Financial Statements and Report of
Independent Certified Public Accountants

Municipal Securities Rulemaking Board

September 30, 2006 and 2005

Municipal Securities Rulemaking Board

Contents

Report of Independent Certified Public Accountants

Audit Committee
Municipal Securities Rulemaking Board

We have audited the accompanying statements of financial position of the Municipal Securities Rulemaking Board (the Board), as of September 30, 2006 and 2005, and the related statements of activities and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America as established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Board's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used, and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Municipal Securities Rulemaking Board as of September 30, 2006 and 2005, and its changes in net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton LLP

McLean, Virginia
November 17, 2006

Tysons Executive Plaza II
2010 Corporate Ridge, Suite 400
McLean, VA 22102-7838
T 703.847.7500
F 703.848.9580
W www.grantthornton.com

Grant Thornton LLP
US member of Grant Thornton International

Municipal Securities Rulemaking Board

Statements of Financial Position

September 30,		2006		2005
Assets				
Cash	$	1,113,757	$	1,048,614
Accounts receivable, including unbilled receivables of $480,814 and $469,434, respectively		2,291,394		2,718,134
Other receivables		750,515		—
Accrued interest receivable		176,758		100,557
Other assets		99,373		120,150
Investments		17,606,032		15,786,227
Fixed assets, net		3,528,218		4,705,481
Total Assets	$	25,566,047	$	24,479,163
Liabilities and Net Assets				
Accounts payable and accrued liabilities	$	642,913	$	394,609
Accrued vacation payable		293,300		286,152
Capital lease obligations		3,894		8,865
Deferred rent		1,902,625		1,765,201
Deferred compensation		1,135,562		571,165
Total Liabilities		3,978,294		3,025,992
Net Assets–Unrestricted		21,587,753		21,453,171
Total Liabilities and Net Assets	$	25,566,047	$	24,479,163

The accompanying notes are an integral part of these statements.

Municipal Securities Rulemaking Board

Statements of Activities and Changes in Net Assets

Year ended September 30,	2006	2005
Revenue		
Underwriting assessment fees	$ 9,852,226	$ 11,149,597
Transaction fees	6,198,630	5,611,792
Annual fees	684,800	712,300
Data subscriber fees	406,295	466,000
Initial fees	9,600	8,800
Other income	2,062	1,523
Investment return	601,322	210,043
Board manuals	14,005	21,386
Total Revenue	17,768,940	18,181,441
Expenses		
MSIL and RTRS operations	7,240,392	7,216,980
Administration and operations	4,619,281	4,514,109
Rulemaking and policy development	3,605,787	3,613,446
Board and committee	1,283,029	1,134,080
Professional qualifications	736,268	731,878
Education and communications	149,601	212,660
Total Expenses	17,634,358	17,423,153
Change in Net Assets	134,582	758,288
Net Assets, beginning of year	21,453,171	20,694,883
Net Assets, end of year	$ 21,587,753	$ 21,453,171

The accompanying notes are an integral part of these statements.

Municipal Securities Rulemaking Board

Statements of Cash Flows

Year ended September 30,	2006	2005
Cash Flows from Operating Activities		
Change in net assets	$ 134,582	$ 758,288
Adjustments to reconcile change in net assets to net cash from operating activities:		
Depreciation and amortization	1,310,106	1,271,696
Gain on disposal of fixed assets	(1,129)	—
Net amortization of investment (discounts) premiums	(32,316)	101,088
Unrealized (gains) losses on investments	(61,417)	101,378
Changes in assets and liabilities:		
Accounts receivable	426,740	(404,758)
Other receivable	(750,515)	—
Accrued interest receivable	(76,201)	(229)
Other assets	20,777	(26,665)
Accounts payable	248,304	40,709
Accrued vacation payable	7,148	40,794
Deferred rent	137,424	207,024
Deferred compensation	564,397	571,165
Net Cash Provided by Operating Activities	1,927,900	2,660,490
Cash Flows from Investing Activities		
Purchases of fixed assets	(132,843)	(798,045)
Proceeds from the sale of fixed assets	1,129	—
Purchases of investments	(11,076,072)	(7,499,416)
Maturities of investments	9,350,000	5,700,000
Net Cash Used in Investing Activities	(1,857,786)	(2,597,461)
Cash Flows from Financing Activities		
Payments on capital lease obligations	(4,971)	(4,729)
Net Increase in Cash	65,143	58,300
Cash, beginning of year	1,048,614	990,314
Cash, end of year	$ 1,113,757	$ 1,048,614
Supplemental Information		
Interest paid	$ 308	$ 550

The accompanying notes are an integral part of these statements.

NOTE A—NATURE OF OPERATIONS

The Municipal Securities Rulemaking Board (the Board) was established in 1975 pursuant to authority granted by the Securities Exchange Act of 1934, as amended by the Securities Acts Amendments of 1975, as an independent, self-regulatory organization charged with rulemaking responsibility for the municipal securities industry. Effective May 17, 1989, the Board became incorporated as a tax-exempt, non-stock corporation in the Commonwealth of Virginia.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets, as well as liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Investments

Investments are stated at fair value as determined by quoted market prices. Investments consist entirely of U.S. Treasury Notes. The U.S. Treasury Notes have various maturity dates through December 2008.

Investment return consists of interest income of $539,905 and $311,421 and unrealized gains (losses) of $61,417 and $(101,378) for the years ended September 30, 2006 and 2005, respectively. Amortization and accretion of investment premiums and discounts are recorded as a component of unrealized gains and losses.

Other receivables in the accompanying September 30, 2006 balance sheet includes $750,000 due from broker relating to fiscal 2006 investment transactions settled in October 2006.

Fixed Assets

Furniture and fixtures, as well as office equipment, are recorded at cost and are depreciated using the straight-line method over five years and three years, respectively. Leasehold improvements are amortized using the straight-line method over the shorter of the remaining lease period or the estimated useful life of the improvement. Internal-use computer software is recorded at cost and amortized over its estimated useful life.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Capitalized Software Costs

The Board capitalizes certain costs associated with computer software developed or obtained for internal use in accordance with the provisions of Statement of Position No. 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*. The Board's policy provides for the capitalization of external direct costs of materials and services, and directly related payroll related costs. Costs associated with preliminary project stage activities, training, maintenance, and post implementation stage activities are expensed as incurred. Costs capitalized are amortized over a three- to five-year period on a straight line basis.

Underwriting Assessment Fees

On March 10, 1992, the Board filed with the Securities and Exchange Commission (SEC) an amendment to Rule A-13 on assessments relating to the underwriting of municipal securities offerings. The amendment relates to the Board's method of assessment, the scope of offerings which are assessed, and assessment rates.

The underwriting assessment fee is equal to a percentage of the face amount of all municipal securities, which are purchased from an issuer as part of a new issue. The fee charged is .001 percent or .003 percent of the par value of the offerings, as specified in Board Rule A-13. As described in this rule, certain transactions are exempt from underwriting fees.

Revenue from underwriting assessment fees is recognized when the underwriter files the offering statement with the Board.

Annual Fees

With respect to each fiscal year of the Board in which a municipal securities broker or dealer conducts business, the broker or dealer is required to pay an annual fee of $300. Revenue is recognized when brokers or dealers are billed annually.

Initial Fees

The initial fee is a one-time fee of $100, which is to be paid by every municipal securities broker or dealer registered with the SEC. Initial fees revenue is recognized when received.

Data Subscriber Fees

Municipal Securities Information Library (MSIL) collects, stores, and provides access to information necessary for the municipal securities market. MSIL operates three computer-based information systems: an electronic-document system for the collection, storage, and dissemination of official statements and advance-refunding documents (the OS/ARD system); a broadcast system for collection and dissemination of material events and notices from municipal securities issuers (the CDI system); and, the collection, processing, and dissemination of all municipal securities transactions for purposes of price transparency and surveillance (the RTRS system). Information in these systems is sold to subscribers on a subscription basis with quarterly billing in arrears. In addition, MSIL maintains files for public access of all Forms G-37, G-38, and other documents. Copying fees are levied at time of use for the reproduction of any documents.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Transaction Fees

On May 10, 1996, the SEC approved an amendment to Board Rule A-13 to implement a new transaction fee on each inter-dealer sales transaction in municipal securities. The fee, one-half cent per $1,000 par value of bonds, is levied on the sellers on inter-dealer transactions.

On April 10, 2000, Board Rule A-13 was expanded to include a fee assessment on the customer sales transaction activities of municipal securities dealers. The customer sales transaction fee was also set at one-half cent per $1,000 par value of bonds. In addition, exemptions from the transaction fees were provided for transactions effected in certain classes of bonds.

Transaction fee revenue is recognized as sales transactions are settled. Unbilled receivables consist of September transaction fees revenue billed in October.

Concentration of Credit Risk

Financial instruments which potentially subject the Board to a concentration of credit risk consist principally of cash and accounts receivable. Cash balances at times are in excess of federally insured amounts and, as a result, subject the Board to a degree of credit risk. The Board's policy is to limit credit risk by depositing its funds with high quality financial institutions. Accounts receivable consist of fees due from municipal securities brokers and dealers. At times, there are certain significant balances due from individual municipal securities brokers and dealers.

NOTE C—FIXED ASSETS

Fixed assets consist of the following as of September 30:

	2006	2005
Leasehold improvements	$ 1,251,524	$ 1,227,238
Office equipment	1,406,511	1,763,066
Furniture and fixtures	1,396,339	1,395,225
Capitalized software costs	5,042,920	5,042,920
	9,097,294	9,428,449
Less: accumulated depreciation and amortization	(5,569,076)	(4,722,968)
	$ 3,528,218	$ 4,705,481

NOTE C—FIXED ASSETS—Continued

Office equipment includes assets acquired under capital leases of approximately $19,000 and $67,000 at September 30, 2006 and 2005, respectively. The related accumulated depreciation for assets acquired under capital leases totaled approximately $19,000 and $63,000 at September 30, 2006 and 2005, respectively.

In January 2005, the Board implemented its Real-Time Transaction Reporting System (RTRS), which is used to collect, process, and disseminate municipal securities pricing information on a real-time basis. The Board capitalized an additional $588,000 in software cost during 2005 for the system to be functional.

NOTE D—COMMITMENTS

Operating and Capital Leases

The Board leases office space and certain office equipment under operating and capital leases. In May 2001, the Board moved its headquarters from Washington, D.C. to new office space in Alexandria, Virginia, and entered into a lease which will expire in fiscal year 2016. The operating lease agreement for this office space contains provisions for future rent increases. The total amount of rental payments due over the lease term is being charged to rent expense on the straight-line method over the term of the lease. The difference between rent expense recorded and the amount paid is credited or charged to deferred rent which is included in the liabilities in the accompanying statements of financial position. The Board also leases office space in Manassas, Virginia for operations as provided in its emergency readiness plan. This lease expires in April 2008.

Office equipment under capital lease obligations consists of a photocopier.

Future minimum lease payments under non-cancelable capital and operating leases are as follows:

Year ending September 30,	Capital Leases	Operating Leases
2007	$ 3,960	1,614,668
2008	—	1,618,953
2009	—	1,595,200
2010	—	1,621,546
2011	—	1,689,604
Thereafter	—	8,464,956
Total minimum lease payments	3960	$ 16,604,927
Less: amount representing interest	(66)	
Capital lease obligation at September 30, 2006	$ 3,894	

NOTE D—COMMITMENTS—Continued

Operating and Capital Leases—Continued

Total rent expense for office space and equipment for the years ended September 30, 2006 and 2005, was $2,211,772 and $2,220,794, respectively.

Employment Agreement

As of September 30, 2005, the Board had an employment agreement with its Executive Director, based in major part on the employment agreement first agreed to by the parties on October 1, 1992, which provided, *inter alia*, for a specific term, salary, general employee benefits, and certain other benefits, including a supplemental retirement plan, life insurance, and others. A Supplemental Executive Retirement Plan (SERP), which was created in 1989, and has been part of the employment agreement since 1992, provides a benefit equal to 50 percent of the Executive Director's base pay, reduced by retirement contributions already provided by the Board under the existing retirement and supplemental plans, and estimated Social Security. Vesting would have occurred if the Executive Director's employment had terminated at or after age 60 and in certain other limited circumstances.

On May 12, 2005, a new contract was entered into by the parties with a term ending on September 30, 2007. Incorporated into the new contract, the SERP benefit, which the parties agreed to fix at $1,561,394, is payable at the end of term of the new contract subject to the terms thereof. As of September 30, 2006, the Board accrued approximately $1,041,000 for the SERP benefit. In addition, according to the new contract, the Executive Director is to receive additional deferred compensation (457(f) contribution). The Board has established a Rabbi Trust for this purpose and has made contributions of $50,700 per annum for the three-year contract term. The aggregate amount held in the Rabbi Trust, including earnings or losses, will be payable at the end of term of the new contract, at the same time the SERP payment is payable, subject to the terms of the contract. As of September 30, 2006, the Board accrued $94,633, to which is deposited into the Rabbi Trust.

In August 2006, the Board informed the Executive Director of its intention not to renew his employment agreement ending September 30, 2007.

NOTE E—RETIREMENT PLAN

The Board has a defined contribution pension plan for all employees. Participation commences upon completion of one month of eligible service as described in the plan document. For all active participants employed on the first day of the calendar quarter, the Board makes a quarterly contribution as required by the plan document. These contributions are based on the participants' quarterly compensation for the calendar quarter immediately proceeding the first day of the calendar quarter. The contribution percentage ranges from 9 percent to 12 percent depending on the length of vested service as scheduled in the plan document. Each employee is fully vested upon being credited with five plan years of service. Employees may also make voluntary contributions to the plan. The Board made contributions to the plan totaling $562,980 and $491,819 for the years ended September 30, 2006 and 2005, respectively.

NOTE E—RETIREMENT PLAN—Continued

All administrative expenses of the plan are paid by the Board. Administrative expenses totaled $13,149 and $13,386 for the years ended September 30, 2006 and 2005, respectively.

In addition, the Board has entered into separate agreements with two employees to provide supplemental benefits in excess of Internal Revenue Service limitations. Payments made by the Board in accordance with these agreements totaled $83,625 and $78,276 for the years September 30, 2006 and 2005, respectively.

NOTE F—INCOME TAXES

The Board is exempt from taxes on income other than unrelated business income under Section 501(c)(6) of the Internal Revenue Code, and applicable income tax regulations of the Commonwealth of Virginia. No provision for income taxes has been made as of September 30, 2006 and 2005, since the Board believes that there is no unrelated business income.