

mail to the MSRB a completed Form G-40 setting forth the dealer's name, date, MSRB Registration Number, name of its E-mail Contact and his/her e-mail address, telephone number and Individual Central Registration Depository (CRD) Number, and the name, title, signature and telephone number of the person who prepared the Form G-40.³ Paragraph (b) also provides that the dealer may change its E-mail Contact or other information previously submitted by sending an amended Form G-40 to the MSRB by e-mail. Paragraph (c) requires each dealer to update information on its E-mail Contact as periodically requested and prescribed by the MSRB and to submit such information to the MSRB by e-mail.

The proposed rule change also amends Rule G-8, on books and records, to require that dealers maintain records reflecting copies of Form G-40 and any amended forms, as required by Rule G-40. The proposed rule change amends Rule G-9, on preservation of records, to require that dealers retain these records for a period of three years.

(b) The MSRB has adopted the proposed rule change pursuant to Section 15B(b)(2)(I) of the Exchange Act, which authorizes the MSRB to adopt rules that provide for the operation and administration of the MSRB.

B. Self-Regulatory Organization's Statement on Burden on Competition

The MSRB does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act since it would apply equally to all brokers, dealers and municipal securities dealers.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to

mail when the dealer completes its Rule A-12 submissions, as noted above.

³ The MSRB will assign passwords in order to limit access to each dealer's Form G-40 and to maintain the integrity of the information contained therein. Therefore, each dealer will be required to submit its initial Form G-40 by mail. The MSRB will then issue a password to the designated E-mail Contact that will be used to electronically submit to the MSRB any required updates and amendments to the form.

90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve the proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing including whether the proposed rule is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. Copies of the submissions, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of the filing will also be available for inspection and copying at the Board's offices. All submissions should refer to File No. SR-MSRB-2002-05 and should be submitted by June 4, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁴

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-45882; File No. SR-MSRB-2002-03]

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Granting Approval of Proposed Rule Change Relating to Professional Qualifications of Municipal Fund Securities Limited Principals

May 6, 2002.

On March 21, 2002, pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange

Act")¹ and Rule 19b-4 thereunder,² the Municipal Securities Rulemaking Board ("MSRB") filed with the Securities and Exchange Commission ("Commission") the proposed rule change relating to professional qualifications of municipal fund securities limited principals.

The Commission published the proposed rule change for comment in the **Federal Register** on March 26, 2002.³ The Commission received two comment letters relating to the forgoing proposed rule change. This order approves the proposal.

I. Description of the Proposed Rule Change

The MSRB proposed rule change consists of an amendment to Rule G-3, on professional qualifications, to address a new category of principals that serve permanently as municipal fund securities limited principals. Under MSRB Rule G-3, which governs professional qualifications, a broker, dealer or municipal securities dealer ("dealer") must have at least one municipal securities principal (and in some cases two municipal securities principals), even if the dealer's only municipal securities transactions are sales of municipal fund securities.⁴ In July 2001, MSRB amended Rule G-3 to provide a temporary alternative method for qualification of principals in connection with municipal fund securities.⁵ The amended rule provided relief to small dealers seeking to enter the market for municipal fund securities from Rule G-3's requirement to immediately obtain a municipal securities principal. Under the temporary provision, until July 31, 2002, if a dealer's municipal securities activities are limited exclusively to municipal fund securities and the dealer has fewer than eleven associated persons engaged in such activities, the dealer may fulfill its obligation to have a municipal securities principal by designating a general securities or investment company/variable contracts limited principal to act as a limited

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Release No. 34-45652 (April 3, 2002), 67 FR 15844.

⁴ A municipal fund security is defined in MSRB's Rule D-12 as a municipal security issued by an issuer that, but for section 2(b) of the Investment Company Act of 1940 (the "Investment Company Act"), would constitute an investment company within the meaning of the Investment Company Act. Section 2(b) exempts states and political subdivisions, and agencies, authorities, and instrumentalities thereof, from the Investment Company Act.

⁵ See SR-MSRB 2001-05; Release No. 34-44584 (July 23, 2001), 66 FR 39541 (July 31, 2001).

principal.⁶ During this period, any designated limited principal has all of the powers and responsibilities of a municipal securities principal under MSRB rules with respect to transactions in municipal fund securities. Under the current transition provision, on and after August 1, 2002, dealers effecting transactions in municipal fund securities are required to comply with the same municipal securities principal requirements applicable to all other dealers effecting transactions in municipal securities.

The MSRB acknowledges that many dealers that wish to participate in the market for municipal fund securities do not currently, and do not plan to, engage in any municipal securities activities other than with respect to municipal fund securities. Since these dealers will not participate in the market for municipal debt securities and the features of municipal fund securities differ significantly from those of debt securities, the MSRB believes that no investor protection purpose is served by requiring principals responsible for supervision of such firms' municipal fund securities activities to demonstrate their understanding of the application of MSRB rules other than with respect to municipal fund securities.

To qualify as a municipal fund securities limited principal would be by means of an examination consisting of questions on the broad range of MSRB-specific topics that are relevant to municipal fund securities activities.⁷ The examination would require that the individual taking it have previously or concurrently taken and passed the general securities principal qualification examination (Series 24) or investment company and annuity principal qualification examination (Series 26) administered by the National Association of Securities Dealers, Inc.

⁶ Dealers that have 11 or more associated persons engaged in municipal fund securities activities may also designate a general securities or investment company/variable contracts limited principal to act as a limited principal. If a dealer is required to have two municipal securities principals under Rule G-3(b)(iii), then it may count one such limited principal toward this numerical requirement but must still have one municipal securities principal qualified other than by reason of being a general securities or investment company/variable contracts limited principal. If any dealer having 11 or more associated persons engaged in municipal fund securities activities is permitted to have only one municipal securities principal by virtue of Rule G-3(b)(iii)(A), the numerical requirement may not be satisfied by designation of a limited principal.

⁷ Since the qualification examination would be tailored specifically to the application of MSRB rules to municipal fund securities, rather than to all types of municipal securities, the MSRB expects that this examination would not be as lengthy as the existing qualification examination for municipal securities principals (Series 53).

("NASD"). The qualification examination for municipal fund securities limited principals is scheduled to become available on October 1, 2002. MSRB staff is currently in the process of developing the qualification examination and will file the study outline and specifications with the Commission under separate cover.

An individual qualified as a municipal fund securities limited principal would be permitted to supervise only the municipal fund securities activities of the dealer and would have no authority to supervise the activities of the dealer with respect to any other type of municipal securities. However, an individual qualified as a municipal securities principal (Series 53) would continue to be qualified to supervise all municipal securities activities of the dealer, including activities relating to municipal fund securities.⁸ Thus, an individual wishing to supervise municipal fund securities activities could qualify to do so either by becoming: (i) a municipal securities principal through the municipal securities principal qualification examination (Series 53) or (ii) a municipal fund securities limited principal through this new qualification examination if the individual is already or concurrently becomes a general securities principal or investment company/variable contracts limited principal.

If a dealer's municipal securities activities are limited to municipal fund securities, the proposed rule change also would count all municipal fund securities limited principals toward the numerical requirement for principals regardless of the number of associated persons engaging in such activities. Thus, any dealer that does not engage in any municipal securities activities other than with respect to municipal fund securities could fully discharge its obligation with respect to municipal securities principals with individuals qualified as municipal fund securities limited principals.

Further, existing rule language indirectly permits investment company/variable contracts limited representatives (Series 6) to take the Series 53 examination to become qualified as municipal securities

⁸ The question bank for the Series 53 examination includes questions relating to municipal fund securities. Individuals taking the Series 53 examination must therefore become familiar with the application of MSRB rules to municipal fund securities.

principals.⁹ Although this was appropriate when there was no other provision under Rule G-3 for qualifying a principal to supervise municipal fund securities activities, the proposed rule change discontinues this method of qualification on October 1, 2002 when the new municipal fund securities limited principal qualification examination becomes available.¹⁰ An investment company/variable contracts limited representative would be able to qualify as a municipal fund securities limited principal by taking both the Series 26 examination and the new municipal fund securities limited principal examination.

In addition, the proposed rule change extends the existing temporary provision permitting general securities principals and investment company/variable contracts limited principals to supervise municipal fund securities activities from July 31, 2002 to December 31, 2002 in order to provide dealers with an adequate opportunity to prepare potential candidates for the new examination. During the extended transition period, the numerical requirement with respect to principals would be simplified so that all dealers, not just those with fewer than eleven associated persons engaged in municipal fund securities activities, could fully meet their principal requirements with principals acting in the temporary capacity permitted under the transition provisions. This rule change makes clear that, beginning on January 1, 2003, all municipal fund securities limited principals (including general securities principals and investment company/variable contracts limited principals supervising municipal fund securities activities under the temporary transition period who wish to continue such supervisory activities after December 31, 2002) must be qualified by taking the new qualification examination.

Finally, the MSRB rule change provides the NASD or any other appropriate regulatory agency the power to waive qualification requirements with respect to municipal fund

⁹ Rule G-3 permits an investment company/variable contracts representative to act as a municipal securities representative solely with respect to municipal fund securities.

¹⁰ Qualification of an investment company/variable contracts limited representative as a full municipal securities principal allows that individual to supervise any municipal securities activities, including debt securities. The MSRB is concerned that an individual who is solely qualified as an investment company/variable contracts limited representative prior to becoming a municipal securities principal may not have an adequate understanding of municipal debt securities to provide effective supervision under all circumstances.

securities limited principals, as with all other qualification categories. Under Rule G-3(g)(i), such waivers are to be granted solely in extraordinary cases.

II. Summary of Comments

The Commission received two comment letters on the proposal.¹¹ Of the two comment letters, one expresses support and the other opposes the creation of a municipal fund securities limited principal.

In favor of the MSRB proposal, the ICI letter states that the new classification of limited principals will provide "needed relief" to firms whose sole securities business consists of municipal fund securities.¹² ICI referenced its recommendation submitted in prior letter, commenting on the MSRB's July 2001 notice, that the MSRB provide temporary and extended relief until the MSRB administers its new municipal fund securities limited principal examination.¹³ Because their concern is addressed in the proposed rule change, the ICI extends its support to the MSRB.

The comment letter sent by Federated opposes the MSRB's establishment of the new permanent category of municipal fund securities limited principals by stating that it creates "unnecessary and inappropriate burdens".¹⁴ Federated asserts that the existing requirements already assure the proper supervision for municipal fund securities, because there is "virtually no substantive distinction between municipal fund securities and mutual funds". The imposition of new MSRB regulation burdens member firms with unnecessary registration requirements, additional costs and administrative encumbrances without adding investor protections.¹⁵ As an alternative, the Federated letter supports supervision of the municipal fund securities under the current registration and continuing education scheme of the NASD. To the extent it is necessary, the letter requests that the MSRB work with the NASD to incorporate changes to the NASD's educational scheme that address

municipal fund securities. Additionally, the Federated letter urges the MSRB to extend its current pilot to permit NASD mutual fund principals to supervise sales of municipals fund securities.¹⁶

The MSRB believes that the proposed rule change would in fact decrease dealers' regulatory burden. Without the amendment, dealers would be required to use fully qualified municipal securities principals to meet their Rule G-3 principal requirement.¹⁷ As stated above, the creation of the municipal fund securities limited principal category provides dealers with an alternative means of meeting this requirement. For dealers that do not otherwise engage in municipal securities activities, allowing their general securities principals or investment company principals to take a shorter, more focused examination than the Series 53 exam in order to qualify as a municipal fund securities principal should be less burdensome. The further reduction in regulatory burden that these commentators most likely desire—*i.e.*, no MSRB qualification requirements—is inappropriate since activities regulated by MSRB rules require ultimate supervision by someone who knows these rules.

III. Discussion

The MSRB believes that the proposed rule change is consistent with section 15B(b)(2)(A) of the Exchange Act, which provides that it is the MSRB's responsibility to propose and adopt rules which require that no municipal securities broker or municipal securities dealer shall effect any transaction in municipal securities unless, "such municipal securities broker or municipal securities dealer and every natural person associated with such municipal securities broker or municipal securities dealer meets such standards of training, experience, competence, and such other qualifications as the Board finds necessary or appropriate in the public interest or for the protection of investors."¹⁸

Section 15B(b)(2)(A) of the Exchange Act also provides that the MSRB may appropriately classify municipal

securities brokers and municipal securities dealers and their associated personnel and require persons in any such class to pass tests prescribed by the MSRB.

The Commission must approve a proposed MSRB rule change if the Commission finds that the proposal is consistent with the requirements set forth under the Exchange Act, the rule and regulations thereunder, which govern the MSRB.¹⁹ The language of section 15B(b)(2)(C) of the Exchange Act requires that the MSRB's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principals of trade, to foster cooperation and coordination with persons engaged in regulating, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market in municipal securities, and, in general, to protect investors and the public interest.²⁰

After careful review, the Commission finds that the MSRB's proposed rule change consisting of an amendment to Rule G-3, on professional qualifications, which relates to municipal fund securities limited principals, meets the statutory standard. The Commission believes that this proposed rule change is consistent with the requirements of the Exchange Act, and the rules and regulations thereunder. In addition, the Commission finds that the proposed rule is consistent with the requirements of section 15B(b)(2)(C) of the Exchange Act, set forth above.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Exchange Act,²¹ that the proposed rule change (File No. SR-MSRB-2002-03) be and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²²

Margaret H. McFarland,

Deputy Secretary.

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¹¹ See letter from John K. Forst, Law Offices of Dechert Price & Rhoads, to Jonathan G. Katz, Secretary, Commission, dated April 30, 2002 (enclosing letter from James F. Getz, President, Federated Securities Corp. ("Federated"), to Mr. Jonathan G. Katz, Secretary, Commission); letter from Tamara K. Reed, Associate Counsel, Investment Company Institute ("ICI"), to Mr. Jonathan G. Katz, Secretary, Commission, dated April 25, 2002.

¹² See ICI letter, note 11, *supra*.

¹³ *Id.* (citing letter from Tamara K. Reed, Associate Counsel, ICI, to Ernesto A. Lanza, Esquire, MSRB, dated January 15, 2002.)

¹⁴ See Federated letter, note 11, *supra*.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ Dealers selling mutual fund IRA accounts and municipal bond mutual funds are not required to comply with MSRB rules because these securities are not municipal securities and are instead subject to regulation under other regulatory schemes. In contrast, municipal fund securities are municipal securities and therefore are subject to MSRB rules and exempt from most other provisions of federal securities laws (such as the Securities Act of 1933 and the Investment Company Act).

¹⁸ 15 U.S.C. 78o-4(b)(2)(A).

¹⁹ Additionally, in approving this rule, the Commission notes that it has considered the proposed rule's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

²⁰ 15 U.S.C. 78o-4(b)(2)(C).

²¹ 15 U.S.C. 78s(b)(2).

²² 17 CFR 200.30-3(a)(12).