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March–May

May 1 —Comments due on G-32 new issue disclosures draft amendments

Pending—Effective date of:

- G-12 and G-15 amendments on automated comparison, clearance and settlement (G-12(f)(i) and G-15(d)(ii) August 1, 1984) (G-12(f)(ii) and G-15(d)(iii) February 1, 1985)
- G-15 amendment on transactions in zero coupon, compound interest, and multiplier securities (September 1, 1984)

Pending—SEC approval of:

- G-12 amendments on CUSIP number discrepancies
- G-12 amendments on reclamation
- G-12 amendments on inter-dealer deliveries in book-entry form
- G-12 and G-15 amendments on automated clearance
- G-15 amendments on standards of delivery to customers

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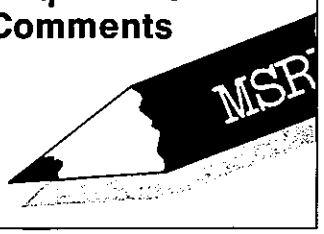
Request For Comments



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Rules G-8, G-9 and G-32

Comments Requested on Draft Amendments Pertaining to Disclosures on New Issues and Recordkeeping

Introduction

Rule G-32 prohibits a municipal securities broker or dealer from selling new issue municipal securities to a customer unless, at or prior to sending the final confirmation of the transaction, a copy of the final official statement, if one is prepared by or on behalf of the issuer and, in the case of negotiated sales, certain additional written information concerning the underwriting arrangements[1] are provided to the customer.[2] With respect to delivering official statements to customers, if an issuer fails to supply a sufficient number of copies of official statements, it is incumbent on a dealer to reproduce the official statement at its own expense. These requirements apply to all municipal securities brokers and dealers who sell new issue securities, not solely to underwriters of the issue. The rule is designed to ensure that a purchaser of new issue securities be provided with all available information relevant to his investment decision.

In January 1983, the Board published frequently asked questions about rule G-32 to assist the industry in complying with the requirements of the rule. Since that time the Board has received information, including complaints from purchasers of new issue securities, that some members of the industry may not be complying with the requirements of the rule. The Board has advised the enforcement agencies of its concern that this rule be vigorously enforced. In addition, the Board is considering adopting amendments to its rules to facilitate compliance with and enforcement of rule G-32. The Board requests comments on the draft amendments which are summarized below.

Summary of Draft Amendments

Rule G-32 requires municipal securities dealers to deliver to customers official statements, if prepared by or on behalf of the issuer, for new issue securities sold during the "underwriting period." Rule G-11 defines "underwriting period" as:

> the period commencing with the first submission to a syndicate of an order for the purchase of new issue municipal securities or the purchase of such securities from the issuer, whichever first occurs, and ending at such time as the issuer delivers the securities to the syndicate or the syndicate no longer retains an unsold balance of securities, whichever last occurs.

The Board is concerned that it may be difficult for municipal securities dealers who sell new issue securities but who are not members of the syndicate to know exactly when the underwriting period begins and ends for the purposes of sending official statements. The draft amendments to rule G-32 seek to alleviate this uncertainty by requiring delivery of an official statement in connection with a sale of new issue securities for a 40-day period commencing with the date of sale. The Board specifically requests comments whether the proposed 40-day period is adequate.[3]

When a syndicate maintains an unsold balance beyond the 40-day period, the draft amendment would require syndicate members to deliver an official statement for sales occurring after the 40-day period until the account is closed. The rationale for this provision is that syndicate members know that the account is still active and continue to be engaged in the primary distribution of the securities.

The Board welcomes comments on the draft amendments from all interested persons. In particular, the Board solicits the views of institutional and individual customers regarding the provisions of the draft amendments. Letters of comment should be received by the Board on or before May 1, 1984, and should be sent to the attention of Angela Desmond, General Counsel. Written comments will be available for public inspection.

[1] In the case of a negotiated sale of new issue municipal securities, a dealer must deliver additional information disclosing the (i) underwriting spread; (ii) the amount of any fee received by the dealer as agent for the issuer in the distribution of the securities; and (iii) the initial offering price for each maturity in the issue that is offered or to be reoffered in whole or in part by the underwriters. The Board has stated that these disclosures may be made in the official statement, but if the final official statement is not available at the time of sending the final confirmation, a dealer must provide the information either on the confirmation of the transaction or in a separate document.

[2] These disclosures also must be provided to a dealer who purchases new issue securities upon its request.

[3] In selecting that time period, the Board reviewed the requirements of Sections 4 and 5 of the Securities Act of 1933 and rule 174 thereunder. Those provisions require that a broker-dealer (including an underwriter no longer acting as an underwriter) deliver a prospectus for a corporate security on or before completion of a transaction to a purchaser who buys the securities within 90 days of the effective date of the registration in the case of an initial public offering, and 40 days after the effective date in the case of a subsequent public offering by the issuer.

The draft amendments to rule G-32 also would require that, if no official statement is prepared by the issuer or its agent, a written statement of that fact must be provided to customers. The Board believes that this provision, coupled with the proposed official statement delivery period, should facilitate compliance with the rule by industry members.

The Board also requests comments on draft amendments to rules G-8 and G-9 which would require dealers to keep a record of deliveries of official statements and other disclosures required under rule G-32. These disclosures include the official statement or notice that no official statement has been prepared (described above), as well as, in the case of negotiated underwritings, the information concerning underwriting arrangements. The draft amendment to rule G-8 would require a record of deliveries of the rule G-32 disclosures and retention of a copy of any notice or other material (other than a copy of an official statement) that is sent. The Board is proposing that these records be retained for a period of not less than three years since most other transaction-related information as well as syndicate records must be kept for a three year period under rule G-9. The Board is considering adopting these recordkeeping requirements in part to facilitate the compliance inspections of rule G-32 by the enforcement agencies. The Board requests comments whether adequate means currently exist to facilitate enforcement of rule G-32 and whether the draft recordkeeping requirement would encourage dealers to initiate procedures for delivering the disclosures required under rule G-32.

March 9, 1984

Text of Draft Amendments*

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

(a) Description of Books and Records Required to be Made. Except as otherwise specifically indicated in this rule, every municipal securities broker and municipal securities dealer shall make and keep current the following books and records, to the extent applicable to the business of such municipal securities broker or municipal securities dealer:

(i) through (xii) No change.

(xiii) Records Concerning Deliveries of Official Statements. A record of the deliveries of the disclosures required under rule G-32, together with a copy of any notice that no official statement had been prepared, or other material concerning the underwriting arrangements (other than a notice or document prepared by the issuer or an agent of the issuer) that was delivered.

Rule G-9. Preservation of Records

(a) No change.

(b) Records to be Preserved for Three Years. Every municipal securities broker and municipal securities dealer shall preserve the following records for a period of not less than three years:

(i) the subsidiary records described in rule G-8(a)(iv);

(ii) the records of put options and repurchase agreements described in rule G-8(a)(v);

(iii) the records relating to agency transactions described in rule G-8(a)(vi);

(iv) the records of transactions as principal described in rule G-8(a)(vii);

(v) the copies of confirmations and other notices described in rule G-8(a)(ix);

(vi) the customer account information described in rule G-8(a)(xi), provided that records showing the terms and conditions relating to the opening and maintenance of an account shall be preserved for a period of at least six years following the closing of such account;

(vii) if such municipal securities broker or municipal securities dealer is subject to rule 15c3-1 under the Act, the records described in subparagraphs (a)(4)(iv) and (vi) and (a)(11) of rule 17a-3 and subparagraphs (b)(5) and (b)(8) of rule 17a-4 under the Act;

(viii) the following records, to the extent made or received by such municipal securities broker or municipal securities dealer in connection with its business as such municipal securities broker or municipal securities dealer and not otherwise described in this rule:

(A) check books, bank statements, cancelled checks, cash reconciliations and wire transfers;

(B) bills receivable or payable;

(C) all written communications received and sent, including interoffice memoranda, relating to the conduct of the activities of such municipal securities broker or municipal securities dealer with respect to municipal securities; and

(D) all written agreements entered into by such municipal securities broker or municipal securities dealer, including agreements with respect to any account; and

(E) all powers of attorney and other evidence of the granting of any authority to act on behalf of any account, and copies of resolutions empowering an agent to act on behalf of a corporation.

(ix) all records relating to fingerprinting which are required pursuant to paragraph (e) of rule 17f-2 under the Act.

(x) all records of deliveries of written disclosures and those disclosures required to be retained as described in rule G-8(a)(xiii).

(c) through (g) No change.

Rule G-32. Disclosures in Connection with New Issues

(a) Disclosure Requirements. No municipal securities broker or municipal securities dealer shall sell, whether as principal or agent, any new issue municipal securities to a customer unless, at or prior to sending a final written confirmation of the transaction to the customer indicating money amount due, such municipal securities broker or municipal securities dealer sends to the customer;

(i) a copy of the official statement in final form ~~voluntarily furnished~~ prepared by or on behalf of the issuer (or an abstract or other summary of such statement which is

*Underlining indicates new language; broken line indicates deletions.

prepared by such municipal securities broker or municipal securities dealer) or if no official statement was prepared by or on behalf of the issuer, a written statement stating that fact; and

(ii) in connection with a negotiated sale of new issue municipal securities, the following information concerning the underwriting arrangements:

(A) the underwriting spread;

(B) the amount of any fee received by the municipal securities broker or municipal securities dealer as agent for the issuer in the distribution of the securities; and

(C) the initial offering price for each maturity in the issue that is offered or to be offered in whole or in part by the underwriters.

In the event an official statement in final form ~~is not available at~~ has not been prepared by the time the final confirmation indicating money amount due is sent to a customer, an official statement in preliminary form, if any, shall be sent to the customer, provided that an official statement in final form, or an abstract or summary thereof, must be sent to the customer promptly after such official statement is prepared ~~becomes available to the municipal securities broker or municipal securities dealer~~. Every municipal securities broker or municipal securities dealer shall promptly furnish the documents and information referred to in this section (a) to any broker, dealer or municipal securities dealer to which it sells new issue municipal securities, upon the request of such broker, dealer or municipal securities dealer.

(b) Definition of New Issue Municipal Securities and Official Statement. For purposes of this rule, the following terms have the following meanings:

(i) the term "new issue municipal securities" shall mean securities of an issue that are sold by a municipal securities broker or municipal securities dealer to a customer ~~during the underwriting period defined in rule G-11 of the Board, and~~ on or before the 40th day after the date of sale as defined in rule G-11, or, in the case of a member of a syndicate, on or before the 40th day after the date of sale or the last day of the underwriting period (as defined in rule G-11), whichever is later.

(ii) the term "official statement" shall mean a document prepared by the issuer or its representatives setting forth, among other matters, information concerning the issuer and the proposed issue of securities. A notice of sale shall not be deemed to be an "official statement" for purposes of this rule.

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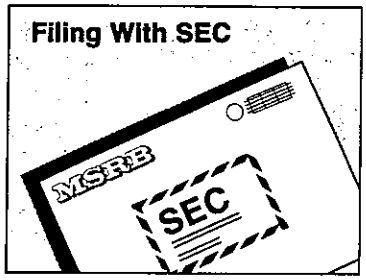

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Rule G-12

Amendments Filed on Reclamation of Inter-Dealer Deliveries

On March 15, 1984 the Board filed with the Securities and Exchange Commission certain proposed amendments to the provisions of Board rule G-12 concerning reclamations of inter-dealer deliveries. The amendments adopt certain substantive changes regarding reclamations of securities reported to be lost, stolen, fraudulent or counterfeit, and make other clarifying changes in the text of the rule. The proposed amendments will not become effective until 60 days following the date of Commission approval.

Background and Reasons for Proposed Rule Change

Board rule G-12 on uniform practice establishes certain standards concerning the confirmation, comparison, clearance and settlement of transactions between municipal securities brokers and municipal securities dealers. Section (g) of the rule sets forth provisions pertaining to the reclamation of inter-dealer deliveries of securities, including requirements concerning certain aspects of the reclamation procedure and time limits for reclamations due to various types of delivery problems. The existing provisions of the rule, however, do not, in certain cases, provide sufficient guidance concerning the specifics of the reclamation procedure or its effects; as a consequence, this guidance has been supplied through the adoption of numerous Board interpretations of this section. In addition, certain of the existing provisions of the rule (or previous Board interpretations) do not appear appropriate in the case of reclamations of securities which have been reported to be lost, stolen, fraudulent or counterfeit.

The proposed amendments would remedy these problems. With respect to the reclamation procedure, the proposed amendments would extensively revise paragraphs (iv), (v), and (vi) of section (g) of the rule to describe in more detail the actions necessary to accomplish a reclamation and the effects of a completed reclamation. The revised paragraphs provide (1) that reclamation (or rejection) is accomplished by returning securities previously delivered, (2) that only those securities on which a delivery problem exists need be returned to accomplish a reclamation, (3) that settlement of a reclamation shall be accomplished by substituting securities in "good delivery" form for those received on the reclamation or by return of the contract moneys previously paid at the time of the delivery being reclaimed, and (4) that reclamation reopens a "fail to deliver" on the reclaimed transaction which may be subsequently completed by a delivery of securities in "good delivery" form or by completion of a close-out procedure. The proposed amendments also detail the appropriate procedure for demanding a reclamation of securities (in circumstances in which the delivering party needs to obtain the return of securities previously erroneously delivered) and make certain technical changes in the language of the rule to distinguish between action by the party originally receiving the delivery (a "reclamation") and action by the original delivering party (a "demand for reclamation").

Proposed Revisions to Rule

The proposed amendments make several substantive revisions to the existing rule in the case of a reclamation of securities which have been reported to be lost, stolen, fraudulent or counterfeit, as follows:

(1) The proposed amendments would permit a dealer seeking to reclaim several securities reported to be lost, stolen, counterfeit or fraudulent to reclaim any of such securities which come into its possession, without having to delay the reclamation until it has possession of all of the securities which are the subject of the report. Although the proposed amendments would require (and previous Board interpretations have required) that for all other types of reclamations dealers must reclaim all of the securities needing to be reclaimed at the same time, the Board does not believe that such a requirement is appropriate in the case of a reclamation of lost, stolen, fraudulent or counterfeit securities. Since such securities typically do not have value to a dealer holding them (e.g., they generally cannot be used as collateral for a bank loan), a requirement that a dealer obtain all of the securities before reclaiming any of them would impose a serious financial burden on the dealer, particularly in cases where a large number of securities need to be reclaimed, or where the customers to whom the securities have been redelivered, who are *bona fide* purchasers, are unwilling to return the securities to the dealer.

(2) The proposed amendments would require that a dealer seeking to reclaim securities reported to be lost, stolen, fraudulent or counterfeit provide at the time of reclamation some evidence of the report that has been obtained from the

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

issuer of the securities, an agent of the issuer (e.g., the transfer agent or paying agent on the issue), or other authorized person (e.g., a law enforcement official or the facilities manager for the Commission's lost and stolen securities program). In view of the serious nature of a reclamation of securities reported to be lost, stolen, fraudulent or counterfeit, the Board believes that documentation evidencing the basis for the reclamation should be provided to the party obliged to accept the reclamation. The Board notes also that the provision of such documentation would eliminate the need for the party receiving the reclamation to verify that a report has been made; in the case of multiple reclamations of the same securities this removes a significant burden on the efficiency of the reclamation process.

In response to a September 1983 exposure draft of the proposed amendments one industry commentator suggested that a dealer seeking to reclaim a security reported to be lost or stolen be required to include with the reclamation, in lieu of any other type of documentation, a copy of the form evidencing the report of the loss or theft provided by the facilities manager of the Commission's lost and stolen securities program. The Board has not adopted this suggestion due to its belief that several kinds of documentary evidence are available that adequately substantiate that a report of loss or theft has been filed.

(3) The proposed amendments also would require, in the case of a reclamation of securities reported to be lost or stolen, that evidence be provided at the time of reclamation that the incident of loss or theft that is the subject of the report had occurred on or prior to the date of the delivery being reclaimed. Since the basis for a reclamation is the discovery of a problem with a delivery which if known at the time of delivery would have caused a rejection of the delivery, the Board believes that it is necessary that such evidence also be provided, to ensure that the reclamation is being made for a valid reason.

(4) The proposed amendments also incorporate into the text of the rule, at the suggestion of a commentator on the September 1983 exposure draft, the provisions of a Board interpretive notice dated June 16, 1978 permitting the use of a receipt from a law enforcement agency or other authorized person for purposes of reclaiming securities reported to be lost, stolen, fraudulent or counterfeit which have been seized by such agency or person.

March 19, 1984

Text of Proposed Amendments*

Rule G-12. Uniform Practice

(a) through (f) No change.

(g) Rejections and Reclamations.

(i) Definitions. For purposes of this section, the terms "rejection" and "reclamation" shall have the following meanings:

(A) "Rejection" shall mean refusal to accept securities which have been presented for delivery.

(B) "Reclamation" shall mean return by the receiving party of securities previously accepted for delivery.

(ii) Basis for Rejection. Securities presented for delivery may be rejected if the contra party fails to make a good delivery.

(iii) Basis for Reclamation and Time Limits. A reclamation may be made by the receiving party or a demand for reclamation may be made by the delivering party if, subsequent to delivery, information is discovered which, if known at the time of the delivery, would have caused the delivery not to constitute good delivery, provided such reclamation or demand for reclamation is made within the following time limits:

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

(1) not good delivery because a coupon, or an interest check in lieu thereof, required by this rule to accompany delivery was missing; or

(2) not good delivery because a certificate or coupon was mutilated in a manner inconsistent with the provisions of paragraphs (e)(vii) or (ix) hereof; or

(3) not good delivery because a legal opinion or other documents referred to in paragraph (e)(xi) hereof were missing; or

(4) not good delivery because the securities (which are issuable in both bearer and registered form) were delivered in registered form and were not identified as such at the time of trade.

(B) Reclamation or demand for reclamation because an interest check accompanying delivery was not honored shall be made within three business days following receipt by the purchaser of the notice of dishonor.

(C) Reclamation or demand for reclamation by reason of the following shall be made within 18 months following the date of delivery:

(1) irregularity in delivery, including, but not limited to, delivery of the wrong issue (i.e., issuer, coupon rate or maturity date), duplicate delivery, delivery to the wrong party or location, or over delivery; or

(2) refusal to transfer or deregister by the transfer agent due to presentation of documentation in connection with the transfer or deregistration which the transfer agent deems inadequate; or

(3) information pertaining to the description of the securities was inaccurate for either of the following reasons:

(i) information required by subparagraph (c) (v) (E) of this rule was omitted or erroneously noted on a confirmation, or

(ii) information material to the transaction but not required by subparagraph (c) (v) (E) of this rule was erroneously noted on a confirmation.

(D) Reclamation or demand for reclamation by reason of the following may be made without any time limitation:

(1) the security delivered is reported missing, stolen, fraudulent or counterfeit; or

(2) not good delivery because notice of call for less than the entire issue of securities was published on or prior to the delivery date and the securities were not identified as "called" at the time of trade.

*Underlining indicates additions; deleted material has been omitted.

The running of any of the time periods specified in this paragraph shall not be deemed to foreclose a party's right to pursue its claim via other means, including arbitration.

(iv) Procedure for Rejection or Reclamation.

(A) If a party elects to reject or reclaim securities, rejection or reclamation shall be effected by returning the securities to the party who had previously delivered them. In the case of a reclamation, the reclaiming party may reclaim all (or, in the case of a reclamation of securities reported to be missing, stolen, fraudulent or counterfeit, any part) of the securities which were not in "good delivery" form on the delivery date in lieu of reclaiming all of the securities delivered. In the case of a reclamation of securities reported missing, stolen, fraudulent or counterfeit, in the event that the securities have been seized by the issuer, an agent of the issuer, or a law enforcement official, reclamation by means of a presentation of a receipt for such securities executed by such person will meet the requirements of this subparagraph (A).

(B) The rejecting or reclaiming party shall also provide a written notice which contains sufficient information to identify the delivery to which the notice relates. The notice shall have attached to it a copy of the original delivery ticket or other proof of delivery, and shall state, to the extent not set forth on the attached document, the following:

(1) the name of the party delivering the securities;
(2) the name of the party receiving the securities;
(3) a description of the securities;
(4) the date the securities were delivered;
(5) the date of rejection or reclamation;
(6) the par value of the securities which are being rejected or reclaimed;
(7) in the case of a reclamation, the amount of money the securities are reclaimed for;
(8) the reason for rejection or reclamation; and
(9) the name and telephone number of the person to contact concerning the rejection or reclamation.

(C) A party demanding reclamation of securities shall send to the contra-party a notice demanding reclamation of the securities. Such notice shall have attached to it a copy of the original delivery ticket or other proof of delivery, and shall state, to the extent not set forth on the attached document, the information specified in items (1) through (9) of subparagraph (B) above.

(D) In the event of a reclamation or a demand for reclamation of a security reported missing, stolen, fraudulent or counterfeit, the reclaiming party or the party demanding reclamation shall also provide a document or documents made available by the issuer, an agent of the issuer, or other authorized person evidencing the report and, in the case of securities reported missing or stolen, evidencing that the loss or theft that is the subject of the report had occurred on or prior to the original delivery date.

(v) Manner of Settlement of Reclamation. Upon reclamation properly made pursuant to this rule, the party receiving the reclamation shall immediately give the party making the reclamation either the correct securities in proper form for delivery in exchange for the securities originally delivered, or the money amount (or the appropriate portion of the money amount) of the original transaction. A party receiving a notice of demand for reclamation shall reclaim the securities which are the subject of such notice as promptly as possible.

(vi) Effect of Rejection or Reclamation. Rejection or reclamation of securities shall not constitute a cancellation of the transaction. In the event of a reclamation of securities, unless otherwise agreed, the party to whom the securities have been reclaimed shall be deemed to be failing to deliver the securities, as of the original transaction settlement date, until such time as a proper delivery is made or the transaction is closed out in accordance with section (h) of this rule.

(h) through (l) No change.

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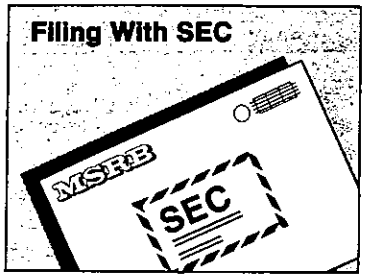

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Rule G-12

Amendments Filed on Inter-Dealer Deliveries of Book-Entry Form Securities

On March 15, 1984 the Board filed with the Securities and Exchange Commission amendments to rule G-12 on uniform practice concerning inter-dealer deliveries of certain types of securities which are available only in book-entry form and certain other technical matters. The substantive amendment would establish a standard for delivery of book-entry form securities in circumstances where the securities are not eligible for book-entry clearance through the facilities of a registered securities depository. The amendments will not become effective until 60 days after the date of Commission approval.

Board rule G-12(e) establishes certain standards regarding deliveries of securities between municipal securities brokers and dealers. Rule G-12(a)(i), however, provides that such standards do not apply to deliveries made through the facilities of a registered clearing agency:

> [A] transaction which is settled or cleared through the facilities of a registered clearing agency shall be exempt from the provisions of section (e) of this rule.

Therefore, book-entry deliveries through the facilities of a registered securities depository would not be subject to the provisions of section (e) of the rule; book-entry deliveries through the facilities of an entity not registered as a clearing agency, however, would be subject to the provisions of section (e).

The Board has become aware that certain securities are currently being traded and sold in the secondary market which are available only in book-entry form through a system managed by a book-entry agent (generally a commercial bank) which is not registered as a clearing agency. Since inter-dealer deliveries of such securities are subject to the "good delivery" provisions of section (e), the Board believes it appropriate to amend section (e) to include a provision setting forth such standards.

The proposed amendments include in section (e) of the rule a standard for deliveries of such securities between dealers. The proposed amendments require that a dealer making delivery of such securities must do so by arranging to have the securities transferred into the name of the purchasing dealer (or into such name as the purchasing dealer may direct) on the records maintained for this purpose by the book-entry agent for the securities. The delivering dealer therefore would be responsible, under this standard, for completing the book-entry transfer of the securities as a part of the transaction settlement process. The Board believes that such a standard is necessary to ensure the integrity of the clearance and settlement process and to establish appropriate safeguards against inadvertent or intentional misuse of this type of book-entry system.

On August 5, 1983 the Board released in exposure draft form an alternative version of this amendment which would have permitted deliveries of these securities to be accomplished by presentation by the selling dealer of the documentation necessary to accomplish the transfer, if such documentation were endorsed by the book-entry agent with a statement confirming that the selling party was reflected on the agent's records as the owner of the securities being sold. After its review of the negative comments received on this proposal, the Board has concluded that the delivery standard reflected in the August 1983 draft amendment was inappropriately permissive, and improperly placed on the purchasing dealer the burden of requiring use of a more secure delivery procedure in circumstances where the purchasing dealer deemed this necessary. As indicated above, the Board has concluded that a delivery standard such as that set forth in the August 1983 draft amendment does not provide in all cases the necessary safeguards for the clearance process, and that purchasing dealers should not be obliged under the Board's rules to forego such safeguards. The Board notes that, under the general provisions of rule G-12(e), the parties to a particular inter-dealer transaction may agree that delivery by means of the necessary documentation will be acceptable. The Board is of the view, however, that the burden of reaching an agreement at the time of trade should be placed on persons seeking to use this more permissive procedure, and that its rules should not compel the purchasing dealer to accept a delivery made by this procedure.

The proposed amendments also revise the current provisions of the rule relating to deliveries of securities in registered form to reflect the existing requirements under the Internal Revenue Code that most long-term municipal securities be issued solely in registered form.

March 19, 1984

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

Text of Proposed Amendments*

Rule G-12. Uniform Practice

(a) through (d) No change.

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

(i) through (v) No change.

(vi) Form of Securities.

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

(B) Book-Entry Form. Notwithstanding the other provisions of this section (e), with respect to a security which may be transferred only by bookkeeping entry, without the physical delivery of securities certificates, on books maintained for this purpose by a person who is not a registered clearing agent, a delivery of such security shall be made only by a book-entry transfer of the ownership of the security to the purchasing dealer or a person designated by the purchasing dealer.

(vii) through (xvi) No change.

(f) through (l) No change.

*Underlining indicates additions.

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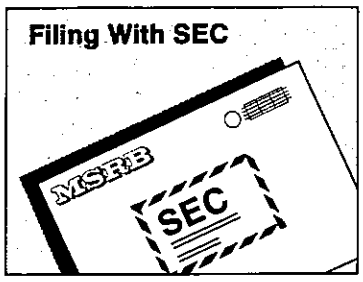

Route To:

- ☒ Manager, Muni. Dept.
- ☐ Underwriting
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- ☒ Compliance
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Rules G-12 and G-15

Amendments Filed on Automated Clearance of Transactions

On March 15, 1984 the Board filed with the Securities and Exchange Commission certain clarifying amendments to the provisions of Board rules G-12(f) and G-15(d) concerning the automated clearance of certain municipal securities transactions. Certain of the provisions being changed by the proposed amendments are scheduled to become effective on August 1, 1984, with the remainder of these requirements to become effective on February 1, 1985.

Rules G-12(f) and G-15(d) will require, when effective, that certain inter-dealer transactions and customer delivery/receipt vs. payment transactions be confirmed or compared (in the case of transactions involving a security assigned a CUSIP number) and settled via book-entry (in the case of transactions involving securities eligible for such settlement) through the facilities of a registered clearing agency or interfaced or otherwise linked registered clearing agencies. These provisions are applicable to transactions involving municipal securities brokers and dealers and customers who are deemed, for purposes of the rules, to be participants in or members of a registered clearing agency. Both rules specify that municipal securities brokers and dealers and customers who clear transactions through an agent who is a participant in or member of a registered clearing agency will be considered to be participants of that registered clearing agency for purposes of the rules' requirements; these persons are generally referred to as "indirect participants" of a registered clearing agency.

Since the Securities and Exchange Commission's approval of these rules in November 1983 the Board has received several inquiries concerning the extent to which non-participants who occasionally use the services of a participant agent will be considered to be participants of a registered clearing agency and therefore subject to the rules' requirements. In particular, certain industry members have noted that many dealers use agents to clear certain transactions in money center cities, but may use other agents to clear other transactions, or clear those other transactions themselves. Similarly, certain customers may use a participant clearing agent with respect to certain transactions, and a non-participant agent with respect to other transactions. These industry members have inquired whether the use by such a person of an agent who is a participant of a registered clearing agency to clear certain transactions is sufficient to make that person an indirect participant of the registered clearing agency, and therefore potentially subject to the requirements of rules G-12(f) and/or G-15(d), with respect to all of its transactions (including transactions which might not otherwise be cleared through the participant agent).

Upon consideration the Board has concluded that it would be desirable to limit the application of the requirements of rules G-12(f) and G-15(d) in the case of these indirect participants at the time these requirements first become effective. The Board believes that the requirements of rules G-12(f) and G-15(d) should apply to such persons only in the case of transactions otherwise subject to the rules which are cleared through the participant agent, and, accordingly, has adopted the proposed amendments to clarify this point in the rules. In the case of transactions cleared through a participant agent, therefore, indirect participant dealers would generally be required, as of August 1, 1984, to submit data concerning any transaction with another participant organization involving a municipal security assigned a CUSIP number to a registered clearing agency (presumably through the facilities of the participant agent) for automated comparison or confirmation of such transaction; indirect participant customers would be required to affirm any delivery/receipt vs. payment transaction so confirmed. As of February 1, 1985, these indirect participants would also be required to settle such transactions via book-entry, if the securities involved in the transaction are eligible for book-entry settlement. Under the proposed amendments, however, these persons would not be considered to be indirect participants with respect to transactions not cleared through the participant agent (e.g., transactions which they clear themselves) and, consequently, would not be subject to the requirements of rules G-12(f) and/or G-15(d) with respect to such transactions.

The Board believes that this approach is appropriate during the initial implementation of the rules over the next year. The Board continues to believe, however, that the use of automated clearance systems with respect to municipal securities transactions will provide significant benefits to the municipal securities industry generally. Accordingly, the Board intends to monitor the effects of the proposed amendments closely during the implementation of the requirements of rules G-12(f) and G-15(d). The Board further intends to

Questions concerning this notice may be directed to Donald F. Donahue, Deputy Executive Director.

consider and adopt amendments, subsequent to the effective dates of the existing provisions, which would at minimum require those dealers who are indirect participants only by virtue of their occasional use of a participant agent to clear certain transactions to use the automated confirmation or comparison systems with respect to all transactions otherwise subject to these rules.

Inquiries About Other G-12(f) and G-15(d) Requirements

The Board has also recently received inquiries from dealers and other interested persons concerning other aspects of the requirements of rules G-12(f) and G-15(d), as follows:

Use of Institutional Delivery system on inter-dealer transactions.—The Board has been advised that the Institutional Delivery (ID) system offered by the registered securities depositories for the automated confirmation of customer transactions will be made available to certain organizations (generally bank dealers) who are depository-only participants for their use in submitting data on inter-dealer transactions to an automated comparison system. The Board has been asked whether, if the ID system is made available to such persons for this purpose, the requirements under rule G-12(f) for the use of automated comparison systems will be applicable to such persons. As the Board has previously stated, if the ID system is made available for this purpose, the automated comparison requirements of rule G-12(f) will apply to these persons.

Members of several depositories.—Certain persons have pointed out to the Board that many industry members are members of two or more securities depositories. These persons have indicated that transactions may be effected between two dealers who are both members of several depositories in securities which are eligible for book-entry settlement in only one of the depositories in which these dealers are members; they further noted that the depository in which the securities are eligible may not be the one which the dealer uses for most of its securities transactions and views as its "primary" depository. These persons have inquired whether the requirements under rules G-12(f) and G-15(d) for book-entry settlement of transactions in depository-eligible securities would apply to these transactions. The Board notes that, since the conditions set forth in the rules have been met (i.e., the securities are eligible for book-entry settlement at a depository in which both parties to the transaction are members), the requirements would be applicable.

"When issued" transactions.—Certain dealers have inquired whether the requirements in the rules for the use of automated confirmation or comparison systems would apply to transactions effected on a "when, as and if issued" basis. To the extent that securities trading on a "when, as and if issued" basis are eligible for confirmation or comparison through such systems, the requirements would apply.

Distinction between inter-dealer and customer transactions.—Several of the registered clearing agencies have advised the Board that many dealers do not distinguish between transactions with customers and transactions with other dealers for purposes of their own internal transaction processing activities. The registered clearing agencies noted that the automated systems used for confirming customer transactions or comparing inter-dealer transactions are different, and suggested that a dealer whose internal processing systems are unable to distinguish between these transactions may experience some problems in initial compliance with rules G-12(f) and G-15(d), since it may have difficulty with directing transactions to the appropriate automated confirmation or comparison system. The Board wishes to call the municipal securities industry's attention to this potential difficulty, and urges that dealers take steps to ensure that they address this possible problem during their preparation for the implementation of the requirements.

Information Available on Implementing Automated Clearance Systems

The Board reminds the industry that the requirements under rule G-12(f) and G-15(d) for the use of automated confirmation or comparison systems on transactions will become effective on August 1, 1984. At the request of the Board, the Public Securities Association has undertaken to assist the industry to prepare for implementation of these requirements, and its Ad Hoc Committee on Municipal Automation is currently working on this project. Information on this effort may be obtained by contacting PSA at (212) 466-1900.

Texts of Proposed Amendments*

Rule G-12. Uniform Practice

(a) through (e) No change.

(f) Use of Automated Comparison, Clearance, and Settlement Systems.

(i) Notwithstanding the provisions of sections (c) and (d) of this rule, with respect to a transaction in municipal securities which are eligible for comparison through the facilities of a clearing agency registered with the Securities and Exchange Commission, if both parties to such transaction are members in one or more of such clearing agencies (and such clearing agencies are interfaced or linked for comparison purposes), each party to the transaction shall submit to its clearing agency information concerning the transaction, as required by the clearing agency's rules, for purposes of automated trade comparison. The provisions of this paragraph (i) shall apply to transactions effected on or after August 1, 1984.

(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 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. The provisions of this paragraph (ii) shall apply to transactions effected on or after February 1, 1985.

(iii) For purposes of this section (f) a municipal securities broker or municipal securities dealer who clears a transaction[s] through an agent who is a member of a registered clearing agency or a registered securities

*Underlining indicates additions; brackets indicate deletions.

depository shall be deemed to be a member of such registered clearing agency or registered securities depository with respect to such transaction.

(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 broker, dealer or municipal securities dealer who is, or whose clearing agent with respect to such transaction is, a participant in a clearing agency registered with the Securities and Exchange Commission shall effect a transaction in any 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 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. The provisions of this paragraph (ii) shall apply to transactions effected on or after August 1, 1984.

(iii) No broker, dealer or municipal securities dealer who is, or whose clearing agent with respect to such transaction is, a participant in a clearing agency registered with the Securities and Exchange Commission shall effect a transaction in any 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 amount 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 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. The provisions of this paragraph (iii) shall apply to transactions effected on or after February 1, 1985.

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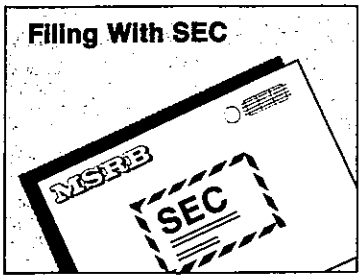

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Rule G-15

Amendments Filed on Standards of Delivery to Customers

On March 22, 1984 the Board filed with the Securities and Exchange Commission proposed amendments to the provisions of Board rule G-15 concerning the confirmation, clearance and settlement of transactions with customers. The proposed amendments establish standards for settlement dates on transactions with customers, and also set forth standards for deliveries of physical securities to customers. The proposed amendments will not become effective until 60 days following the date of Commission approval.

Similarities Between Rule G-12 and Proposed Rule G-15

Board rule G-12 on uniform practice sets forth certain requirements concerning inter-dealer transactions, including provisions specifying the required content of inter-dealer confirmations, provisions establishing standards for physical deliveries of securities between dealers, and provisions relating to other aspects of the clearance and settlement of inter-dealer transactions. In contrast, Board rule G-15 sets forth requirements concerning the content of transaction confirmations sent to customers, but historically has not set forth specific standards relating to the clearance and settlement of customer transactions.

The proposed amendments would incorporate into rule G-15 specific provisions, comparable to the equivalent provisions of rule G-12 on inter-dealer transactions, relating to the establishment of settlement dates on customer transactions (proposed section (b)) and deliveries of physical securities to customers (proposed section (c)). The provisions of proposed section (b) establish the fifth business day following the trade date as the standard settlement date for customer transactions, and provide for the establishment of settlement dates on "cash" and other exceptional transactions. The provisions of proposed section (c) establish certain standards relating to the proper delivery of securities to customers, covering such matters as the fungibility and specific identification of securities delivered, units of delivery, the form of the securities to be delivered, delivery of coupon and registered securities, and similar matters.

Differences Between Rule G-12 and Proposed Rule G-15

As noted above, the standards for deliveries to customers set forth in the proposed amendments are substantially similar to those relating to the clearance and settlement of inter-dealer transactions set forth in rule G-12. The proposed amendments do, however, impose slightly different or additional delivery standards in certain cases, as follows:

(1) Proposed section (c) is, by its terms, applicable to deliveries made by municipal securities brokers and dealers to customers or persons other than the delivering broker or dealer acting as agent for the receiving customer. The proposed amendments make clear, however, that the delivery standards set forth therein are not applicable to deliveries made by customers or their agents to municipal securities brokers and dealers, nor is a customer barred under the proposed amendments from establishing delivery standards with respect to a particular transaction in addition to those specified in proposed section (c).

(2) Proposed subparagraph (c)(iv)(B) sets forth standards for deliveries to customers of securities which are available only in book-entry form; an amendment to rule G-12 setting forth comparable standards for inter-dealer deliveries of certain types of such securities has recently been filed by the Board.

(3) Proposed paragraph (c)(xii) sets forth certain standards regarding the delivery of registered securities to customers that, in part, differ significantly from the standards applicable to inter-dealer deliveries. In particular, subparagraph (c)(xii)(A) provides that, in the case of a registered security delivered directly to a customer, the delivering municipal securities broker or dealer shall deliver a security "registered in the customer's name or in such name as the customer shall direct." In the case of a delivery of registered securities to a person acting as agent for the customer, however, subparagraph (c)(xii)(B) of the proposed amendments permits delivery of registered securities in "good delivery" form, as well as securities registered in the name of (or as directed by) the customer. The standards for "good delivery" form are specified in items (1) through (6) of the subparagraph, and are the same as those applying to inter-dealer deliveries.

This requirement is substantially the same as that set forth in the August 1983 exposure draft of the proposed amendments. One commentator disagreed with the exposure draft proposal regarding the delivering of registered securities, suggesting that the delivering municipal securities broker

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

or dealer should be responsible for registering the securities as directed by the customer regardless of whether the delivery is made directly to the customer or to an agent acting on the customer's behalf. The Board continues to believe that regulatory action to place the burden of transferring securities on a customer's behalf on the delivering municipal securities professional is appropriate only in circumstances where the customer would otherwise have to undertake the often complex and difficult transfer process itself. In circumstances where the customer uses an agent to clear its securities transactions and perform other safekeeping and securities handling functions the Board does not believe it necessary to interfere in this clearing arrangement by imposing the transfer burden on the delivering dealer; the Board notes that the rule would still permit the customer to require the dealer to handle the transfer function by agreement at the time of trade.

(4) The proposed amendments do not include provisions paralleling certain of the requirements of rule G-12 regarding deliveries on inter-dealer transactions, in circumstances where the Board did not believe such provisions would be appropriate for customer transactions.

March 23, 1984

Texts of Proposed Amendments*

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

(a) No change.

(b) Settlement Dates.

(i) Definitions. For purposes of this rule, the following terms shall have the following meanings:

(A) Settlement Date. The term "settlement date" shall mean the day used in price and interest computations, which shall also be the day delivery is due unless otherwise agreed by the parties.

(B) Business Day. The term "business day" shall mean a day recognized by the National Association of Securities Dealers, Inc. as a day on which securities transactions may be settled.

(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 all other transactions, a date agreed upon by both parties.

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

(i) Securities Delivered.

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

(B) CUSIP Numbers.

(1) The securities delivered on a transaction shall have the same CUSIP number as that set forth on the confirmation of such transaction pursuant to the requirements of subparagraph (a)(i)(F) of this rule; provided, however, that for purposes of this item (1), a security shall be deemed to have the same CUSIP number as that specified on the confirmation (a) if the number assigned to the security and the number specified on the confirmation differ only as a result of a transposition or other transcription error, or (b) if the number specified on the confirmation has been assigned as a substitute or alternative number for the number reflected on the security.

(2) A new issue security delivered by an underwriter who is subject to the provisions of rule G-34 shall have the CUSIP number assigned to the security imprinted on or otherwise affixed to the security.

(ii) Delivery Ticket. A delivery ticket shall accompany the delivery of securities. Such ticket shall contain the information set forth in subparagraphs (A), (B), (D) through (H), (M) and (O) of paragraph (a)(i) and, to the extent applicable, the information set forth in subparagraphs (A), (B), (C), (E), (F) and (G) of paragraph (a)(iii).

(iii) Units of Delivery. Delivery of bonds shall be made in the following denominations:

(A) for bearer bonds, in denominations of $1,000 or $5,000 par value; and

(B) for registered bonds, in denominations which are multiples of $1,000 par value, up to $100,000 par value. Delivery of other municipal securities shall be made in the denominations specified on the confirmation as required pursuant to paragraph (a)(iii) of this rule.

(iv) Form of Securities.

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

(B) Book-Entry Form. Notwithstanding the other provisions of this section (c), a delivery of a book-entry form security shall be made only by a book-entry transfer of the ownership of the security to the purchasing customer or a person designated by the purchasing customer. For purposes of this subparagraph a "book-entry form" security shall mean a security which may be transferred only by bookkeeping entry, without the issuance or physical delivery of securities certificates, on books maintained for this purpose by a registered clearing agency or by the issuer or a person acting on behalf of the issuer.

(v) Mutilated Certificates. Delivery of a certificate which is damaged to the extent that any of the following is not ascertainable:

*All the language of rule G-15 (b) and (c) below is new.

(A) name of issuer;
(B) par value;
(C) signature;
(D) coupon rate;
(E) maturity date;
(F) seal of the issuer; or
(G) certificate number

shall not constitute good delivery unless validated by the trustee, registrar, transfer agent, paying agent or issuer of the securities or by an authorized agent or official of the issuer.

(vi) Coupon Securities.

(A) Coupon securities shall have securely attached to the certificate in the correct sequence all appropriate coupons, including supplemental coupons if specified at the time of trade, which in the case of securities upon which interest is in default shall include all unpaid or partially paid coupons. All coupons attached to the certificates must have the same serial number as the certificate.

(B) Anything herein to the contrary notwithstanding, if securities are traded "and interest" and the settlement date is on or after the interest payment date, such securities shall be delivered without the coupon payable on such interest payment date.

(C) If delivery of securities is made on or after the thirtieth calendar day prior to an interest payment date, the seller may deliver to the purchaser a draft or bank check of the seller or its agent, payable not later than the interest payment date or the delivery date, whichever is later, in an amount equal to the interest due, in lieu of the coupon.

(vii) Mutilated or Cancelled Coupons. Delivery of a certificate which bears a coupon which is damaged to the extent that any one of the following cannot be ascertained from the coupon:

(A) title of the issuer;
(B) certificate number;
(C) coupon number or payment date (if either the coupon number or the payment date is ascertainable from the coupon, the coupon will not be considered mutilated); or
(D) the fact that there is a signature;

or which coupon has been cancelled, shall not constitute good delivery unless the coupon is endorsed or guaranteed. In the case of damaged coupons, such endorsement or guarantee must be by the issuer or by a commercial bank. In the case of cancelled coupons, such endorsement or guarantee must be by the issuer or an authorized agent or official of the issuer, or by the trustee or paying agent.

(viii) Delivery of Certificates Called for Redemption. A certificate for which a notice of call has been published on or prior to the delivery date shall not constitute good delivery unless the securities are identified as "called" at the time of trade or the notice of call is applicable to the entire issue of securities. For purposes of this subparagraph an "entire issue of securities" shall mean securities of the same issuer having the same date of issue, maturity date and coupon rate.

(ix) Delivery Without Legal Opinions or Other Documents. Delivery of certificates without legal opinions or other documents legally required to accompany the certificates shall not constitute good delivery unless identified as "ex legal" at the time of trade.

(x) Insured Securities. Delivery of certificates for securities traded as insured securities shall be accompanied by evidence of such insurance, either on the face of the certificate or in a document attached to the certificate.

(xi) Endorsements for Banking or Insurance Requirements. A security bearing an endorsement indicating that it was deposited in accordance with legal requirements applicable to banking institutions or insurance companies shall not constitute good delivery unless it bears a release acknowledged before an officer authorized to take such acknowledgements and was designated as a released endorsed security at the time of trade.

(xii) Delivery of Registered Securities.

(A) Delivery to the Customer. Registered securities delivered directly to a customer shall be registered in the customer's name or in such name as the customer shall direct.

(B) Delivery to an Agent of the Customer. Registered securities delivered to an agent of a customer may be registered in the customer's name or as otherwise directed by the customer. If such securities are not so registered, such securities shall be delivered in accordance with the following provisions:

(1) Assignments. Delivery of a certificate in registered form must be accompanied by an assignment on the certificate or on a separate bond power for such certificate, containing a signature or signatures which correspond in every particular with the name or names written upon the certificate, except that the following shall be interchangeable; "and" or "&"; "Company" or "Co."; "Incorporated" or "Inc."; and "Limited" or "Ltd."

(2) Detached Assignment Requirements. A detached assignment shall provide for the irrevocable appointment of an attorney, with power of substitution, a full description of the security, including the name of the issuer, the maturity date and interest date, the bond or note number, and the par value (expressed in words and numerals).

(3) Power of Substitution. When the name of an individual or firm has been inserted in an assignment as attorney, a power of substitution shall be executed in blank by such individual or firm. When the name of an individual or firm has been inserted in a power of substitution as a substitute attorney, a new power of substitution shall be executed in blank by such substitute attorney.

(4) Guarantee. Each assignment, endorsement, alteration and erasure shall bear a guarantee acceptable to the transfer agent or registrar.

(5) Form of Registration. Delivery of a certificate accompanied by the documentation required in this subparagraph (B) shall constitute good delivery if the certificate is registered in the name of:

(a) an individual or individuals;
(b) a nominee;
(c) a member of a national securities exchange

whose specimen signature is on file with the transfer agent or any other municipal securities broker or municipal securities dealer who has filed specimen signatures with the transfer agent and places a statement to this effect on the assignment; or

(d) an individual or individuals acting in a fiduciary capacity.

(6) Certificate in Legal Form. Good transfer of a security in legal form shall be determined only by the transfer agent for the security. Delivery of a certificate in legal form shall not constitute good delivery unless the certificate is identified as being in such form at the time of trade. A certificate shall be considered to be in legal form if documentation in addition to that specified in this subparagraph (B) is required to complete a transfer of the securities.

(C) Payment of Interest. If a registered security is traded "and interest" and transfer of record ownership cannot be or has not been accomplished on or before the record date for the determination of registered holders for the payment of interest, delivery shall be accompanied by a draft or bank check of the seller or its agent, payable not later than the interest payment date or the delivery date, whichever is later, for the amount of the interest.

(D) Registered Securities In Default. If a registered security is in default (*i.e.*, is in default in the payment of principal or interest) and transfer of record ownership cannot be or has not been accomplished on or before the record date for the determination of registered holders for the payment of interest, an interest payment date having been established on or after the trade date, delivery shall be accompanied by a draft or bank check of the seller or its agent, payable not later than the interest payment date or the delivery date, whichever is later, for the amount of the payment to be made by the issuer, unless the security is traded "ex-interest."

(d) No change.

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Rule G-17

Use of Lotteries to Allocate Partial Calls of Securities Held in Safekeeping

The Board has received inquiries concerning the duty of municipal securities brokers and dealers to allocate partial calls fairly among customer securities held in safekeeping. In particular, it has come to the Board's attention that certain municipal securities dealers use lottery systems that include only customer positions and exclude the dealer's proprietary accounts when the call is exercised at a price below the current market value.

The Board recognizes that lottery systems are a proper method for allocating the results of a partial call. Fair dealing requires that all such lotteries treat dealer and customer accounts alike. The Board is of the view that a municipal securities dealer which uses a lottery that excludes the dealer's proprietary accounts when the call is exercised at a price below the current market value is acting in violation of rule G-17, the Board's fair dealing rule.[1]

March 6, 1984

Questions concerning this notice may be directed to Diane G. Klinke, Deputy General Counsel.

[1]Rule G-17 provides:
In the conduct of its municipal securities business, each broker, dealer, and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice

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Rules G-13, G-17, and G-30

Transactions in Municipal Securities Subject to Secondary Market Insurance or Other Credit Enhancement Features

It has come to the Board's attention that insurance companies are offering to insure whole maturities of issues of municipal securities outstanding in the secondary market. The Board understands that municipal securities professionals must apply for the insurance which, once issued, will remain in effect for the life of the security. The Board further understands that other credit enhancement devices also may be developed for secondary market issues.

The Board wishes to remind the industry of the application of rule G-17, the Board's fair dealing rule, in connection with transactions with customers in securities that are subject to secondary market insurance or other credit enhancement devices or in securities for which arrangements for such insurance or device have been initiated.[1] The Board is of the view that facts, for example, that a security has been insured or arrangements for insurance have been initiated, that will affect the market price of the security are material and must be disclosed to a customer at or before execution of a transaction in the security. In addition, the Board believes that a dealer should advise a customer if evidence of insurance or other credit enhancement feature must be attached to the security for effective transference of the insurance or device.[2]

The Board also wishes to remind the industry that under rule G-13, concerning quotations, all quotations relating to municipal securities made by a dealer must be based on the dealer's best judgment of the fair market value of the securities at the time the quotation is made. Offers to buy securities that are insured or otherwise have a credit enhancement feature, or for which arrangements for insurance or other credit enhancement have been initiated, must comply with rule G-13. Similarly, the prices at which these securities are purchased or sold by a municipal securities dealer must be fair and reasonable to its customers under Board rule G-30 on prices and commissions.

March 6, 1984

Questions concerning this notice may be directed to Angela Desmond, General Counsel.

[1]Rule G-17 provides:
in the conduct of its municipal securities business, each broker, dealer, and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.

[2]The Board has adopted amendments to rule G-15 which, among other things, require that deliveries to customers of insured securities be accompanied by some evidence of the insurance. These amendments are awaiting SEC approval.

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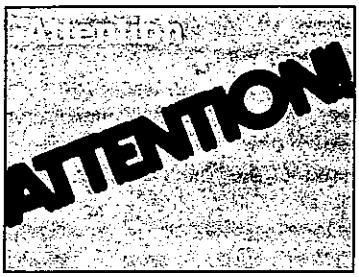

Route To:

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

Letters of Interpretation

Rule G-12—Close-Out Procedures: Transactions Involving Introducing Broker

I am writing in response to your recent letter concerning the use of the close-out provisions under Board rule G-12(h) with respect to a transaction in which one of the two parties "introduces" all transactions to a third, "clearing" dealer such as [name of clearing dealer deleted]. You indicate that [the clearing dealer] was recently involved in a situation in which a close-out notice was issued directly to a securities firm which uses [the clearing dealer] as its clearing dealer, introducing all of its transactions to [the clearing dealer]. Due to this firm's failure to notify [the clearing dealer] of the issuance of the close-out notice in a timely fashion [the clearing dealer] was unable to retransmit the notice to the dealer owing it the securities, and consequently was exposed to liability on the close-out. You express the view that [the clearing dealer's] inability to retransmit the notice was attributable to the fact that the notice was improperly directed to the introducing broker, rather than to [the clearing dealer]. You suggest that the Board's close-out rules should be amended to require that, in circumstances in which one party to an inter-dealer transaction introduces all trades to a clearing dealer, all communications with respect to a close-out of the transaction should be sent to the clearing dealer. I note that others have proposed that, in situations of this type, the clearing dealer should also have the authority to issue close-out notices on the transaction on behalf of the introducing broker.

The Board does not agree with your suggestion that a dealer purchasing securities from an introducing broker should be required to send all communications related to a close-out procedure to such broker's clearing dealer. In general, the Board has declined to include in the close-out rules requirements that certain specific persons or types of persons be contacted to handle aspects of the procedure; the Board believes that such requirements would inappropriately restrict dealers' flexibility in determining how best to handle close-out notices, and in establishing their own procedures for processing such notices.[1] In the specific case where the selling party in the transaction is an introducing broker, the Board is of the view that the adoption of your suggestion (which would have the effect of prohibiting the purchasing dealer from issuing a close-out notice directly to the introducing broker) inappropriately places on the purchasing dealer the burden of ensuring that a close-out notice is directed properly. Further, this approach improperly makes the purchasing dealer responsible for knowing the nature of the introducing broker's clearing arrangements (*i.e.*, that there is an "introducing" relationship, rather than simply a use of clearing services) and determining the proper way to proceed in light of those arrangements.

The responsibility for ensuring that a close-out notice is directed properly clearly rests and should rest with the introducing broker. In the situation you described the improper handling of the notice and the consequent exposure to [the clearing dealer] was the result of the introducing broker's failure to understand the significance of the notice and to respond appropriately. The Board continues to believe that it is incumbent upon municipal securities brokers and dealers, including introducing brokers, to ensure that their personnel understand the importance of prompt handling of close-out notices and know the procedure established by the dealer to accomplish this.

With respect to the issuance of a close-out notice by a clearing dealer acting on behalf of an introducing broker, the Board is of the view that (1) if the clearing dealer confirms inter-dealer transactions on behalf of the introducing broker, with the confirmation identifying both entities, (2) if all communications related to the close-out issued by the clearing dealer indicate that the clearing dealer is acting on behalf of the introducing broker, and (3) if the clearing dealer takes all responsibility for the issuance of notices, with the introducing broker not involving itself in the close-out procedure at any time, then the clearing dealer may issue close-out notices on the introducing broker's behalf. I note that the ability of the clearing dealer to issue notices on the introducing broker's behalf is also contingent upon the existence of the "introducing" relationship; a party acting solely as a dealer's clearing agent, without the presence of an "intro-

[1]See, for example, the discussion in Question 6 of the Board's *Manual on Close-Out Procedures:*

Q: When you say "call the seller," what does that mean? Whom should I call?

A: Every dealer has its own procedures to handle close-outs, so the Board doesn't require that a specific person, or a specific type of person, be contacted . . . . A number of dealers have the trader who made the trade contact the person from whom he or she bought the bonds . . . .

While we're on this subject, remember that sometimes you will be the recipient of a close-out notice. People in your office should know who handles close-outs for you and that they're responsible for referring calls and notices on close-outs to these people. If a close-out is mishandled in your office and, due to this error, you inadvertently fail to meet certain requirements (for instance, not retransmitting the notice to another dealer on time), you will be exposed to some risk on the close-out.

ducing" relationship, would not be able to issue close-out notices on transactions effected by the dealer.—*MSRB interpretation of March 5, 1984, by Donald F. Donahue, Deputy General Counsel.*

Rules G-12 and G-15—Callable Securities: Transactions in Construction Loan Notes

I am writing in response to your letter of February 3, 1984 concerning the application of certain of the confirmation requirements of Board rules G-12 and G-15 to transactions in construction loan notes. In your letter you note that both rules require that the confirmation of a transaction in callable securities effected on a yield basis set forth a dollar price that has been computed to the lowest of the price to the call, the price to the par option, or the price to maturity of the securities; rule G-15 requires that customer confirmations effected on a dollar price basis state the resulting yield computed to the lowest of the yield to call, to the par option, or to maturity. You inquire how these comparative calculation requirements would apply to a confirmation of a transaction in construction loan notes, which generally are callable "in whole" six months prior to the stated maturity date at par.

Your inquiry was referred to a committee of the Board which has responsibility for interpreting the Board's confirmation rules; that committee has authorized my sending you this response. The committee notes that a board interpretive notice of December 1980, which discussed the types of call features which should be used for purposes of the comparative calculation requirements, stated clearly that these requirements would apply to a transaction in a callable security if the issue of which the security is a part is callable "in whole" and if there is no restriction on the source of the funds which may be used to exercise the call. Since the call feature applicable to issues of construction loan notes is this type of "in whole" call feature, the committee is of the view that the comparative calculation requirements would apply. The confirmation of a transaction in a construction loan note effected on a yield basis, therefore, should state a dollar price computed to the lower of the price to this call feature or the price to maturity. Similarly, a customer confirmation of a transaction in these securities effected on a dollar price basis should set forth a yield to the lower of the yield to this call feature or a yield to maturity.—*MSRB interpretation of March 5, 1984, by Donald F. Donahue, Deputy General Counsel.*