

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46380; File No. SR-MSRB-2002-07]

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Granting Approval of a Proposed Rule Change Relating to Rule G-14, on Reports of Sales or Purchases

August 19, 2002.

On July 3, 2002, pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act" or "Exchange Act"),¹ and Rule 19b-4 thereunder,² the Municipal Securities Rulemaking Board ("Board" or "MSRB") filed with the Securities and Exchange Commission ("Commission" or "SEC") a proposed rule change (File No. SR-MSRB-2002-07). The proposed rule change relates to MSRB Rule G-14, on Reports of Sales or Purchases.

The Commission published the proposed rule change for comment in the *Federal Register* on July 17, 2002.³ The Commission received one comment letter relating to the forgoing proposed rule change. The proposed rule change does not change the wording of Rule G-14. This order approves the Board's proposal.

I. Description of the Proposed Rule Change

To add greater transparency in the municipal securities market, the MSRB filed with the Commission the forgoing proposed rule change. The MSRB has a long-standing policy to increase price transparency in the municipal securities market, with the ultimate goal of disseminating comprehensive and contemporaneous pricing data. Since 1995, the MSRB has expanded the scope of the public transparency reports in several steps. Each step has provided industry participants and the public successively more information about the market.⁴

In May, 2001, the MSRB announced its plan to begin reporting trades in "real time" on a schedule coordinated

with the industry's timetable for migration to an environment of next-day settlement of securities transactions.⁵ To attain real-time reporting, the MSRB intends in the future to file an amendment to Rule G-14 to require dealers to report their trades within 15 minutes of the time they are effected. The planned implementation date for real-time reporting is now set for mid-2004.

Prior to the implementation of real-time transaction reporting, the MSRB intends to continue to increase transparency in the market using the currently available data. As its next step, the MSRB is now proposing to disseminate the Daily Comprehensive Report with a one-week delay. The proposed Report would contain details of all municipal securities transactions that were effected during the trading day one week earlier. Data about each trade on the proposed Report would be the same as that on the current Daily Comprehensive Transaction Report. For each trade, the proposed Report, like the current report, would show the trade date, the CUSIP number of the issue traded, a short issue description, the par value traded, the time of trade reported by the dealer, the price of the transaction, and the dealer-reported yield of the transaction, if any. Each transaction would be categorized as a sale by a dealer to a customer, a purchase from a customer, or an inter-dealer trade.

The current Daily Comprehensive Report began operation on November 1, 2001.⁶ The proposed Report, with a one-week delay, would replace the current report that has a two-week delay.

Description of Service

Like the current two-week delayed report, the new Report will be available daily to subscribers. Subscribers to the current two-week delayed report would continue to access the proposed Report via the Internet and download copies from the MSRB's computer using a password-protected FTP account. The MSRB expects that the proposed Report would be available within two weeks of approval by the Commission.

The MSRB will continue the established annual fee for the Service of \$2,000. The fee is structured approximately to defray the MSRB's costs for production of daily data sets, operation of telecommunications lines, and subscription maintenance. Subscription fees that have been paid

for the two-week delayed report will be applied toward the one-week delayed report.

To enable the MSRB to compile a comprehensive trades database for enforcement purposes, dealers report a small amount of data after trade date, and a few trades may be added, deleted or amended as late as a few weeks after trade date.⁷ To ensure that subscribers to the report have access to those trades, the MSRB will make available each day an "updated" report containing all trades effected one month previously. This will enable subscribers to see the effect of changes reported by dealers after the one-week report was disseminated.

II. Summary of Comments

The Commission received one comment letter addressing the proposed rule change.⁸ In addition to offering support for the proposed rule change, this letter provided suggestions on how to advance price transparency in the future.

The comment letter, from The Bond Market Association ("TBMA"), expressed strong support of the MSRB's initiative to decrease the time interval for transparency of all reported bonds.⁹ The TBMA expressed its belief that decreasing the dissemination of trade data to one-week delay, from two-weeks, may enhance the value of the data to all market participants. Moreover, the more current information would not confuse investors or adversely impact the municipal market.¹⁰ But, with its support of the proposal, the letter urges the MSRB to create a process for evaluating any adverse market impacts that may result from disseminating trade information for "very inactive bonds".¹¹ This process of evaluation would involve several critical questions relating to the objective and relevancy of "full transparency" in the municipal market.¹² TBMA believes that price dissemination on a next-day basis for all bonds that trade only once per day

⁷ See Release No. 34-43060 (July 20, 2000), 65 FR 46188-46189 (July 27, 2000) at note 7. Approximately one percent of the trades in the database have data submitted between one week and one month after trade date.

⁸ Letter from Frank Chin, Salomon Smith Barney, Chair, Municipal Executive Committee, The Bond Market Association, to Mr. Jonathan G. Katz, Secretary, Commission, dated August 8, 2002.

⁹ See *id.* at page 2.

¹⁰ See *id.*

¹¹ The TBMA letter makes reference to the recent Commission approval of the MSRB's proposed rule change that decreases the trade threshold for information dissemination to three trades per day from four trades. See Release No. 34-45861 (May 1, 2002) 67 FR 30989.

¹² See TBMA letter at page 3.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Release No. 34-46180 (July 10, 2002), 67 FR 47012.

⁴ The MSRB's report summarizing prices for issues that are frequently traded on the inter-dealer market began operation in 1995; in 1998, dealer-customer prices were added in a second summary report; in January 2000, a report with details of trades in frequently traded issues was added; in October 2000, a monthly comprehensive report, covering all transactions effected during the previous month, began operation; and in November 2001, a daily comprehensive report was begun, with trades effected two weeks earlier.

⁵ See "Real-Time Reporting of Municipal Securities Transactions," *MSRB Reports*, Vol. 21, No. 2 (July 2001) at 31-36.

⁶ See Release No. 34-44894 (October 2, 2001), 66 FR 51485 (October 9, 2001).

“would not necessarily provide useful information to investors and other market participants or could adversely affect liquidity and be misleading.”¹³ Furthermore, the TBMA believes that trading activity that is limited to a single trade may reflect insufficient market interest to justify dissemination.

III. Discussion

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 Act and the rules and regulations thereunder, which govern the MSRB.¹⁴ The language of Section 15B(b)(2)(C) of the 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.¹⁵

After careful review, the Commission finds that the MSRB’s proposed rule change relating to Rule G–14, on Reports of Sales or Purchases, meets the requisite statutory standard. The Commission believes that this proposed rule change is consistent with the requirements of the 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 Act, as set forth above.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Exchange Act,¹⁶ that the proposed rule change (File No. SR–MSRB–2002–07) be and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁷

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–46376; File No. SR–NASD–99–04]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 2 to the Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Microcap Initiative—Recommendation Rule

August 19, 2002.

I. Introduction

On February 19, 1999, the National Association of Securities Dealers, Inc. (“NASD” or “Association”), through its wholly owned subsidiary, NASD Regulation, Inc. (“NASD Regulation”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b–4 thereunder,² a proposed rule change that would require members to review current financial statements of, and current material business information about, an issuer prior to recommending a transaction to a customer in an over-the-counter (“OTC”) equity security.

The proposed rule change was published for comment in the **Federal Register** on March 1, 1999.³ The Commission received six comment letters on the Original Proposal. On January 11, 2002, the NASD filed Amendment No. 1 to the proposed rule change, which among other things addressed the issues raised by commenters.⁴ Amendment No. 1 was published for comment in the **Federal Register** on January 22, 2002.⁵ On July 26, 2002, the NASD filed Amendment No. 2 to the proposed rule change.⁶

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b–4.

³ See Securities Exchange Act Release No. 41075 (February 19, 1999), 64 FR 10037 (“Original Proposal”).

⁴ In the Original Proposal, the NASD proposed subparagraph (e) to NASD Rule 6740. That provision would have permitted a member to submit a certification to the NASD stating that the firm complied with the requirements of SEC Rule 15c2–11, 17 CFR 240.15c2–11, including the member’s review obligation, if the documents the firm was required to review were contained in the Commission’s Electronic Data Gathering and Retrieval System, in lieu of submitting a copy of the documents reviewed. This proposed rule text was deleted as part of Amendment No. 1, although the change was not reflected in the narrative portion of the Amendment.

⁵ See Securities Exchange Act Release No. 45277 (January 14, 2002), 67 FR 2937.

⁶ See Letter from Marc Menchel, Senior Vice President and General Counsel, NASD, to Katherine A. England, Assistant Director, Division of Market

The Commission received no comments regarding the proposal as amended. This order approves the proposed rule change, as amended.

II. Description of Proposal

To respond to concerns about abuses in the trading and sales of thinly traded, thinly capitalized securities (*i.e.*, microcap securities) quoted in the OTC market, NASD Regulation has proposed to amend NASD rules to include new NASD Rule 2315, entitled “Recommendations to Customers in OTC Equity Securities” (“Recommendation Rule” or “Rule”). In the view of NASD Regulation, the lack of reliable and current financial information about issuers of microcap securities can create the potential for fraud and manipulation.

The proposed rule would be limited to equity securities that are published or quoted in a quotation medium and that either: (1) Are not listed on Nasdaq or a national securities exchange, or (2) are listed on a regional securities exchange and do not qualify for dissemination of transaction reports via the Consolidated Tape (“covered securities”).⁷ The requirements in the Recommendation Rule is intended to supplement requirements under the federal securities laws and under NASD rules that a broker-dealer that recommends securities to its customers is required to have a reasonable basis for those recommendations.⁸ In addition, the proposed rule is not intended to act or operate as a presumption or as a safe harbor for purposes of determining suitability or for any other legal

Regulation (“Division”), Commission, dated July 26, 2002 (“Amendment No. 2). In Amendment No. 2, the NASD amended proposed NASD Rule 2315(a) to clarify that members conducting transactions in securities that are listed on a regional securities exchange, but do not qualify for dissemination of transaction reports via the Consolidated Tape, must comply with the review requirements of the Recommendation Rule if such securities are published or quoted in a quotation medium. The NASD also amended NASD Rule 2315(e)(1)(G)(2) to substitute “NASD” for the reference to “the Association” contained in the Rule.

⁷ “Quotation medium” is defined as a system of general circulation to brokers or dealers that regularly disseminates quotations or indications of interest of identified brokers or dealers; or a publication, alternative trading system or other device that is used by brokers or dealers to disseminate quotations or indications of interest to others. The Recommendation Rule is intended to cover equity securities that are published or quoted in a quotation medium and that either: (1) Are not listed on Nasdaq or a national securities exchange, or (2) are listed on a regional securities exchange and do not qualify for dissemination of transaction reports via the Consolidated Tape.

⁸ See NASD Rule 2310 (Suitability Rule), which requires a member to have reasonable grounds for believing that a recommendation to a customer is suitable based on facts disclosed, other security holdings and financial situation and needs.

¹³ See *id.* at page 2.

¹⁴ 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).

¹⁵ 15 U.S.C. 78o–4(b)(2)(C).

¹⁶ 15 U.S.C. 78s(b)(2).

¹⁷ 17 CFR 200.30–3(a)(12).