

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50294; File No. SR-MSRB-2004-02)

August 31, 2004

Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Approving Proposed Rule Change Relating to Amendments to the MSRB's Rule G-12(f) on Automated Comparison and G-14 on Transaction Reporting, and to the Implementation of a Facility for Real-Time Transaction Reporting and Price Dissemination

On June 2, 2004, the Municipal Securities Rulemaking Board ("MSRB" or "Board"), 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 relating to the MSRB's implementation of real-time transaction reporting and price dissemination. The proposed rule change was published for comment in the Federal Register on June 29, 2004.³ The Commission received one comment letter on the proposal.⁴ This order approves the proposed rule change.

I. Description of the Proposed Rule Change

The MSRB's proposed rule change relates to Rule G-12(f), on automated comparison, Rule G-14, on transaction reporting, and the implementation of a facility for real-time transaction reporting and price dissemination (the "Real-Time Transaction Reporting System" or "RTRS"). The purpose of the proposed rule change is to increase

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 49902 (June 22, 2004), 69 FR 38925 (June 29, 2004) ("Notice").

⁴ See letter to Jonathan G. Katz, Secretary, Commission, from Leslie M. Norwood, Vice President and Assistant General Counsel, The Bond Market Association ("TBMA"), dated July 20, 2004 ("TBMA Letter").

transparency in the municipal securities market and to enhance the surveillance database and audit trail of transaction data used by enforcement agencies. The proposed rule change to Rule G-14 would require brokers, dealers, and municipal securities dealers (“dealers”) to report transactions in municipal securities to RTRS within 15 minutes of the time of trade execution instead of by midnight on trade date, as is currently required. Upon receipt of this transaction data, RTRS would immediately perform automated error checking and would electronically disseminate prices, providing the municipal securities market with real-time transaction price transparency.

The MSRB expects the proposed RTRS facility for real-time collection and dissemination of transaction prices will become operational in January 2005, at which time MSRB would begin to disseminate transaction data electronically in real time. MSRB expects to make a second filing on the RTRS facility in the future, stating the date of effectiveness, describing the technical means of data dissemination, and proposing fees to be charged for RTRS data products.

The proposed RTRS facility would replace the existing Transaction Reporting System (TRS), which currently receives and disseminates transaction data in an overnight batch process. The proposed amendments to Rules G-12 and G-14 require dealer participation in RTRS and are designed to ensure that transactions are reported to RTRS in a timely manner.

II. Summary of Comments

The Commission received one comment letter addressing the proposed rule change.⁵ The TBMA Letter expressed support for the MSRB’s goals, but expressed

⁵ See supra note 4.

reservations regarding the proposal in its current form.⁶ Specifically, TBMA believes that all trades on the first day of trading in a new issue should be exempt from the requirement to report within 15 minutes of trade execution (i.e. real-time reporting).⁷ In addition, TBMA states that they “continue to express liquidity concerns for immediate dissemination of trades of bonds rated “BBB” or below in sizes over \$1 million.”⁸

A. New Issue Reporting

The proposed rule change generally would require dealers to report trades to the MSRB within 15 minutes, with certain limited exceptions. First, syndicate managers, syndicate members, and selling group members that effect trades in new issues on the first day of trading at the list offering price would be required to report such trades by the end of the first day of trading in the issue. Second, on a temporary basis, a dealer would be required to report trades within three hours of the time of trade if the CUSIP number and indicative data of the issue traded are not in the dealer’s securities master file, the dealer has not traded the issue in the previous year, and the dealer is not a syndicate manager or syndicate member for the issue. This provision would sunset automatically one year after RTRS implementation.

In its comment letter, TBMA reiterated its suggestion made in previous comment letters to the MSRB that all trades on the first day of a new issue be exempt from 15-minute reporting and, be submitted no later than end of day.⁹ In the proposed rule

⁶ See TBMA Letter, at 2.

⁷ See TBMA Letter, at 3.

⁸ See TBMA Letter, at 4.

⁹ See TBMA Letter, at 2 and 3.

change, MSRB acknowledged that the existing information dissemination services in the municipal securities market may not, in some cases, be capable of providing a dealer with such indicative information in a sufficiently timely manner for the dealer to update its securities master file, process the transaction, and then report the transaction in real-time.¹⁰ Therefore, the proposed rule change provides that when a dealer has not traded an issue within the past year, a three-hour trade reporting requirement will apply rather than a 15-minute reporting requirement.

The proposed rule change also states that on the first day of trading in a new issue, the three-hour exception will be available to most dealers because they will be trading the issue for the first time.¹¹ However, by the terms of the three-hour exception, it is not available to dealers in the underwriting group (i.e., the syndicate manager and syndicate members).¹² TBMA disagrees with this decision and states “we feel the exception is not adequate because it does not cover trades by a syndicate manager or syndicate member and sunsets after one year.”¹³ In the Notice, the MSRB stated that they intentionally made the three-hour exception temporary to help ensure that dealers, trade associations and information vendors will use the one-year period to respond to the need for more automated and timely updating of indicative data and that industry practice will evolve so that the purposes of real-time price transparency can be more fully realized for trades on the first day of trading in a new issue.¹⁴ Furthermore, the MSRB noted that

¹⁰ See supra note 3, at 38937.

¹¹ Id.

¹² Id.

¹³ See TBMA Letter, at 2.

¹⁴ See supra note 3, at 38937.

the three-hour exception should not be necessary for the syndicate manager and syndicate members because they do have, or should have, timely access to information on a new issue that they are underwriting.¹⁵

TBMA also noted that on “the first day trades are executed for a new issue, which is the day of formal award for a new issue, there will likely be trades reflecting that day's market environment, in addition to trades reflecting the booking of tickets at the prices agreed to by the original buyers days before.”¹⁶ TBMA argues that by mixing the two types of trade reports together, the prices would “not be any more or less informative if all trades in new issue were subject to end-of-day reporting.”¹⁷ With respect to the specific issue of “mixing” prices, the MSRB notes that syndicate and selling group trades done at the list price will be marked as such when they are disseminated.¹⁸

Consequently, there should be no confusion about what these prices represent. In addition, the MSRB has stated that it is reviewing general market practices with respect to new issue offerings, including issues related to pre-award orders and the use of conditional trading commitments made before the time of formal award trade. As part of

¹⁵ Although the three-hour exception is not available to dealers in the underwriting group, the proposed rule change provides another exception from the real-time reporting requirement for list-price transactions by syndicate and selling group members. Such trades are likely to be voluminous and all executed in a short period of time, so that a 15-minute reporting deadline could present substantial operational challenges. Because of the operational difficulties and because the price information (the list price of the issue) is generally already available in the market at the time of trade execution, the proposed rule change allows these transactions to be reported at end-of-day. Trades that are not at list price, however, do not qualify for this exception and will have to be reported within 15 minutes unless another exception is available. See supra note 3, at 38937.

¹⁶ See TBMA Letter, at 3.

¹⁷ Id.

¹⁸ See supra note 3, at 38937.

this process, the MSRB recently published a "Notice Requesting Comment on Draft Amendments to Rule G-34 to Facilitate Real-Time Transaction Reporting and Explaining Time of Trade for Reporting New Issue Trades."¹⁹

B. Liquidity Concerns

Finally, TBMA states "we continue to express liquidity concerns for immediate dissemination of trades of bonds rated "BBB" or below in sizes over \$1 million."²⁰

TBMA suggests further study of this market segment to assess effects on liquidity before disseminating trade prices in real-time.²¹ The MSRB noted in its filing that comment on this particular issue was mixed and that some investors expressed strong support for full transparency, specifically to include the market segment identified by TBMA.²² In light of these comments, the MSRB has weighed the potential for liquidity problems against the potential for transparency benefits and has concluded that any liquidity problems that may occur with respect to the issues in question are likely to be temporary and will resolve over time as market participants make adjustments in response to the more transparent environment.²³ The MSRB also believes that the potential for transparency benefits, such as more accurate pricing, lower transaction costs for investors and increased investor confidence, outweighs the potential for short-term liquidity problems.²⁴

¹⁹ See MSRB Notice 2004-18 (June 18, 2004), available at www.msrb.org.

²⁰ See TBMA Letter, at 4.

²¹ See TBMA Letter, at 3 and 4.

²² See *supra* note 3, at 38939.

²³ *Id.*

²⁴ *Id.*

III. Discussion and Commission Findings

The Commission has carefully reviewed the proposed rule change and comment letter, and finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to the MSRB²⁵ and, in particular, the requirements of Section 15B(b)(2)(C) of the Act and the rules and regulations thereunder.²⁶ Section 15B(b)(2)(C) of the Act requires, among other things, that the MSRB's rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal 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.

In particular, the Commission finds that the proposed rule change will provide the market with more efficient pricing information, enhance the surveillance database and audit trail of transaction data used by enforcement agencies, and enhance investor confidence in the market. The Commission believes that real-time price transparency will enhance investor confidence by providing, for the first time, a comprehensive and contemporaneous view of the municipal securities market to any interested party. The Commission also believes that the open availability of market prices should instill greater confidence that pricing mechanisms in the municipal securities market are fair, open, and efficient.

²⁵ 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).

²⁶ 15 U.S.C. 78o-4(b)(2)(C).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²⁷ that the proposed rule change (SR-MSRB-2004-02) be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁸

Margaret H. McFarland
Deputy Secretary

²⁷ 15 U.S.C. 78s(b)(2).

²⁸ 17 CFR 200.30-3(a)(12).