

# MSRB REPORTS

Volume 6, Number 1

Municipal Securities Rulemaking Board

January 1986

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The amendment would require dealers to disclose on inter-dealer confirmations the amount of concession on transactions in zero coupon, compound interest and multiplier securities as a percentage of the bond's price.

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**Amendment Filed: Rule G-34**

The amendment would require managing underwriters to communicate CUSIP numbers and the initial trade date for new issues to syndicate and selling group members on the initial trade date.

## Recommendations Requested for Board Nominations

The process has begun for selecting five new board members to serve three year terms beginning October 1, 1986. One securities firm, two bank dealers and two public representatives must be elected. Members of the industry and the general public are asked to participate in this process. Information on how to make a recommendation, the names of those currently serving on the Board and the form for submitting a recommendation are published in this issue.

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**Route To:**

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

## EXAMINATIONS

### Application Fee Increased

The NASD has informed the Board that, effective October 1, 1985, the fee charged for administration of qualification examinations was increased from \$40.00 to \$50.00. This \$50.00 fee must accompany all applications submitted to the NASD requesting an administration of a qualification examination. This includes the Board's qualification examinations, which are:

- Series 52 (Municipal Securities Representative)
- Series 8 (General Securities Sales Supervisor)<sup>1</sup>
- Series 53 (Municipal Securities Principal)
- Series 54 (MSRB Financial and Operations Principal)

For further information please refer to Chapter Six on "Qualification Examination Procedures" in the MSRB *Professional Qualification Handbook*. This Handbook is available from the Board upon request.

**December 23, 1985**

**Questions concerning professional qualifications and examinations should be directed to Peter H. Murray, Assistant Executive Director.**

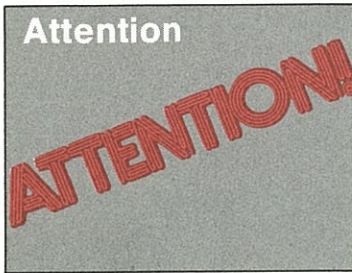
**Important Announcement**

**National Securities Clearing Corporation is scheduled to begin comparing when-issued transactions on February 28, 1986; contact NSCC for further information.**

### Calendar

- November 14**—Effective date of amendments to G-12 and G-15 on interest payment claims
- December 19**—Effective date of amendment to Rule G-34 on timely assignment of CUSIP numbers for new issues
- January 1**—Effective date of amendment to Rule G-12 on settlement dates for WALL securities
- February 28**—WALL trades eligible for NSCC comparison
- March 21**—Recommendations due for Board Nominations
- March 28**—Comments due on G-12 and G-15 draft amendments on automated clearance
- Pending**
  - G-26 on customer account transfers
  - G-34 on dissemination of CUSIP numbers and initial trade dates by managing underwriters
  - G-12 on inter-dealer concession disclosures for zero coupon, compound interest and multiplier securities
  - G-35 on arbitration

<sup>1</sup>The General Securities Sales Supervisor Qualification Examination (Test Series 8) qualifies an individual for the Board's purposes as a municipal securities sales principal.



**Route To:**

- Manager, Muni. Dept.**
- Underwriting**
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- Training**
- Other \_\_\_\_\_**

# Recommendations Requested for Board Nominations

The 1986 Nominating Committee requests recommendations of persons to be considered for the five Board positions opening on October 1, 1986.

## Membership Requirements

When making recommendations, keep in mind these Board membership requirements:

- Two public representatives, two bank dealer representatives and one securities firm representative must be elected this year to ensure equal representation in each membership category.
- Municipal securities brokers and municipal securities dealers of diverse size and type must be represented.
- Wide geographic representation must be maintained.

The Board, established by Congress in 1975 to act as the primary rulemaking body for the municipal securities industry, consists of 15 members—five representatives of bank dealers, five representatives of securities firms and five public members. One public member must be a representative of issuers and one of investors. Public members may not be associated with a securities firm or bank dealer other than by reason of being under common control with, or directly controlling, any broker or dealer which is not a municipal securities broker or municipal securities dealer.

## Procedure for Recommending Candidates

1. Complete the form printed on page 5 or a photocopy of that form. (Additional forms may be obtained from the Board offices.) The following information must be included on the form:

- The name, business affiliation, business address and telephone number, home address and telephone number and category (bank representative, securities firm representative or public representative) of the individual recommended. (Item 1.)
- The educational and professional background of the individual recommended. (Item 2.)
- The proposer's name, business address, telephone number and professional relationship (if any) to the individual recommended. (Item 3.)
- The affiliation (if any) of the individual with any broker, dealer or municipal securities dealer. (Item 4.)

2. Determine in advance that the individual recommended is willing to serve on the Board.

3. Submit recommendations no later than **March 21, 1986** to:

Stephen C. Stone  
Chairman, Nominating Committee  
Municipal Securities Rulemaking Board  
Suite 800  
1818 N Street, N.W.  
Washington, DC 20036-2491

# Terms of Present Board Members

## Terms Expire September 30, 1986

**Robert N. Downey**, Partner  
Goldman, Sachs & Co.  
New York, New York

**Peter J.D. Gordon**, Vice President  
T. Rowe Price Associates, Inc.  
Baltimore, Maryland

**Ralph Horn**, Executive Vice President  
First Tennessee Bank, N.A. Memphis  
Memphis, Tennessee

**Stephen C. Stone**, Senior Vice President and Manager  
Cullen/Frost Bank  
Dallas, Texas

## Terms Expire September 30, 1987

**H. Keith Brunner, Jr.**, President  
First Charlotte Corp.  
Charlotte, North Carolina

**Leonard M. Leiman**, Partner  
Reavis & McGrath  
New York, New York

**Walter P. Stern**, Vice Chairman  
Capital Research Co.  
New York, New York

**Samuel A. Ramirez**, President  
Samuel A. Ramirez & Co., Inc.  
New York, New York

**Byron G. Thompson**, Chairman of the Board  
Country Club Bank  
Kansas City, Missouri

## Terms Expire September 30, 1988

**W.J. Turner L. Cobden**, Senior Vice President  
Smith Barney, Harris Upham & Co., Inc.  
New York, New York

**Terrence E. Comerford**, Managing Director  
PaineWebber Inc.  
San Francisco, California

**James B.G. Hearty**, Vice President  
Bank of Boston  
Boston, Massachusetts

**Gerald Timothy Lane**, Executive Vice President  
Barnett Bank of Florida, Inc.  
Jacksonville, Florida

**Thomas H. Locker**, Comptroller  
Orange County  
Orlando, Florida

# Recommendation Form

1. Individual Recommended: \_\_\_\_\_

Business Address: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Home Address: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Telephone Number: \_\_\_\_\_

Telephone Number: \_\_\_\_\_

- Category: Bank representative .....   
Securities firm representative .....   
Public member .....

2. Educational and Professional Bankground

Professional: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Education: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Associations: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

3. Proposer: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

4. Associated Person under Securities Exchange Act of 1934: \_\_\_\_\_  
\_\_\_\_\_



**Route To:**

- Manager, Muni. Dept.
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**Automated Clearance and Settlement: Rules G-12 and G-15**

**Comments Requested**

The Board is considering rule changes which would—

- allow parties to agree to settle inter-dealer transactions eligible for book-entry by physical delivery, and
- require the use of automated systems for confirmation/affirmation and book-entry delivery of customer transactions if requested or agreed to by the customer.

The Board is circulating for comment draft amendments to rule G-12(f)(ii) concerning book-entry settlement of inter-dealer transactions and rule G-15(d) concerning use of automated confirmation/affirmation and book-entry settlement systems for customer transactions. All interested parties are invited to submit comments on the draft amendments by March 28, 1986.

**Background**

In July 1983, the Board adopted amendments to rules G-12 and G-15 which require certain municipal securities transactions to be cleared and settled through the automated facilities of clearing agencies and depositories registered with the Securities and Exchange Commission.<sup>1</sup> At the time the Board adopted these amendments, it stated its belief, based in part on the comments received from industry and other municipal securities market participants, that use of automated clearance and settlement systems would provide substantial benefits to the municipal securities industry in increased efficiency and cost savings in the clearance and settlement of municipal securities transactions.

Since the effective dates of these amendments, the Board has monitored the implementation of its automated clearance and settlement rules through contact with industry participants, and at meetings with representatives of clearing agencies, depositories and enforcement agencies. The Board believes that the industry has made substantial progress in making the transition from physical clearance and settlement procedures to using automated systems. Many industry

members continue to express support for the use of the automated systems stating that, as they become better acquainted with the systems, they are realizing substantial efficiencies and cost savings. The Board notes, however, that the current systems available for automated clearance and settlement do not fully accommodate transactions in all eligible municipal securities (*i.e.*, those having CUSIP numbers). Moreover, it appears that some industry participants have not completed certain in-house modifications necessary to use the systems to their full advantage. As a result, the full benefits that should flow from the use of automated clearance and settlement systems are not yet being enjoyed by all municipal securities industry members.<sup>2</sup>

The Board remains firmly committed to the implementation of automated clearance and settlement systems for processing municipal securities transactions. After reviewing the status of its automated clearance rules, however, the Board has concluded that it may be appropriate to define certain priorities to facilitate their implementation, rather than to require the industry and others to expend resources on several areas of automated clearance and settlement simultaneously. It appears that certain difficulties and costs associated with the transition to automated clearance and settlement could be minimized if efforts are concentrated at this time on furthering the development and use of the automated comparison system for inter-dealer transactions. Once the automated comparison system is working efficiently and can accommodate all inter-dealer transactions in eligible municipal securities, efforts could be concentrated on facilitating book-entry deliveries for inter-dealer transactions. Finally, after the automated clearance and settlement rules for inter-dealer transactions are implemented satisfactorily, the Board intends to direct its and the industry's efforts to expanding the use of automated systems for clearance and

**Comments on the matters discussed in this notice should be submitted not later than March 28, 1986, and may be directed to Angela Desmond, General Counsel or Harold L. Johnson, Assistant General Counsel. Written comments will be available for public inspection.**

<sup>1</sup>The amendments were approved by the Securities and Exchange Commission on November 14, 1983. See *MSRB Reports* Vol. 3, No. 7 (December 1983). The rules requiring use of automated facilities for comparison of inter-dealer transactions and confirmation/affirmation of customer transactions became effective on August 1, 1984; the rules requiring settlement of inter-dealer and customer transactions by book-entry delivery were effective on February 1, 1985.

<sup>2</sup>The Board is aware that other impediments to the efficient clearance and settlement of municipal securities transactions exist in the transfer of registered securities, use of intermediaries which are not subject to clearance and settlement requirements, and the interfaces between depositories.

settlement of customer transactions. The draft amendments set forth below reflect these priorities. The Board will continue to monitor the operation of the automated clearance and settlement systems and, if the draft amendments are adopted, will propose further rule changes at appropriate times in the future to complete the transition of the industry to automated clearance and settlement.

**Summary of Current Automated Clearance Rules**

**Automated Comparison of Inter-Dealer Transactions:  
Rule G-12(f)(i)**

Rule G-12(f)(i) requires that an inter-dealer municipal securities transaction be compared in the automated comparison system if the following conditions apply:

- (1) each party to the transaction is a member of a registered securities clearing agency offering comparison services, or its clearing agent for the transaction is a member;<sup>3</sup> and
- (2) the transaction is eligible for automated comparison.

**Book-Entry Settlement of Inter-Dealer Transactions:  
Rule G-12(f)(ii)**

Rule G-12(f)(ii) currently requires an inter-dealer transaction to be settled by book-entry delivery if the following conditions apply:

- (1) the transaction has been compared in the automated comparison system;
- (2) each party to the transaction is a member of a registered securities depository, or its clearing agent for the transaction is a member; and,
- (3) the securities are eligible for deposit at a depository of which both parties are members, or, if the parties are members of different depositories, the securities are eligible at each of the two depositories and the depositories are linked for inter-depository delivery.

**Automated Confirmation/Affirmation and Book-Entry Settlement of Customer Transactions:**

**Rules G-15(d)(ii) and G-15(d)(iii)**

Rule G-15(d)(ii) currently requires that a customer transaction be confirmed using the confirmation/affirmation system of a registered securities clearing agency if the following conditions apply:

- (1) settlement of the transaction is on a delivery vs. payment (DVP) or receipt vs. payment (RVP) basis;
- (2) the security has a CUSIP number; and,
- (3) each party to the transaction is a member of a registered securities clearing agency, or its clearing agent for the transaction is a member.

Rule G-15(d)(iii) currently requires a customer transaction to be settled by book-entry delivery if the following conditions apply:

- (1) settlement of the transaction is done on a DVP or RVP basis;
- (2) each party to the transaction is a member of a registered securities depository, or its agent for the transaction is a member; and,

- (3) the securities are eligible for deposit in a depository of which both parties are members, or, if the parties are members of different depositories, the securities are eligible in each depository and the depositories are linked for inter-depository deliveries.

**Discussion and Summary of Amendments**

**Inter-Dealer Comparison: Rule G-12(f)(i)**

The Board has concluded that the first priority should be automated comparison of inter-dealer transactions. The Board has found widespread support among industry members for the automated comparison system and many dealers report that trades compared through the system are more likely to settle on time, minimizing expenses and personnel time associated with rejected deliveries. Notwithstanding this support, a number of dealers have noted that, because the current automated comparison system cannot yet accommodate a substantial percentage of all municipal securities transactions, they have continued automatically to prepare and send physical confirmations for all their municipal securities transactions, including transactions that are compared through the automated comparison system. This practice naturally has reduced the cost savings that could be obtained from use of the system. In January 1985, the Board stated that the sending of physical confirmations should be discontinued for transactions compared through the automated comparison system, noting that the practice is costly for the sending dealer as well as for the receiving dealer which would be required to process the duplicate information.<sup>4</sup> The Board expects that one when-issued and extended settlement date transactions are included in the automated comparison system, which National Securities Clearing Corporation (NSCC) has scheduled for February 28, 1986, dealers will discontinue the sending of duplicate physical confirmations for inter-dealer transactions because most inter-dealer transactions then will be eligible for automated comparison. The Board notes that NSCC also has committed to modify its comparison system to accommodate municipal securities transactions subject to special conditions or agreements (e.g., subject to the security having a specified rating).

The Board also wishes to point out that the current comparison rate of inter-dealer transactions is only approximately 63 percent on the initial comparison cycle.<sup>5</sup> This suggests that many dealers are not submitting all eligible transactions for comparison by the day after trade date and, as a result, the industry still must bear the costs of resolving un-compared transactions. One of the reasons transactions are not being compared in the original comparison cycle is that some dealers have continued to treat certain inter-dealer transactions (e.g., transactions with dealer banks) as customer transactions and are not submitting these transactions for comparison. The Board strongly urges dealers to take steps to ensure that all eligible inter-dealer transactions are submitted by both parties to the inter-dealer automated com-

<sup>3</sup>A dealer that is not a direct member of a registered securities clearing agency may be subject to the rule for purposes of some transactions (those on which a member clearing agent is used) and not on others (those on which a member clearing agent is not used).

<sup>4</sup>MSRB Interpretation of January 2, 1985, *MSRB Manual* (CCH) ¶3556.70 at pp. 3559-20-3560.

<sup>5</sup>Approximately 85 percent of trades submitted compare by their settlement dates.

parison system.<sup>6</sup> The Board also has been advised that certain dealers do not obtain transaction information from their regional offices in time to submit the transactions for comparison in the initial comparison cycle. The Board emphasizes that the cost savings resulting from automated comparison flow from comparing transactions in the initial comparison cycle and urges dealers who may be experiencing problems in this area to effect the necessary in-house procedures to ensure timely submission of all transactions.<sup>7</sup> Finally, the Board urges dealers to establish in-house procedures that enable identification of specific transactions that have been submitted (or should have been submitted) for comparison. These procedures should identify transactions sufficiently to allow uncomparated trades to be resolved quickly and, for dealers submitting transactions on behalf of other dealers, should identify the dealers on whose behalf the transactions are submitted.

#### **Inter-Dealer Book-Entry Settlement: Draft Amendment to Rule G-12(f)(ii)**

The Board believes that the second priority should be book-entry settlement of inter-dealer transactions. The book-entry delivery systems offer the greatest benefits when securities remain at a depository. The Board understands that many industry members already are realizing significant cost savings on inter-dealer transactions settled via book-entry because the securities typically are left in safekeeping at a depository. However, a dealer that must withdraw securities from a depository to satisfy a customer request for physical securities must bear the cost of withdrawing the securities as well as the cost of making the physical delivery to the customer.<sup>8</sup> Although dealers report that customers increasingly allow securities to remain in depositories, some customers—both individuals and institutions—continue to insist on physical delivery of securities. In addition, several states still have laws which require securities used for certain purposes to be located within the geographic boundaries of the states. It therefore appears that until there is a wider acceptance of safekeeping arrangements, certain dealers, particularly those who do a predominantly retail business, will be unable to derive substantial benefits from the book-entry delivery systems.

Accordingly, the Board is proposing an amendment to rule G-12(f)(ii) that would permit the parties to an inter-dealer transaction eligible for book-entry delivery to agree to settle the transaction by physical delivery rather than by book-entry delivery. If, however, either party declines to agree to a physical delivery, the rule would require book-entry delivery. The Board anticipates that the amendment would have limited application to those transactions in which a physical delivery clearly would be beneficial to both parties to the transactions and expects that the majority of eligible transactions will continue to be settled by the less-costly book-entry method. The Board urges dealers to facilitate the transition to book-entry settlement by educating customers about the benefits of safekeeping of securities.

The Board requests comments on the probable effect and application of the draft amendment. Specifically, the Board requests comment whether the draft amendment generally would discourage dealers from making or accepting book-entry deliveries and, on what types of transactions would dealers be likely to agree to make physical deliveries. The Board requests information whether dealers are more likely to request or to agree to physical deliveries of bearer or registered securities and, if so, whether the draft amendment should be limited in its application to bearer or registered securities.

#### **Automated Clearance and Settlement of Customer Transactions: Draft Amendments to Rule G-15(d)**

The Board believes that the third priority should be the automated clearance and settlement of customer transactions. The Board continues to believe that the use of automated confirmation/affirmation and book-entry settlement systems will reduce greatly the number of failed customer transactions and result in significant cost savings for the industry and major market participants. Although the Board understands that the industry generally supports use of these automated systems for customer transactions, it appears that customer acceptance and use of the automated confirmation/affirmation systems has been limited, with only approximately 43 percent of transactions in depository eligible securities submitted being affirmed by customers, compared to 85 percent for corporate transactions.

Many institutional customers are not aware of these systems for municipal securities or how to use them; other customers, particularly indirect depository participants, may find the systems difficult to use because of the lack of direct communications links with the depositories offering the services. Some dealers have reported to the Board that many customers continue to require physical confirmations from dealers even though the transactions can be confirmed through one of the automated systems. Various dealers have stated that some customers must provide written instructions to their agents before the agents may accept deliveries which limits the ability of agents to accept deliveries on trades affirmed through the systems.

With respect to the use of book-entry systems for settling customer transactions, dealers report that many institutional customers, especially smaller institutions, continue to request physical deliveries of securities eligible for book-entry delivery. The Board also is aware, however, that some institutional customers, who do not affirm eligible transactions through the automated confirmation/affirmation systems, nevertheless accept, and may prefer, book-entry settlement of their transactions.

Based upon the experience of the corporate securities industry in implementing automated clearance and settlement systems for customer transactions, it is apparent that significant resources and concentrated efforts will be needed to overcome the structural impediments to automated clearance and settlement of municipal securities transactions

<sup>6</sup>See MSRB Interpretation of December 13, 1984, *MSRB Manual* (CCH) ¶3556 at p. 3559. These transactions may not be compared through the confirmation/affirmation systems for customer transactions.

<sup>7</sup>For example, the Board understands that at least one dealer has established regional centers which submit transaction data directly to NSCC as well as to the home office.

<sup>8</sup>Similar expenses must be borne by a dealer who receives physical securities from a customer and must place them into a depository to complete a transaction with another dealer.



with customers. This will require concentrated efforts to educate municipal securities customers about the benefits of these systems as well as the establishment of additional communications links between customers, their clearing agents, and the depositories. As a result, the Board believes that the industry would benefit more from directing its immediate efforts to implementing the automated clearance requirements for inter-dealer transactions and then devoting its efforts to expanding the use of the automated clearance systems for customer transactions.

The draft amendments to rules G-15(d)(ii) and G-15(d)(iii) would not require use of the automated confirmation/affirmation and book-entry delivery systems for eligible customer transactions unless the customer requests or agrees to use the systems. The Board intends to monitor use of the automated confirmation/affirmation and book-entry delivery systems with a view toward requiring the use of the systems at an appropriate time in the future.

The Board is soliciting comment on the draft amendments, particularly whether the draft amendments generally would discourage use of the confirmation/affirmation systems by those currently using them. If so, the Board would welcome information about current use of the confirmation/affirmation systems. The Board also requests comment whether the draft amendments would discourage book-entry deliveries by dealers and customers currently using the systems. If so, the Board would welcome comment identifying the types of transactions currently being settled by book-entry delivery which would be settled by physical delivery. The Board also requests comments whether benefits exist for book-entry delivery of customer transactions which are not affirmed through a confirmation/affirmation system and whether the draft amendments to rule G-15(d) should retain the requirement to settle certain transactions by book-entry delivery. Finally, the Board welcomes comment whether institutional customers would be more likely to request physical delivery of bearer securities or registered securities and whether the draft amendment should be limited to transactions in securities in bearer or registered form.

**January 13, 1986**

### **Text of Draft Amendments\***

#### **Rule G-12. Uniform Practice**

- (a) through (e) No change.
- (f) Use of Automated Comparison, Clearance and Settlement Systems.
  - (i) No change.
  - (ii) Notwithstanding the provisions of section (e) of this rule, if a transaction submitted to one or more registered clearing agencies for comparison in accordance with paragraph (i) above has been compared successfully, and if such transaction involves municipal securities which are eligible for deposit at one or more securities depositories registered with the Securities and Exchange Commission in which both parties to the transaction are mem-

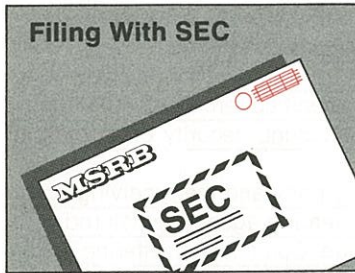
bers, the parties to such transaction shall settle the transaction by book-entry through the facilities of the depository or through the interface or link, if any, between the depositories unless both parties to the transaction agree to settle the transaction with a physical delivery of securities in accordance with the provisions of section (e) of this rule. ~~The provisions of this paragraph (ii) shall apply to transactions effected on or after February 1, 1985.~~

- (iii) No change.
- (g) through (l) No change.

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

- (a) through (c) No change.
- (d) Delivery/Receipt vs. Payment Transactions.
  - (i) No change.
  - (ii) No A broker, dealer or municipal securities dealer who which is, or whose which uses a clearing agent with respect to such transaction which is, a participant in a clearing agency registered with the Securities and Exchange Commission shall effect and which executes a transaction in any a municipal security to which a CUSIP number has been assigned on a delivery vs. payment or receipt vs. payment basis for the account of a customer who is, or whose agent with respect to such transaction is, a participant in such clearing agency (or in a clearing agency interfaced or otherwise linked with such clearing agency) unless shall use the facilities of such clearing agency (or the facilities of a clearing agency interfaced or otherwise linked with such clearing agency, as necessary) are used for the confirmation and acknowledgement of such transaction upon the request of or agreement by the customer. ~~The provisions of this paragraph (ii) shall apply to transactions effected on or after August 1, 1984; provided, however, that transactions in federally guaranteed public housing authority project notes effected prior to January 1, 1985 shall not be subject to the provisions of this paragraph.~~
    - (iii) No A broker, dealer or municipal securities dealer who which is, or whose which uses a clearing agent with respect to such transaction which is, a participant in a clearing agency registered with the Securities and Exchange Commission shall effect and which executes a transaction in any a municipal security which is eligible for book-entry settlement through the facilities of such clearing agency on a delivery vs. payment or receipt vs. payment basis for the account of a customer who is, or whose agent with respect to such transaction is, a participant in such clearing agency (or in a clearing agency interfaced or otherwise linked with such a clearing agency) unless shall use the facilities of such clearing agency (or the facilities of a clearing agency interfaced or otherwise linked with such clearing agency, as necessary) are used for the book-entry settlement of such transaction upon the request of or agreement by the customer. ~~The provisions of this paragraph (iii) shall apply to transactions effected on or after February 1, 1985.~~
  - (e) No change.

\*Underlining indicates new language; broken rule indicates deletions.



**Route To:**

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

**Customer Account Transfers: Rule G-26**

**Amendment Filed**

**The new rule would establish standards for customer account transfers.**

On January 2, 1986, the Board filed with the Securities and Exchange Commission a new rule G-26 concerning customer account transfers. The new rule is designed to ensure that customer account transfers are accomplished in a timely and efficient manner by municipal securities dealers. The new rule, which parallels rules recently adopted by the New York Stock Exchange (NYSE)<sup>1</sup> and the National Association of Securities Dealers (NASD),<sup>2</sup> will ensure that a uniform account transfer standard applies to all municipal securities dealers. The Board has asked the Commission to approve the new rule with an effective date of February 24, 1986.

**Background**

The securities industry recently has sought to address the problems that sometimes arise when a customer decides to transfer its entire account from one industry member to another. Both the NYSE and NASD have adopted specified procedures for transfers of customer accounts by their members. New rule G-26 is designed to enhance these developments by ensuring that all municipal securities dealers, including sole municipal securities firms and dealer banks, are subject to uniform customer account transfer requirements. The Board believes that new rule G-26 will benefit the securities industry as a whole by establishing a uniform customer account transfer standard which will provide greater efficiency in the transfer of customer accounts and protect customers who are entitled to prompt action in this area.

**Summary of Amendment**

New rule G-26 requires municipal securities brokers and dealers to cooperate in the transfer of customer accounts. The rule establishes specific time limits, generally 10 days, within which a dealer would be required to transfer a customer account. It limits the reasons for which a dealer may

object to an account transfer instruction to those not involving securities positions or money balance differences. The rule provides for the establishment of fail-to-receive and fail-to-deliver contracts, and requires that fail contracts be resolved in accordance with the Board's close-out procedures, rule G-12(h). In addition, the rule requires the use of automated customer account transfer systems in place at registered clearing agencies when both dealers are participants in the clearing agency.<sup>3</sup> Finally, the rule requires municipal securities dealers to submit copies of account transfer instructions to the enforcement agency having jurisdiction over the dealer carrying the account, if the enforcement agency requests them, as dealers should be prepared to expect on a routine basis.

**January 2, 1986**

**Text of Proposed Rule\***

**Rule G-26. Customer Account Transfers**

(a) When a customer whose municipal securities account is carried by a municipal securities broker or dealer (the "carrying party") wishes to transfer its entire account to another municipal securities broker or dealer (the "receiving party") and gives written notice of that fact to the receiving party, both municipal securities brokers or dealers must expedite and coordinate activities with respect to the transfer as follows:

(i) Upon receipt from the customer of a signed transfer instruction to receive such customer's securities account from the carrying party, the receiving party shall immediately submit such instruction to the carrying party. The carrying party shall, within five business days following receipt of such instruction, validate and return the transfer instruction to the receiving party (with an attachment reflecting all positions and money balances as shown on its books) or take exception to the transfer instruction for reasons other than securities positions or money balance differences and advise the receiving party of the exception taken.

**Questions about the notice may be directed to William E. Hawxhurst, Assistant General Counsel.**

<sup>1</sup>NYSE rule 412 was approved by the Commission on November 26, 1985, and takes effect on February 24, 1986.

<sup>2</sup>NASD section 65 to the Uniform Practice Code, SR-NASD-85-29, is expected to be approved in time to take effect at the same time as NYSE rule 412.

<sup>3</sup>The National Securities Clearing Corporation (NSCC) currently offers a pilot automated customer account transfer system. Currently, however, the system only may be used by full clearing members of NSCC.

\*Underlining indicates new language.

(ii) The carrying party and the receiving party shall promptly resolve any exceptions taken to the transfer instruction.

(iii) Within five business days following the validation of a transfer instruction, the carrying party shall complete the transfer of the account to the receiving party. The receiving party and the carrying party shall immediately establish fail-to-receive and fail-to-deliver contracts as of the date of validation upon their respective books of account against the long/short positions in the customer's account that have not been physically delivered/received and the receiving party/carrying party shall debit/credit the related money amount. The customer's account shall thereupon be deemed transferred.

(b) Any fail contracts resulting from this account transfer procedure shall be closed out in accordance with rule G-12(h).

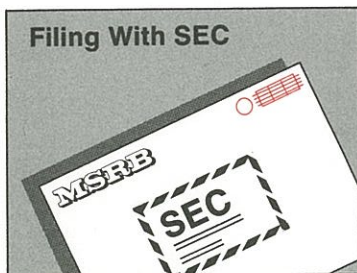
(c) Any discrepancies relating to positions or money bal-

ances that exist or occur after transfer of a customer's securities account shall be resolved promptly.

(d) The Board may exempt from the provisions of this rule, either unconditionally or on specified terms and conditions, any dealer or any type of account, security or municipal security.

(e) When both the carrying party and the receiving party are direct participants in a clearing agency registered with the Securities and Exchange Commission offering automated customer securities account transfer capabilities, the account transfer procedure, including the establishing and closing out of fail contracts, shall be accomplished pursuant to the rules of and through such registered clearing agency.

(f) The carrying party shall provide a copy of each customer account transfer instruction issued pursuant to paragraph (a) (i) to the enforcement authority having jurisdiction over the carrying party member, at the request of such authority.



**Route To:**

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

**Concession Disclosure for Zero Coupon, Compound Interest and Multiplier Securities: Rule G-12**

**Amendment Filed**

**Dealers would be required to disclose on inter-dealer confirmations the amount of the concession on transactions in zero coupon, compound interest and multiplier securities as a percentage of the bond's price.**

On January 6, 1986, the Board filed with the Securities and Exchange Commission proposed amendments to rule G-12(c)(v)(J) regarding disclosure on inter-dealer confirmations of amount of concession on transactions in zero coupon bonds (including "GAINS") and compound interest and multiplier securities. The proposed amendments will not become effective until they are approved by the Commission.

Rule G-12(c)(v)(J) requires dealers to disclose on inter-dealer confirmations the amount of concession on the transaction, if any, per \$1000 par value unless stated to be an aggregate figure. In response to industry inquiries on how the rule applies to zero coupon, compound interest, and multiplier securities, the Board is amending rule G-12(c)(v)(J) to require the disclosure of the amount of concession on these securities as a percentage of the bond's price. The new requirement is more consistent with current industry

practice. The Board also was concerned that disclosure of the amount of concession based on the maturity or par value of these securities may be confusing.

January 3, 1986

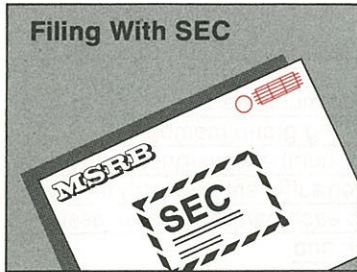
**Text of Proposed Amendments\***

**G-12. Uniform Practice**

- (a) and (b) No change.
- (c) Dealer Confirmations.
  - (i) through (iv) No change.
  - (v) Each confirmation shall contain the following information:
    - (A) through (I) No change.
    - (J) amount of concession, if any, per \$1000 par value unless stated to be an aggregate figure, provided, however, that for a transaction in securities maturing in two or more years and, at the time of the transaction, paying investment return solely through capital appreciation, the concession, if any, shall be expressed as a percentage of the price of these securities;
    - (K) through (N) No change.
  - (vi) No change.
- (d) through (l) No change.

**Questions about the proposed amendments may be directed to Diane G. Klinke, Deputy General Counsel.**

\*Underlining indicates new language.



**Route To:**

- Manager, Muni. Dept.
- Underwriting
- Trading
- Sales
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- Training
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**Dissemination of CUSIP Numbers and Initial Trade Dates for New Issues: Rule G-34**

**Amendment Filed**

**Managing underwriters would be required to communicate CUSIP numbers and the initial trade date for new issues to syndicate and selling group members on the initial trade date.**

On January 6, 1986, the Board filed with the Securities and Exchange Commission an amendment to rule G-34 on CUSIP numbers. The amendment would require a managing underwriter to disseminate CUSIP numbers and information on the date that trading begins in a new issue of municipal securities (the "initial trade date") to syndicate and selling group members on the initial trade date. The amendment is intended to facilitate use of the automated comparison system for when, as and if issued ("when-issued") transactions, which is scheduled to become operational on February 28, 1986. The Board has requested the Commission to accelerate approval of the amendment if necessary to ensure effectiveness prior to or concurrent with the commencement of the when-issued comparison system.

**Background**

Rule G-34 requires a municipal securities dealer acting as an underwriter of a new issue to apply to the Board or its designee (currently the CUSIP Service Bureau) for assignment of CUSIP numbers to the issue.<sup>1</sup> National Securities Clearing Corporation is planning to provide automated comparison facilities for when-issued transactions on February 28, 1986. The automated comparison system will require that a dealer submitting a transaction to the system include the CUSIP number for the issue, which will require dealers to have access to CUSIP numbers for new issues at the time

that trading in the issue begins. For when-issued transactions that are not between a syndicate manager and a syndicate member, both dealers should submit transactions to the registered clearing agency by the day after trade date in order for the system to work efficiently. Therefore, dealers submitting transactions to the system will need CUSIP numbers on, or as soon as possible after, trade date.<sup>2</sup>

In addition, since many dealers wish to begin trading in an issue as soon as possible, it is necessary for the industry to be advised by the underwriters when trading begins. For purposes of rule G-12(c), which requires when-issued confirmations to be sent within two business days of trade date, the Board has interpreted "trade date" to be no earlier than the date of award, for competitive issues, or the date of the execution of the contract to purchase the issue, for negotiated issues. The Board also has interpreted rule G-17, on the conduct of municipal securities business, to prohibit the sending of when-issued confirmations prior to these dates.<sup>3</sup> As the Board noted in the publication of this interpretation, it does not wish to question the validity of a "pre-sale" order for new issue municipal securities,<sup>4</sup> but believes that the sending of when-issued confirmations of transactions prior to these dates would be misleading. Although managing underwriters will know the date of award or the execution of the contract to purchase the issue, other dealers with pre-sale orders also will need to know the "initial trade date" on which trades can be submitted to the automated comparison system.

**Summary of Amendment**

The amendment would require managing underwriters to communicate CUSIP numbers and the initial trade date to syndicate members and to selling group members on the initial trade date. The initial trade date is defined in the

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

<sup>1</sup>The Board recently adopted, and the Commission approved on December 19, 1985, an amendment to rule G-34 which requires an underwriter for a negotiated issue to apply to the CUSIP Service Bureau for CUSIP numbers at a time sufficient to ensure that the numbers will be assigned on or prior to the date that the contract to purchase the securities from the issuer is executed. If an application for CUSIP numbers for a competitive issue has not been made prior to the date of award, the amendment requires the underwriter to apply for CUSIP numbers on the date of award. The amendment also places a requirement on municipal securities dealers serving as financial advisors to issuers on competitive issues to ensure that CUSIP numbers are assigned prior to the date of award. SEC Release No. 34-22730 (December 19, 1985).

<sup>2</sup>The CUSIP Service Bureau disseminates CUSIP numbers that have been assigned during the previous week in weekly supplements to the *CUSIP Directory* and arranges for some CUSIP numbers assigned two business days prior to be published in *The Blue List of Current Municipal Offerings*, a daily publication of Standard and Poor's Corporation.

<sup>3</sup>See MSRB Interpretation of April 30, 1982, *MSRB Manual* (CCH) ¶3556 at 3559-19.

<sup>4</sup>A "pre-sale" order is an expression of the willingness of the party placing the order to purchase new issue securities having certain characteristics at a stated price. Pre-sale orders are expressions of the purchasers' firm intent to buy the new issue municipal securities in accordance with the stated terms and, in contrast to "indications of interest" for corporate securities, such orders may be filled and confirmed immediately upon the award of the issue or the execution of a bond purchase agreement.

amendment to mean, for competitive issues, either the date of award or the first date allocations are made to syndicate or selling group members, whichever date is later, and, for negotiated issues, either the date on which the contract to purchase the securities from the issuer is executed or the first date allocations are made to syndicate or selling group members, whichever date is later. This would ensure that syndicate members and selling group members have information necessary for timely submission of transactions to the automated comparison system. If the amendment does not result in adequate dissemination of this information, the Board will consider other measures to accomplish this end, such as a requirement that managing underwriters publish the information through channels generally available to the industry.

January 2, 1986

**Text of Draft Amendments\***

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

- (a)-(b) No change.
- (c) Each municipal securities broker or municipal securities

dealer who acquires, whether as principal or agent, a new issue of municipal securities from the issuer of such securities for the purpose of distributing the new issue shall on the initial trade date communicate the following information to syndicate and selling group members:

(i) the CUSIP number or numbers assigned to the issue and descriptive information sufficient to identify the CUSIP number corresponding to each part of the issue assigned a specific CUSIP number; and

(ii) the initial trade date. For purposes of this paragraph (c), initial trade date shall mean, for competitive issues, either the date of award, or the first date allocations are made to syndicate or selling group members, whichever date is later, and, for negotiated issues, either the date on which the contract to purchase the securities from the issuer is executed, or the first date allocations are made to syndicate or selling group members, whichever date is later.

(d) No change.

\*Underlining indicates new language.



**Route To:**

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

## Settlement Dates for When, As and If Issued Transactions: Rule G-12

### Amendment Approved

Managing underwriters are required, for when, as and if issued transactions compared through automated comparison facilities, to—

- provide the clearing agency with not less than six business days' notice of settlement date,
- specify that the settlement date for when-issued transactions would be not less than five business days following the date notice of the final settlement date is provided to the clearing agency, and
- delete provisions permitting acceleration of settlement of when-issued transactions when issuer has accelerated delivery to managing underwriter.

On October 25, 1985, the Securities and Exchange Commission approved amendments to rule G-12(b)(ii)(C) and (iii) concerning settlement dates for when, as and if issued ("when-issued") transactions. The amendments standardize settlement dates for when-issued transactions that are compared and settled either under rule G-12 or through automated facilities provided by a clearing agency registered with the SEC. The amendments also delete provisions that permit syndicate managers and members to accelerate settlement dates for intra-syndicate trades when an issuer accelerates settlement with the managing underwriter. The amendments are designed to accommodate the new automated comparison facilities for when-issued transactions which will not distinguish between intra-syndicate transactions and transactions between syndicate members and other dealers ("street trades") for purposes of specifying settlement dates for when-issued transactions. The Board filed the proposed amendments on August 13, 1985,<sup>1</sup> and on October 7, 1985, filed a clarifying amendment to those provisions as summarized below. The amendments became effective on January 1, 1986.

### Summary of Amendments

The amendments retain the current definition of settlement date for when-issued transactions compared pursuant to rule G-12 (i.e., five business days, or six business days in the case of transactions between a manager and syndicate

members, after the date the final confirmation is sent). In addition, for transactions compared through the automated comparison facilities of a registered clearing agency, the rule requires a managing underwriter to provide the registered clearing agency with not less than six business days' notice of settlement for the issue and specifies that the settlement date be not less than five business days following the date notice of the final settlement date is provided to the clearing agency. The originally proposed amendments provided that the settlement date for when-issued municipal securities transactions would be at least five business days after the clearing agency provided notice of that date. As noted previously, the Board filed an amendment to the originally proposed amendments which provided that the settlement date for these transactions would be not less than five business days following the date notice of the final settlement date is provided to the clearing agency. National Securities Clearing Corporation (NSCC), the registered clearing agency that intends to offer automated comparison facilities for when-issued transactions, requested that the Board revise the proposed amendments to provide that the settlement date for these transactions be not less than five business days following the date notice of the final settlement date is provided to it. It was concerned that if a systems failure prevented it from providing at least five days notice of settlement, it would be required to establish a settlement date different than that set by the manager. The amendments track the provision applicable to physical settlements under which a settlement date must be at least five business days following the date the final confirmation indicating the settlement date is sent, since the manager informing NSCC of the settlement date is analogous to its sending a final confirmation. The Board believes the suggested revision satisfies its intention that managers provide sufficient notice of settlement.

The amendments also delete the provisions that permit acceleration of when-issued transactions when a manager receives less than six business days' notice of settlement from an issuer. The rule amendments, however, do not limit the ability of a syndicate manager to accept an accelerated delivery from an issuer.

The Board concluded that it is appropriate to adopt these provisions in light of the need to standardize settlement

**Questions about these amendments may be directed to Angela Desmond, General Counsel.**

<sup>1</sup>See *MSRB Reports*, vol. 5, no. 5 (August 1985).

dates to accommodate the current automated clearance systems. It believes that substantial cost savings should be realized from comparing when-issued trades on an automated basis. In addition, the Board understands that instances in which issuers accelerate settlements are rare and that in most instances final confirmations of when-issued transactions are sent well in advance of the six- and five-day minimum time periods. The Board urges all syndicate managers to take appropriate steps in settling settlement dates with issuers to avoid unnecessary settlement accelerations by issuers.

**December 5, 1985**

**Text of Amendments\***

**Rule G-12. Uniform Practice**

- (a) No change.
- (b) Settlement Dates.
  - (i) No change.
  - (ii) Settlement Dates. Settlement dates shall be as follows:
    - (A) for "cash" transactions, the trade date;
    - (B) for "regular way" transactions, the fifth business day following the trade date;
    - (C) for "when, as and if issued" transactions, a date agreed upon by both parties, which date shall not be earlier than the fifth business day following the date the confirmation indicating the final settlement date is sent, or, with respect to transactions between the manager and members of a syndicate or account formed to purchase securities from an issuer, a date not earlier than the sixth business day following the date the confirmation indicating the final settlement date is sent; pro-

vided, however, that if the issuer gives notice of pending delivery within less than six business days before delivery, the settlement date for transactions with respect to such issue of securities may be accelerated

(1) for transactions between the manager and members of the syndicate or account, as determined by the manager,

(2) for transactions between members of the syndicate or account, as determined by each seller, but by not more than the number of days of acceleration by the syndicate manager, and

(3) for all other transactions, as may be determined by agreement between the parties to such transactions; and

for when, as and if issued transactions compared through the automated comparison facilities of a registered clearing agency under paragraph (f) of this rule, a managing underwriter shall provide the registered clearing agency with not less than six business days notice of settlement for the issue, and the settlement date shall be not less than five business days following the date notice of the final settlement date is provided to the registered clearing agency; and

(D) No change.

~~(iii) Notice of Accelerated Delivery.—In the event the issuer gives notice of pending delivery of securities within less than six business days before delivery, the manager of a syndicate or account formed to purchase the securities from the issuer shall, immediately upon determination of the accelerated delivery date pursuant to subparagraph (b)(ii)(C) hereof, give immediate notice to the members of the syndicate or account of the settlement date for transactions between the manager and the members.~~

(c)-(1) No change.

\*Underlining indicates new language; broken rule indicates deletions.





**Route To:**

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

**CUSIP Numbers—Timely Assignment; Automated Comparison of When-Issued Trades with Pending CUSIP Number Assignments: Rules G-34 and G-12**

**Amendment Approved: Rule G-34**

**Underwriters are required to ensure assignment of CUSIP numbers for new issues on date of contract award or sale.**

**Interpretation Approved: Rule G-12**

**Once when-issued automated comparison is available, when-issued trades in securities with pending CUSIP number assignments should be submitted for automated comparison on an "as of" basis upon assignment of CUSIP numbers.**

On December 19, 1985, the Securities and Exchange Commission approved an amendment to rule G-34(a) concerning the timely assignment of CUSIP numbers and also approved an interpretation of rule G-12(f) which requires that, under certain circumstances, when-issued trades should be submitted for comparison in the automated system on an "as of" basis once the CUSIP numbers are assigned to the issue.<sup>1</sup>

**Summary of Amendment to Rule G-34**

Rule G-34 requires a municipal securities dealer acting as an underwriter of a new issue of municipal securities to apply to the Board or its designee (currently the CUSIP Service Bureau) for CUSIP numbers for the issue. Under previous paragraph (a)(i)(A) of rule G-34, application for CUSIP numbers had to be made promptly, and in any event no later than the business day after the date of the contract to purchase the issue (for negotiated issues) or the business day after the award of the issue (for competitive issues).

The National Securities Clearing Corporation (NSCC), the central processor for municipal securities comparisons, plans to begin comparing when-issued trades in February 1986.

Since automated comparison depends on CUSIP numbers, in order for when-issued transactions to be compared in the automated system, CUSIP numbers should be available on the day when-issued trading begins in a new issue. If the underwriter were to delay its application for CUSIP number assignments to the extent permitted by the rule prior to this amendment, an issue could begin to trade on a when-issued basis without the CUSIP numbers being assigned.

Accordingly, the Board has adopted an amendment to rule G-34(a) that establishes requirements for specific dealers to ensure that CUSIP numbers are available once when-issued trading in an issue begins.<sup>2</sup> The amended rule presumes that underwriters and/or issuers will provide preliminary information to the CUSIP Service Bureau as soon as possible so that CUSIP numbers can be assigned on the date of award or sale. The Board understands that in some instances preliminary information is not being submitted, which has resulted in delays in CUSIP number assignments until after when-issued trading begins in a new issue.

In the case of a negotiated issue, the amended rule requires the managing underwriter to ensure CUSIP number assignments on or before the business day that the contract to purchase the issue is executed.<sup>3</sup> In a competitive issue, if the issuer has not already applied for CUSIP numbers, the managing underwriter is required to ensure that CUSIP numbers will be assigned on the date of the award. In the event that a municipal securities dealer is serving as a financial advisor to the issuer on a competitive issue, the financial advisor is required to apply for CUSIP numbers in sufficient time to permit assignment of the numbers prior to or on the date of award. If the financial advisor fails to apply for CUSIP number assignments, the managing underwriter must ensure that CUSIP numbers are assigned to the issue as required by the rule.

The amendment went into effect on December 19, 1985, the date of Commission approval. The Board reminds managing underwriters and financial advisors to begin the application process for CUSIP number assignments as soon as possible to ensure that CUSIP numbers will be available on

**Questions about the amendment and interpretation may be directed to William E. Hawxhurst, Assistant General Counsel.**

<sup>1</sup>SEC Release No. 34-22730 (December 19, 1985).

<sup>2</sup>If the issuer has applied for CUSIP number assignments on an issue, then the requirements do not apply.

<sup>3</sup>If the contract is executed after the normal business hours of the CUSIP Service Bureau, the dealer should ensure that numbers can be assigned as soon as possible on the following business day.

the date of award or sale. The assignment process can be facilitated by submitting preliminary information about the issue as soon as it is available. Although the managing underwriter or financial advisor may not know all the details about an issue that are necessary to obtain CUSIP number assignments until immediately prior to the date of contract execution or the date of award of an issue, the Board believes that sufficient preliminary information can be provided to the CUSIP Service Bureau to ensure timely assignment of CUSIP numbers once final and complete information on an issue becomes available, thereby permitting the use of the automated comparison system for when-issued trades.

#### **When-Issued Transactions Must Be Submitted to Automated System if Application for CUSIP Number is Pending**

Rule G-12(c) requires that physical confirmations of when-issued transactions be sent out within two business days of trade date. Rule G-12(f) requires trades to be submitted for comparison in an automated comparison system operated by a registered securities clearing agency if certain conditions are met.<sup>4</sup> Rule G-12(a) provides that trades submitted for comparison in the automated system are not subject to the physical confirmation requirements of rule G-12(c).

The Board has received some inquiries from dealers concerning the requirements of rules G-12(c) and (f) once the automated comparison system for when-issued trades becomes operational. These dealers have asked whether when-issued trades should be compared using the physical confirmation process set forth in rule G-12(c) if the trades cannot be submitted immediately into the automated comparison system due to the lack of CUSIP number assignments. The Board notes that a when-issued transaction in a new issue for which no CUSIP number will be assigned is not eligible for automated comparison and must be compared by the use of physical confirmations. The Board has interpreted rule G-12(f) to require that, when when-issued automated comparison becomes available, if a request for a CUSIP number is pending, the trade should be submitted into the automated system on an "as of" basis once the CUSIP number is assigned.

**December 31, 1985**

### **Text of Amendments\***

#### **Rule G-34. CUSIP Numbers**

(a) New Issue Securities.

(i) Assignment of Numbers.

(A) Except as otherwise provided in this section (a), each municipal securities broker or municipal securities dealer who acquires, whether as principal or agent, a new issue of municipal securities from the issuer of such securities for the purpose of distributing such new issue shall apply in writing to the Board or its designee for assignment of a CUSIP number or numbers to such new issue. The municipal securities broker or municipal securities dealer shall make such application as promptly as possible, but in no event later than, ~~in the case of competitive sales, the business day following the date of award, or, in the case of negotiated sales, the business day following the date on which the contract to purchase the securities from the issuer is executed.~~ in the case of negotiated sales, a time sufficient to ensure assignment of a CUSIP number or numbers on or prior to the business day on which the contract to purchase the securities from the issuer is executed; or, in the case of competitive sales, the date of award. A municipal securities broker or dealer acting as a financial advisor to an issuer in connection with a competitive sale of an issue shall ensure that application for a CUSIP number or numbers is made in sufficient time to permit assignment of CUSIP numbers prior to the date of award. The municipal securities broker or municipal securities dealer shall provide to the Board or its designee the following information:

(1) through (8) No change.

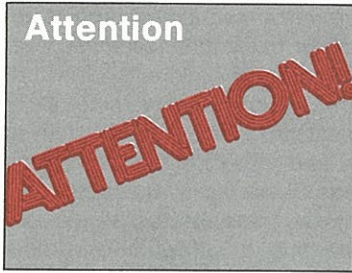
(B) through (D) No change.

(ii) through (iii) No change.

(b) through (c) No change.

<sup>4</sup>Rule G-12(f) requires eligible inter-dealer transactions between participants in a registered securities clearing agency to be submitted for comparison through the automated comparison system. For transactions in which a dealer uses a clearing agent that is a member of a registered securities clearing agency, the dealer is considered to be a participant in the registered securities clearing agency.

\*Underlining indicates new language; broken rule indicates deletions.



**Route To:**

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

**Automated Systems for Reporting Municipal Quotations and Transaction Data**

**The Board requests comments on the status and prospective development of automated systems for the dissemination of municipal quotations and transaction information.**

**Action: Send Comments**

In March 1985, the Board published a notice reviewing the history of automated systems for the dissemination of quotation and other transaction related information on municipal securities and soliciting industry comments on the development and use of such systems.<sup>1</sup> As summarized below, the Board received five comment letters, expressing general interest in such systems and seeking additional views of other market participants. Due to the number and nature of the comments, and because of the experience that may have been gained by the industry from the Municipal Bond Trading System for automated quotation and transaction execution, the Board is publishing a summary of the comments received to date and encourages the industry to continue its dialogue regarding these issues.

**Summary of March 1985 Notice**

In its March 1985 notice, the Board sought specific comment on several issues pertaining to automated quotation systems *per se* and systems incorporating transaction reporting data. With regard to quotations, the Board suggested that some type of automated system likely would be developed within the next several years, and posed the following questions:

1. Are there improvements which could be made in the present systems for the dissemination of quotations on municipal securities issues? If so, what are these?
2. Would the development of an automated system for the dissemination of real-time quotations on municipal securities issues be useful for the industry, issuers and/or public investors? If so, why?
3. To what extent do the systems presently in use in other

segments of the securities industry provide useful models for a comparable quotation system for municipal securities?

4. How would the development of such a system affect the municipal market?

5. If the development of such a system is desirable, how should the industry proceed toward its development? What should the role of the Board be in the development of such a system?

As concerns automated transaction reporting, the Board stated its understanding that, as a result of the automated clearance and settlement requirements which went into effect over the past year, the registered clearing agencies were repositories of certain aggregate data on transactions compared through the automated comparison system which could form the rudimentary basis of a transaction reporting system. The Board solicited answers to the following questions:

1. What types of transaction data, if any, should be released?
2. Should special consideration be given to the timing of the release of data?
3. What safeguards should be followed to eliminate or reduce the risk of distortion or manipulation of the data?

**Summary of Comments**

The Board received five comment letters on its March notice.<sup>2</sup> The Board also received information on two automated quotation and trading systems: the Municipal Bond Trading System (MBTS),<sup>3</sup> and the Automated Bond System (ABS) sponsored by the New York Stock Exchange (NYSE). The commentators generally expressed interest in the issues discussed in the notice and in hearing the views of other industry members. Nevertheless, as discussed below, they generally expressed reservations as to whether such systems would work fundamental changes in the secondary market for municipal securities.

**Automated Quotation Systems**

As discussed below, two of the four commentators who addressed this issue were generally in favor of automated quotation and transaction data systems, one questioned

**Comments on the matters discussed in this notice may be directed to William E. Hawxhurst, Assistant General Counsel. Written comments will be available for public inspection.**

<sup>1</sup>MSRB Reports, vol. 5, no. 3 (April 1985).

<sup>2</sup>Copies of these letters available upon request.

<sup>3</sup>MBTS, which commenced operation on October 1, 1985, discontinued its service on December 3, 1985. The system provided automated facilities for dealers and institutional investors to advertise offers for, request bids for, or execute transactions in municipal securities. All bids and offers remained on the system until the submitting party deleted or modified the information, and sellers had to validate offers daily. When a transaction was executed, MBTS generated the confirmation, showing the trade with MBTS. If the trade was eligible for automated clearance, MBTS submitted the trade data to NSCC for comparison.

whether a system could accommodate current quotation practice (dollar price for term bonds and yield for serial bonds), and a fourth opposed the idea on the ground that a centralized quotation system is unnecessary due to current brokers' broker practices, and because such a system would not increase the depth or liquidity of the secondary market.

One commentator stated that automated systems for reporting quotations and transaction data would broaden the secondary market in certain municipal issues. That commentator encouraged the Board to pursue the issue further, and suggested that the Board consider the differences between the secondary markets for municipal and corporate securities. It also urged the Board to minimize start-up costs, for example, by creating an adjunct to the National Association of Securities Dealers Automated Quotation (NASDAQ) system. Another commentator suggested that an automated system could provide additional market information, but it doubted whether the information would improve market efficiency to any significant extent. Three of the four commentators agreed that an automated system would be of limited utility in a secondary market characterized by a small supply of actively traded issues.

#### **Transaction Reporting Information**

Only one commentator addressed this issue specifically. That commentator suggested that transaction reports should be limited to trades of at least \$1 million in issues for which there are a specified minimum of daily trades (e.g., two or three trades per given day), and also suggested that reporting issues should have a par value of at least \$10 million with a serial maturity of \$1 million or more per year. Even with these provisos, this commentator noted that transaction information would be outdated quickly.

One commentator asked generally who would be entitled to share in the quotation and transaction information.

#### **NYSE Automated Bond System**

The NYSE submitted a letter describing its Automated Bond System, an automated trading/information system for

corporate bonds that has an automated execution feature and that may have relevance for municipal securities. The system, which began operations in 1977, displays bids and offers which ABS subscribers enter by price and time priority.<sup>4</sup> Execution occurs automatically through ABS when a match is found in the system, and, therefore, bids and offers are "firm" for the full amounts displayed. Immediately following a trade, ABS transmits the trade data showing price and volume to the bond tape (and to 130,000 market data terminals) and ABS subscribers receive immediate hard-copy reports of their trades. At the end of each day, ABS submits reports directly to the National Securities Clearing Corporation's comparison system on a locked-in basis.

#### **Further Comments Requested**

The Board is interested in furthering the ongoing dialogue on issues involving automated quotations and transaction reporting for municipal securities. The Board requests comments whether steps could be taken to improve current systems for the dissemination of quotations, increasing the quantity and reliability of quotation information available to market participants, and thereby enhancing the efficiency of the trading markets for municipal securities. Moreover, it is apparent that automated trading facilities for municipal securities are becoming more prominent. Because these systems may alter the manner in which municipal securities are traded, permitting investors to participate more directly in the market, the Board feels it important to encourage the exchange of views on and information concerning these developments.

For these reasons, the Board is offering to act as a clearing house for those who care to offer further views or information on these topics. The Board will publish summaries of any comments it receives.

**December 16, 1985**

<sup>4</sup>ABS calculates and displays yield-to-maturity against the bid and asked prices, and provides other additional trade data, including coupon rate, maturity date, accrued interest, and transaction histories.



**Route To:**

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

**Automated Settlement Involving Multi-Depository Participants: Rule G-12**

**Letter of Interpretation**

- **Parties to a transaction are free to agree, on a trade-by-trade basis or with standing delivery agreements, on the depository to be used for making book-entry deliveries.**
- **Absent an agreement, a seller may effect good delivery by delivering at any depository of which the receiving dealer is a member.**

This will respond to your letter concerning the requirements of rule G-12(f)(ii) applicable to transactions involving firms that are members of more than one registered securities depository. Your inquiry concerns situations in which a dealer that is a member of more than one depository executes a transaction with another dealer that is a member of one or more depositories. Your question is whether such dealers may specify the depository through which delivery must be made, either as a term of an individual transaction or with standing delivery instructions.

Your inquiry was referred to the Committee of the Board with the responsibility for interpreting the Board's automated

clearance and settlement rules, which has authorized my sending this response.

Rule G-12(f)(ii) provides in part:

[I]f a transaction submitted to one or more registered clearing agencies for comparison in accordance with paragraph (i) above has been compared successfully, and if such transaction involves municipal securities which are eligible for deposit at one or more securities depositories registered with the Securities and Exchange Commission in which both parties to the transaction are members, the parties to such transaction shall settle the transaction by book-entry through the facilities of the depository or through the interface or link, if any, between the depositories.

As you will note, the language of the rule specifies that, when certain conditions are met, a transaction must be settled via book-entry delivery. The rule does not specify which depository shall be used for settlement if the transaction is eligible for settlement at more than one depository.

The Board is of the view that, under rule G-12(f), parties to a transaction are free to agree, on a trade-by-trade basis or with standing delivery agreements, on the depository to be used for making book-entry deliveries. Absent such an agreement, a seller may effect good delivery under rule G-12(f) by delivering at any depository of which the receiving dealer is a member.—*MSRB interpretation of November 18, 1985, by Harold L. Johnson, Assistant General Counsel.*



**Route To:**

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## Publications

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### New Issues of *MSRB Manual* and *MSRB Rules*

The Board has issued its updated *MSRB Manual* and *MSRB Rules*, dated November 1, 1985, which are now available.

The *MSRB Manual*, published by Commerce Clearing House, includes the texts of the Securities and Exchange Act of 1934 and the Securities Investor Act of 1979, the Board rules, pertinent regulations of other agencies, notices concerning rule amendments and indexes to those materials. The *MSRB Rules* contains the Board rules, interpretive notices

and letters and samples of forms. Use of the *Rules* satisfies the requirements of rule G-29.

Copies of the updated *MSRB Manual* and *MSRB Rules* may be obtained from the Board offices. The cost of the *Manual* is \$6.00 per copy and of the *Rules*, \$2.50 per copy.

### Close-Out Procedures Manual

The third edition of the Board's *Manual on Close-Out Procedures*, dated January 1985, also is available. A copy of the *Manual* was mailed to each municipal securities broker and dealer when it was originally published. The *Manual* contains discussion of the close-out procedures of rule G-12(h)(i) in question-and-answer format, a glossary and rule text. Copies may be obtained from the Board offices at a cost of \$3.00 per *Manual*.



**Route To:**

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**Financial Statements—Fiscal Years  
Ended September 30, 1984  
and 1985**

**Coopers  
& Lybrand**

certified public accountants

To the Members of the  
Municipal Securities Rulemaking Board

We have examined the balance sheets of the Municipal Securities Rulemaking Board as of September 30, 1985 and 1984, and the related statements of revenues and expenses and change in fund balance and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the Municipal Securities Rulemaking Board as of September 30, 1985 and 1984, and the results of its operations and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

A handwritten signature in cursive script that reads "Coopers &amp; Lybrand".

1800 M Street, N. W.  
Washington, D. C. 20036  
October 25, 1985

MUNICIPAL SECURITIES RULEMAKING BOARD

BALANCE SHEETS

September 30, 1985 and 1984

	1985	1984
<b>ASSETS</b>		
Cash	\$ 121,118	\$ 35,074
Investments (Notes 1 and 2)	860,549	941,934
Assessment fees receivable (Note 1)	425,965	144,960
Accrued interest receivable	23,284	56,338
Other assets	15,047	57,979
Office furniture, equipment and leasehold improvements, at cost, less accumulated depreciation and amortization of \$75,029 in 1985 and \$100,330 in 1984 (Note 1)	140,319	39,752
	<u>\$1,586,282</u>	<u>\$1,276,037</u>
<b>LIABILITIES AND FUND BALANCE</b>		
Accounts payable	\$ 62,027	\$ 23,772
Accrued salaries and vacation pay	41,882	40,398
Deferred rent credit (Note 3)	100,890	-
	<u>204,799</u>	<u>64,170</u>
Commitments (Note 3)		
Fund balance	1,381,483	1,211,867
	<u>\$1,586,282</u>	<u>\$1,276,037</u>

The accompanying notes are an integral part  
of these financial statements.



MUNICIPAL SECURITIES RULEMAKING BOARD  
STATEMENTS OF REVENUES AND EXPENSES AND  
CHANGE IN FUND BALANCE  
for the years ended September 30, 1985 and 1984

	1985	1984
<b>Revenues:</b>		
Assessment fees (Note 1)	\$1,810,798	\$ 830,534
Annual fees (Note 1)	233,825	220,125
Initial fees (Note 1)	27,300	29,800
Investment income	79,892	113,950
Board manuals and other	40,631	30,716
	2,192,446	1,225,125
<b>Expenses:</b>		
Salaries and employee benefits (Note 4)	715,565	556,151
Board and committee	535,852	377,914
Operations (Note 3)	391,183	178,690
Education and communication	321,164	228,057
Professional services	72,965	61,603
Depreciation and amortization (Note 1)	32,944	23,292
	2,069,673	1,425,707
Income (loss) from operations	122,773	(200,582)
Gain on termination of lease (Note 3)	46,844	-
Revenues over (under) expenses	169,617	(200,582)
Fund balance, beginning of year	1,211,867	1,412,449
Fund balance, end of year	\$1,381,484	\$1,211,867

The accompanying notes are an integral part  
of these financial statements.

MUNICIPAL SECURITIES RULEMAKING BOARD  
STATEMENTS OF CHANGES IN FINANCIAL POSITION  
for the years ended September 30, 1985 and 1984

	<u>1985</u>	<u>1984</u>
<b>Sources of funds:</b>		
Operations:		
Revenues over (under) expenses	\$169,617	\$(200,582)
Noncash expenses - depreciation and amortization	<u>32,944</u>	<u>23,292</u>
Funds provided (used) by operations	202,561	(177,290)
Decrease in cash and investments	-	293,096
Decrease in accrued interest receivable	33,054	-
Decrease in other assets	42,931	-
Disposition of fixed assets	5,836	-
Increase in accounts payable	38,254	-
Increase in accrued salaries and vacation pay	1,485	9,895
Increase in deferred rent credit	<u>100,890</u>	<u>-</u>
	<u>\$425,011</u>	<u>\$ 125,701</u>
<b>Uses of funds:</b>		
Increase in cash and investments	\$ 4,659	\$ -
Increase in assessment fees receivable	281,005	37,649
Increase in accrued interest receivable	-	9,987
Increase in other assets	-	49,240
Purchase of fixed assets	139,347	16,492
Decrease in accounts payable	<u>-</u>	<u>12,333</u>
	<u>\$425,011</u>	<u>\$ 125,701</u>

The accompanying notes are an integral part  
of these financial statements.

MUNICIPAL SECURITIES RULEMAKING BOARD  
NOTES TO FINANCIAL STATEMENTS

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1. Accounting policies

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.

Assessment fees

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 by or through such municipal securities broker or municipal securities dealer, whether acting as principal or agent, and which have a final stated maturity of not less than two years and an aggregate par value of not less than \$1,000,000. This fee amounted to .001% of all such sales during fiscal year 1984, .001% from October 1, 1984 to June 30, 1985, and .002% from July 1, 1985 through September 30, 1985. Revenue from assessment fees is recognized upon the sale of the issue and is payable within 30 days of settlement between the underwriter and the issuer.

Annual fees

Each municipal securities broker and municipal securities dealer is required to pay an annual fee of \$100 with respect to each fiscal year of the Board in which the municipal securities broker or municipal securities dealer conducts business. This fee is due by February 15 of the fiscal year for which the fee is paid.

Initial fees

The initial fee is a one-time fee of \$100 which is to be paid by every municipal securities broker or municipal securities dealer registered with the Securities and Exchange Commission.

Continued

MUNICIPAL SECURITIES RULEMAKING BOARD  
NOTES TO FINANCIAL STATEMENTS

Revenue from initial fees is recognized when received by the Board.

Investments

Investments in securities are stated at cost which closely approximates market value.

Depreciation and amortization

Depreciation of fixed assets is computed on the straight-line method over the estimated useful lives of the assets. Amortization of leasehold improvements is computed on the straight-line method over the shorter of the remaining lease period or the estimated useful life of the improvement.

2. Investments

A summary of investments is as follows:

	September 30,	
	1985	1984
T. Rowe Price U. S. Treasury Money Fund	\$ 89,422	\$ 91,011
U. S. Treasury Bills	565,940	850,923
U. S. Treasury Notes	205,187	-
	\$860,549	\$941,934

3. Lease agreements

Effective December 15, 1984, the Board assigned the rights to lease its former office space to a tenant of the building and was released of all further obligations under this lease. The Board realized a net gain of \$46,844, after receiving cash for assigning its rights under this lease and charging to expense the net book value of abandoned leasehold improvements.

Continued

**MUNICIPAL SECURITIES RULEMAKING BOARD**  
**NOTES TO FINANCIAL STATEMENTS**

Commencing November 16, 1984, the Board leased new office space under a lease agreement expiring in November 1994. This agreement calls for the Board to receive a rent credit equal to one-half of the base monthly rent for the first 30 months of the lease. As a result, the monthly rental payments will be \$9,350 through May 1987, and \$18,700 a month for the remainder of the lease term, subject to an annual escalation based on the Consumer Price Index and a proportionate share of the increase in the costs of operating the building. For financial reporting purposes, the Board is recognizing rental expense evenly during the 10-year lease term at \$16,105 a month. The Board is required to maintain an irrevocable letter of credit of \$18,700, in lieu of a security deposit, payable to the lessor as part of the lease agreement. The lease may be renewed at the Board's option, for a period of five years, in accordance with the terms set forth in the lease agreement.

Total lease expense for office space and equipment for the years ended September 30, 1985 and 1984, was \$236,838 and \$91,700, respectively.

**4. Retirement plans**

The Board has a defined-contribution retirement plan. Participation in the plan is voluntary, and all employees are eligible to participate upon attaining a minimum length of service. The Board makes contributions to an insurance company based on a percentage of the salaries of covered employees and their lengths of service. Retirement plan costs are funded as they accrue. Employees may also make voluntary contributions. Costs of the plan were approximately \$41,900 in 1985 and \$37,200 in 1984.

During 1985, the Board adopted a deferred compensation plan which covers all employees. The Board contributes \$.50 for every \$1 contributed by an employee, with a maximum Board contribution of 2% of the employee's annual salary. The cost of this plan was approximately \$6,000 in 1985.

Continued

**MUNICIPAL SECURITIES RULEMAKING BOARD  
NOTES TO FINANCIAL STATEMENTS**

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5. Income taxes

Under provisions of the Internal Revenue Code and applicable income tax regulations of the District of Columbia, the Board is exempt from taxes on income other than unrelated business income. No provision for income taxes is required as of September 30, 1985 and 1984, since the Board had no unrelated business income.