on other than an "all or none" basis *or* the syndicate must have provided that there will be no order period, that only group orders will be accepted, and that the syndicate may purchase and sell the municipal securities for its own account.

The rule amendments exempt members and managers of qualified note syndicates from the provisions of rule G-11(d) and (g) which require respectively the disclosure of the identity of customers who place group orders and the disclosure of the identity of group orders to which securities have been allocated. The previous disclosure requirements were designed to afford syndicate members a means of policing order priorities established by the syndicate. The Board concluded that these requirements were unnecessary if all orders were treated as group orders since there would be no priority concerns to be protected.

The amendments also exempt managers of qualified note syndicates from the requirement in subsection (h)(ii) of the rule that a manager deliver, at or before final settlement, a summary statement showing the aggregate par values and prices of all securities sold from the account. The Board has adopted this exemption because, in larger offerings such as an issue of project notes, the allocation disclosures required by the rule would be many pages long and of little practical value to syndicate members.

As indicated, the proposed exemptions only apply to syndicates which are "qualified note syndicates" as defined. Only qualified note syndicates purchasing or distributing issues of municipal securities that mature in less than two years can avail themselves of the exemptions.

The text of the rule amendments follows. The amendments became effective upon Commission approval.

May 31, 1983

Text of Amendment*

Rule G-11. Sales of New Issue Municipal Securities During the Underwriting Period

(a) No change.

(i) through (ix) No change.

(x) the term "qualified note syndicate" means any syndicate formed for the purpose of purchasing and distributing a new issue of municipal securities that matures in less than two years where:

(A) the new issue is to be purchased by the syndicate on other than an "all or none" basis; or

(B) the syndicate has provided that:

(1) there is to be no order period;

(2) only group orders will be accepted; and

(3) the syndicate may purchase and sell the municipal securities for its own account.

(b) through (c) No change.

(d) Disclosure of Group Orders. Every municipal securities dealer that submits a group order to a syndicate or to a member of a syndicate, shall disclose at the time of submission of such order the identity of the person for whom the order is submitted. This section shall not apply to a qualified note syndicate as defined in paragraph (a)(x) above.

(e) through (f) No change.

(g) No change.

(i) No change.

(ii) the identity of each person submitting a group order to which securities have been allocated as well as the aggregate par value and maturity date of each maturity allocated except that this paragraph shall not apply to the senior syndicate manager of a qualified note syndicate as defined in paragraph (a)(x) above; and

(iii) No change.

(h) No change.

(i) No change.

(ii) a summary statement showing the aggregate par values and prices (expressed in terms of dollar prices or yields) of all securities sold from the syndicate account. This paragraph shall not apply to a qualified note syndicate as defined in paragraph (a)(x) above.

Questions regarding this notice may be addressed to Angela Desmond, Deputy General Counsel.

*Underlining indicates new language.

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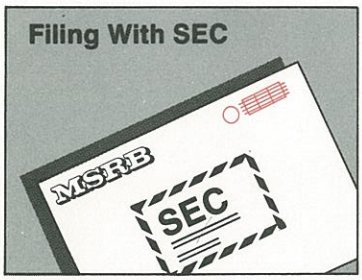

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Rule G-15

Amendment Filed on Yield Disclosure

The Board has filed with the Securities and Exchange Commission an amendment to Board rule G-15 concerning the disclosure on customer confirmations of information relating to yield.

Board rule G-15 requires disclosure on a customer confirmation of the yield and dollar price of a municipal securities transaction. In the case of a transaction effected on the basis of a yield price, the confirmation must state the yield and the resulting dollar price, computed to the lowest of price to premium call, par option or maturity. In the case of a transaction effected on the basis of a dollar price, the confirmation must state the dollar price and the resulting yield, computed to the lowest of yield to premium call, par option or maturity.

The rule presently requires confirmation disclosure of the details of a call or option feature where the dollar price of a transaction effected on a yield basis is computed to such call or option. However, there is no requirement to disclose the details of a call or option feature where the resulting yield of a transaction effected on a dollar basis is computed to such call or option. The recently-filed amendment will require such disclosure.

The Board has concluded that for transactions with customers, where the yield disclosed on the confirmation as that which, at minimum, can reasonably be expected to be realized has been calculated to a call or option feature, the confirmation should set forth the call or option date and price so that the customer knows the exact basis on which such yield would be realized. The Board also believes that the amendment will help to assure that the dealer and customer agree with respect to the determinants of the basis on which the customer will realize the stated yield.

The text of the amendment follows. The amendment will not become effective until approved by the Commission.

June 3, 1983

Text of Proposed Amendment*

Rule G-15. Customer Confirmations

(a) At or before the completion of a transaction in municipal securities with or for the account of a customer, each broker, dealer or municipal securities dealer shall give or send to the customer a written confirmation of the transaction containing the following information:

(i) through (viii) No change.

(ix) yield and dollar price as follows:

(A) for transactions effected on a yield basis, the yield at which transaction was effected and the resulting dollar price shall be shown. Such dollar price shall be calculated to the lowest of price to premium call, price to par option, or price to maturity. ~~In cases in which the dollar price is calculated to premium call or par option, this must be stated, and the call or option date and price used in the calculation must be shown.~~

(B) for transactions effected on the basis of dollar price, the dollar price at which transaction was effected, and the lowest of the resulting yield to premium call, yield to par option, or yield to maturity shall be shown; ~~provided, however, that yield information for transactions in callable securities effected at a dollar price in excess of par, other than transactions in securities which have been called or prerefunded, is not required to be shown until October 1, 1984.~~

(C) for transactions at par, the dollar price shall be shown.

In cases in which the resulting dollar price or yield shown on the confirmation is calculated to premium call or par option, this must be stated, and the call or option date and price used in the calculation must be shown;

(x) through (xiv) No change.

(b) through (i) No change.

Questions concerning the proposed amendments may be directed to Donald F. Donahue, Deputy Executive Director.

*Underlining indicates additions; broken line indicates deletions.

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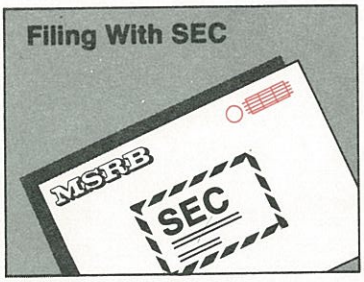

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Rules G-12 and G-15

Amendments Filed Requiring That Confirmations Disclose Interest Payment Basis if Other Than Semi-Annual

On June 3, 1983 the Board filed with the Securities and Exchange Commission certain amendments to Board rules G-12 and G-15. The text of the proposed amendments follows this notice. The proposed amendments will not become effective until they are approved by the Commission.

Board rules G-12 and G-15 set forth certain requirements concerning the information to be provided on inter-dealer and customer confirmations, respectively. Among other matters, confirmations are required to state any unusual aspects of the securities relating to the payment of principal or interest. The proposed amendments would require that, if the securities involved in a transaction are periodic-interest securities paying interest on other than a semi-annual basis (*e.g.*, annually or quarterly), the confirmation of the transaction must state the basis on which interest is paid.

Since the payment of interest on a periodic-interest security on a basis other than semi-annually is very unusual, the Board believes that purchasers of periodic-interest municipal securities, both municipal securities brokers and dealers and investors, should be advised of this exception on the confirmation of their transaction. The payment of interest on an alternative basis may be of concern to such purchasers, particularly investors, since this alternative payment basis may not accord with their cash flow needs or reinvestment plans,[1] or may have implications for their operational procedures (*e.g.*, if securities paying interest on a more frequent cycle are available only in registered form, they would have to be transferred quickly to prevent misdirection of the next interest payment).

June 10, 1983

Text of Proposed Amendments*

Rule G-12. Uniform Practice

(a) and (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) through (D) No change.

(E) any special instructions or qualifications, or factors affecting payment of principal or interest, such as (1) "ex legal," or (2) if the securities are traded without interest, "flat," or (3) if the securities are in default as to the payment of interest or principal, "in default," or (4) with respect to securities with periodic interest payments, if such securities pay interest on other than a semi-annual basis, a statement of the basis on which interest is paid; and

(F) No change.

(d) through (l) No change.

Rule G-15. Customer Confirmations

(a) and (b) No change.

(c) In addition to the information required by paragraphs (a) and (b) above, each confirmation to a customer shall contain the following information, if applicable:

(i) through (v) No change.

(vi) any special instructions or qualifications, or factors affecting payment of principal or interest, such as (A) "ex legal," or (B) if the securities are traded without interest, "flat," or (C) if the securities are in default as to the payment of interest or principal, "in default," or (D) with respect to securities with periodic interest payments, if such securities pay interest on other than a semi-annual basis, a statement of the basis on which interest is paid, and

(vii) No change.

(d) through (i) No change.

Questions concerning the proposed amendments may be directed to Donald F. Donahue, Deputy Executive Director.

[1]Many investors seek to maximize their total rate of return by reinvesting interest income when it is paid. A variance in the payment cycle, therefore, will substantially affect the investor's total rate of return on the investment, since there would be less (or more) frequent opportunity for reinvestment than the investor might anticipate.

*Underlining indicates additions. Certain material which is deleted by the proposed amendments has been omitted.

MSRB REPORTS
Volume 3, Number 4 July 1983

Route To:

- ☒ Manager, Muni. Dept.
- ☒ Underwriting
- ☐ Trading
- ☐ Sales
- ☐ Operations
- ☒ Compliance
- ☐ Training
- ☒ Other Corporate Finance

Rules G-1, G-3, and G-23

Application of Board Rules to Private Placements and Financial Advisory Services Rendered to Corporate Obligors on Industrial Development Bonds

In a recent letter to the Office of the Comptroller of the Currency, the staff of the Securities and Exchange Commission has taken the position that private placements of industrial development bonds ("IDBs") constitute transactions in municipal securities as defined in the Securities Exchange Act of 1934, as amended. The Municipal Securities Rulemaking Board has received a number of inquiries concerning this letter. The Board is publishing this notice for the purposes of: (1) reviewing the application of its rules to private placements of municipal securities and (2) expressing its views concerning whether certain Board rules apply to financial advisory services rendered by municipal securities dealers and brokers to corporate obligors on IDBs.

Private Placements of IDBs

The Board's rules apply, of course, to all transactions in municipal securities, including securities which are IDBs. The SEC letter dealt in particular with the activities of commercial banks. That letter pointed out that if a commercial bank has a registered municipal securities dealer department, under Board rule G-1, which defines the term "separately identifiable department or division of a bank," any private placement activities of the bank in securities which are IDBs must be conducted as a part of the registered dealer department. The Board urges all bank dealers which have registered as a separately identifiable department or division to review their organizations and assure that all departments or units which engage in the private placement of IDBs are designated on the bank's Form MSD registration and other applicable bank records as part of its separately identifiable department or division. The Board also notes that such activities must be under the supervision of a person designated by the bank's board of directors as responsible for these activities. In addition, under Board rule G-3 concerning professional qualifications, persons who are engaged in privately placing municipal securities must be qualified as municipal securities representatives and be supervised with respect to that activity by a qualified municipal securities principal.

Financial Advisory Services Rendered to Corporate Obligors on IDBs

Board rules G-1 and G-3 provide that rendering "financial advisory or consultant services for *issuers*" is an activity to which those rules are applicable (emphasis added). Similarly, Board rule G-23, on the activities of financial advisors, applies to brokers, dealers, and municipal securities dealers who agree to render "financial advisory or consultant services to or on behalf of an *issuer*" (emphasis added). Clearly these rules are applicable to financial advisory services rendered to state or local governments and their agencies, as well as to municipal corporations. In the Board's view, however, rules G-1, G-3, and G-23 do not apply to financial advisory services which are provided to corporate obligors in connection with proposed IDB financings.

The Board wishes to emphasize that the scope of its definition of financial advisory services is limited to "advice with respect to the structure, timing, terms, and other similar matters" concerning a proposed issue.* If persons providing such advice to the corporate obligor on an IDB issue also participate in negotiations with prospective purchasers or are otherwise engaged in effecting placement of the issue, then, as indicated above, rules G-1 and G-3 would apply to their activities.

Excerpts of the Commission letter follow.

May 23, 1983

Comments or questions relating to this notice may be directed to Richard B. Nesson, General Counsel.

*Rule G-23(b).

Securities and Exchange Commission
Washington, D.C. 20549

May 21, 1982

Owen Carney
Director
Investment Securities Division
Comptroller of the Currency
Washington, D.C. 20219

This is in response to your letter of December 1, 1981, requesting our views concerning certain activities by commercial banks in connection with industrial development bonds ("IDBs").[1] Specifically, you asked (1) whether the private placement activities of banks in IDBs involve transactions in municipal securities, (2) whether involvement in such activities alone would require such banks to register with the Commission under Section 15B of the Securities Exchange Act of 1934 (the "Exchange Act") as municipal securities dealers, (3) whether a bank that had registered a separately identifiable department or division with the Commission as a municipal securities dealer would be required to conduct such activities through such separately identifiable department or division, and (4) if such bank activities are required to be conducted in the separately identifiable department or division, whether the advisory services provided by those banks to the corporate obligor on an IDB should be regarded as advisory services provided to an issuer of municipal securities in connection with the issuance of municipal securities. Pursuant to your letter and subsequent telephone conversations, we understand the following facts to be typical of the activities in question.

A commercial bank offers private placement and financial advisory services to corporate entities on a regular and continuous basis. From time to time the bank recommends to the corporate entity that IDBs be used to raise capital. The bank advises the corporate entity regarding the terms and timing of the proposed IDB issuance, prepares the Direct Placement Memorandum describing the terms of the IDB, and contacts potential purchasers of the IDB. Such purchasers then make independent reviews of the corporate entity's financial status. The bank then obtains comments from the potential buyers and relays such comments to the corporate entity. The bank might also assist the corporate entity in subsequent negotiations with the purchasers. An industrial development authority nominally issues the IDB on behalf of the corporate entity which becomes the economic obligor on the issue.

The bank engages in these activities in order to assist the corporate obligor in the sale of the IDBs. In return for its services, the bank receives from the corporate entity either a fixed fee or a percentage of the proceeds of the sale. The bank does not purchase any of the IDBs. The bank could, however, supply "bridge loans" to the corporate entity pending receipt of the proceeds of the IDB sale. In addition, the bank might provide investors with a letter of credit committing the bank to pay any interest or principal not paid by the corporate issuer. The bank might also act as trustee or paying agent for the nominal issuer of the IDB, for which the bank would receive a set fee.

IDBs as Municipal Securities

Section 3(a)(10) of the Exchange Act defines a "security" as, among other things, "any note, . . . bond, debenture, . . . investment contract, . . . or in general, any instrument commonly known as a 'security' . . . ." Section 3(a)(29) of the Exchange Act defines "municipal securities" to include any security which is an industrial development bond as defined in Section 103(b)(2) of the Code the interest on which is tax-exempt under Sections 103(b)(4) or 103(b)(6) of the Code. In our opinion, the private placement activities you have described involve transactions in municipal securities as defined in the Exchange Act.[2]

Registration as Municipal Securities Dealer

Section 15B(a) of the Exchange Act makes it unlawful for any municipal securities dealer to use the mails or any instrumentality of interstate commerce to "effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security unless such municipal securities dealer is registered" with the Commission. Section 3(a)(30) of the Exchange Act defines "municipal securities dealer" to include a bank or a separately identifiable department or division of a bank if that bank is engaged in the business of buying and selling municipal securities for its own account other than in a fiduciary capacity, through a broker or otherwise. Banks that engage solely in private placement activities in IDBs as described by you would not be required to register as municipal securities dealers since they do not appear to be engaged in the business of buying and selling municipal securities for their own accounts, but rather appear to be acting as brokers. Section 3(a)(4) of the Exchange Act defines the term broker as "any person engaged in the business of effecting transactions in securities for the account of others, but does not include a bank." Since they are excluded from the definition of broker, banks that act solely as brokers need not register under the Exchange Act.[3]

Inclusion in Separately Identifiable Department or Division

Section 15B(b)(2)(H) of the Exchange Act authorizes the Municipal Securities Rulemaking Board (the "MSRB") to make rules defining the term "separately identifiable department or division" ("SID") of a bank as used in Section 3(a)(30) of the Exchange Act. MSRB rule G-1 defines the SID as "that unit of the bank which conducts all the activities of the bank relating to the conduct of business as a municipal securities

[1]You have represented that the IDBs involved would be primarily those defined in Section 103(b)(2) of the Internal Revenue Code of 1954 (the "Code"), the interest on which is tax-exempt under Sections 103(b)(4) and 103(b)(6) of the Code.

[2]This determination is based on an analysis of the specific facts as described by you. Different facts and circumstances could result in a transaction involving municipal debt instruments being treated as loan participations not subject to the federal securities laws. Such determinations can only be made on a case by case basis after a thorough examination of the context of the transaction.

[3]See letter dated February 17, 1977, from Anne E. Chafer, Attorney, Securities and Exchange Commission, to Bruce F. Golden and letter dated January 11, 1982, from Thomas G. Lovett, Attorney, Securities and Exchange Commission, to Harriet E. Munratt regarding Citytrust of Bridgeport, Connecticut.

dealer. . . ." The rule defines municipal securities dealer activities to include "sales of municipal securities" and "financial advisory and consultant services for issuers in connection with the issuance of municipal securities." Therefore, those banks that have registered an SID with the Commission also must conduct the private placement activities within the SID in accordance with MSRB rules. . . .

Based upon the facts and representations set forth in your letter, it would appear that the private placement activities of banks involving IDBs, as described in your example, constitute transactions in municipal securities that, if done alone, would not require a bank to register with the Commission as a municipal securities dealer. However, such activities, when conducted by a bank municipal securities dealer that had registered a separately identifiable department or division, would be treated as municipal securities dealer activities and, therefore, would be required to be conducted in the bank's dealer department. . . .

Susan J. Walters
Attorney
Office of Chief Counsel