

Network Subsidiaries would be liable under rule 17f-5 (e.g., despite the exercise of reasonable care, Acts of God and the like).

4. With respect to the Agency Custody Arrangements, applicant will enter into a Subcustodian Agreement with each Exemptive Order Network Subsidiary pursuant to which applicant will delegate to the Exemptive Order Network Subsidiary such of applicant's duties and obligations as would be necessary to permit the Exemptive Order Network Subsidiary to hold in custody in the country in which it operates Assets of U.S. Investment Companies or their custodians. Each Subcustodian Agreement will provide an acknowledgement by the applicable Exemptive Order Network Subsidiary that it is acting as a foreign custodian for U.S. Investment Companies pursuant to the terms of the order requested hereby. Each Subcustodian Agreement will also explicitly provide that U.S. Investment Companies or their custodians, as the case may be, that have entered into a Custody Agreement with applicant will be third party beneficiaries of such Subcustodian Agreement, will be entitled to enforce the term thereof and will be entitled to seek relief directly against the applicable Exemptive Order Network Subsidiary so acting as foreign custodian or against applicant.

5. Applicant will attempt to have such Subcustodian Agreement governed by New York law. However, if any Subcustodian Agreement is governed by the local law of the foreign jurisdiction in which the applicable Exemptive Order Network Subsidiary is located, applicant shall obtain an opinion of counsel from such foreign jurisdiction opining as to the enforceability of the rights of a third party beneficiary under the laws of such foreign jurisdiction. Applicant will not utilize Agency Custody Arrangements involving a Subcustodian Agreement governed by the law of a foreign jurisdiction that does not provide for the enforceability of third party beneficiary rights.

6. Applicant currently satisfies and will continue to satisfy the minimum shareholders' equity requirement set forth in rule 17f-5(c)(2)(i).

For the SEC, by the Division of Investment Management, under delegated authority.

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34-37861; File No. SR-DCC-96-09]

Self-Regulatory Organizations; Delta Clearing Corp.; Order Granting Approval of a Proposed Rule Change Relating to Securities Eligible for Margin

October 24, 1996.

On July 2, 1996, Delta Clearing Corp. ("DCC") filed a proposed rule change (File No. SR-DCC-96-09) with the Securities and Exchange Commission ("Commission") pursuant to section 19(b) of the Securities Exchange Act of 1934 ("Act").¹ On August 16, 1996, DCC filed an amendment to the proposed rule change.² Notice of the proposal was published in the Federal Register on September 12, 1996, to solicit comments from interested persons.³ No comments were received. As discussed below, this order approves the proposed rule change.

I. Description

DCC's proposal expands the permissible forms of margin that may be deposited by participants to include U.S. Treasury notes and bonds. Previously, DCC allowed only U.S. Treasury bills or central bank funds as margin collateral for trades in over-the-counter options and for repurchase and reverse repurchase ("repo") agreements. With respect to options, participants also can continue to post margin in the form of cover (i.e., Treasury securities that would be deliverable upon exercise of an option).

The proposal also changes the haircuts applicable to Treasury securities deposited as margin collateral. Previously, such securities were valued at the lesser of the market value or the par value if deposited as margin for options trades or 95% of the market value of deposited as margin for repo trades. Under the proposal, DCC will use the Commission's schedule for valuation of government securities as set forth in the Commission's uniform net capital rule.⁴

II. Discussion

Section 17A(b)(3)(F) of the Act requires that a clearing agency's rules be designed to ensure the safeguarding of securities and funds in its custody or control or for which it is responsible.⁵

¹ 15 U.S.C. § 78s(b) (1988).

² Letter from John Grebenstein, Executive Director, DCC, to Michele Bianco, Division of Market Regulation, Commission (August 16, 1996).

³ Securities Exchange Act Release No. 37639 (September 4, 1996), 61 FR 48186.

⁴ 17 CFR 240.15c3-1 (1966). The schedule for valuation of government securities is set forth in paragraph (c)(2)(vi)(A)(1) of Rule 15c3-1.

⁵ U.S.C. § 78q-1(b)(3)(F) (1988).

While DCC participants trade and maintain inventory in a wide range of U.S. Treasury Securities, they do not always maintain inventory in U.S. Treasury bills. As a result, participants have incurred costs in meeting DCC's requirements that only U.S. Treasury bills could be posted as margin collateral. By expanding the types of collateral DCC will accept for margin purposes, the likelihood that participants will be able to fulfill their margin obligations from inventory is greatly increased. Furthermore, the combination of the highly liquid nature of U.S. Treasury notes and bonds and the haircuts imposed by DCC should allow DCC to accept these securities as margin collateral without adding additional risk to DCC's clearing and settlement operations.

Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and particularly with Section 17A(b)(3)(F) of the Act and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,⁶ that the proposed rule change (File No. SR-DCC-96-09) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁷

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 96-27808 Filed 10-29-96; 8:45 am]

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[Release No. 34-37859; File No. SR-MSRB-96-10]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Reports of Sales and Purchases, Pursuant to Rule G-14

October 23, 1996.

On August 29, 1996, 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-96-10), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. § 78s(b)(1). The proposed rule change is described in Items I, II, and III below, which Items have been prepared by the Board. The Commission is publishing this notice to

⁶ 15 U.S.C. § 78s(b)(2) (1988).

⁷ 17 CFR 200.30(a)(12) (1996).

solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Board is filing an amendment to Board rule G-14 concerning reports of sales and purchases, and to the Rule G-14 Transaction Reporting Procedures. The purpose of the proposed rule change is to increase transparency in the municipal securities market by adding retail and institutional customer transaction information to the inter-dealer transactions currently included in the Board's Transaction Reporting Program ("Program"). The proposed rule change would require brokers, dealers and municipal securities dealers to (1) obtain an executing broker symbol, if one has not already been assigned, from the National Association of Securities Dealers ("NASD"); (2) provide the Board with the name and telephone number of a person responsible for testing the dealer's capabilities to report customer transaction information; (3) test its capabilities to report such information; and (4) report to the Board each day its municipal securities transactions with customers. The Board is requesting that the proposed rule change become effective according to the following proposed schedule:

- Obtain executing broker symbol—Thirty days after Commission approval of proposed rule change.
- Provide contact information—July 1, 1997.
- Test reporting capabilities—July through December 1997, on a schedule to be announced by the Board.
- Effective date for customer transaction reporting—January 1, 1998.

Although portions of the proposed rule change would not become effective until 1998, the Board is requesting Commission approval of the proposed rule change now to allow dealers adequate time to change their internal systems to report customer transactions.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Board included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The texts of these statements may be examined at the places specified in Item VI below. The Board has prepared summaries, set forth in Sections A and B below, of the most significant aspects of such statements.

A. Purpose

The purpose of the proposed rule change is to increase transparency in the municipal securities market by adding retail and institutional customer transaction information to the inter-dealer transactions currently included in the Program. Under the proposed rule change, aggregate data about inter-dealer and customer market activity, and certain volume and price information about all transactions in frequently traded securities, would be disseminated to promote investor confidence in the market and its pricing mechanisms. The information would continue to be provided in the Program's daily report summarizing prices and volumes of trading in the municipal securities market during the previous day (the "Daily Report").¹ In addition, the transaction information on all transactions reported would be made available to regulatory agencies responsible for enforcement of Board rules, as a means to assist in market surveillance.

The Transaction Reporting Program—Overview

The Board has developed the Program to accomplish two objectives. The first is to increase the amount of information available about the market value of individual municipal securities, which has been a longstanding Board goal.² This concept of disseminating information to the public about transactions is now generally referred to by the Board as bringing "transparency" to the market. The second, but equally important, purpose of the Program is to provide a centralized audit trail of municipal securities transactions by making available to the NASD, the Commission, and other enforcement agencies a computer database reflecting all municipal securities transactions reported to the Board. This "surveillance database" helps meet the requirements of those organizations for an audit trail of transaction data, in connection with their surveillance of the market and inspection for compliance with Board rules and securities laws.

At this time, the Program is limited to inter-dealer transactions. Under Board rule G-14, dealers currently report their

inter-dealer transactions to the MSRB each night through the automated comparison system operated by National Securities Clearing Corporation ("NSCC"). This reporting mechanism is convenient for dealers, since most of the trade data that must be reported to the Board has to be reported to NSCC in any event, for clearance and settlement purposes. The Board accomplishes the transparency function by making summary price and volume information available about these transactions on the Daily Report. If the inter-dealer trade data received by the Board indicates that there were four or more trades in an issue during that day, the next morning's Daily Report includes the high, low and average prices, and the total par traded, for that issue.³ Prices and volumes for approximately 100 municipal securities issues are reported daily.

The Board's Daily Report Service currently has nine subscribers who receive electronic copies of the Daily Report each morning. Some subscribers, such as news services, redistribute the information broadly to their own clienteles. Paper copies of the Daily Report are available for inspection in the Board's Public Access Facility in Alexandria, Virginia. Information from the Daily Report is also utilized in the Public Securities Association's transparency initiatives: a generic AAA insured yield scale for publication in newspapers, and an 800-number investor service.⁴

The surveillance database contains information on all transactions reported to the Board and is not limited to transactions in issues traded four or more times. The database also contains information reported to the Board but not included in Daily Reports, such as dealer identities. The NASD currently uses the database to assist in its surveillance of the market and provides direct access to the database to

³ Inter-dealer trades are reported publicly only if they were successfully "compared" on trade date in the automated clearance and settlement system, *i.e.*, if the parties to the trade agreed on trade details such as par value, price, and yield. Average prices are reported only for those trades with par value between \$100,000 and \$1 million.

⁴ The generic AAA insured yield scale provides composite prices based on round lot trades (\$250,000 or above) of municipal bonds which have coupons that reflect current market conditions. Certain yield scale data is published daily in a national newspaper, *USA Today* (see, *e.g.*, "Key Indicators Thursday," *USA Today*, Friday, August 23, 1996, at 3B). The 800 number investor service enables investors to obtain benchmark price quotes relating to particular issues of municipal bonds. Both PSA services incorporate information from the Daily Report, and, in the case of the 800-number service, the caller receives prices from the Daily Report if they are available.

¹ The Board expects in the second quarter of 1997 to file and obtain Commission approval of an additional proposed rule change specifying revisions to the Daily Report format to accommodate customer trade information. The proposed rule change will also specify the fee for subscriptions to the Daily Report.

² See "Planned Pilot Program for Publishing Inter-Dealer Transaction Information," *MSRB Reports*, Vol. 13, No. 3 (June 1993) at 3-6.

surveillance staff at its headquarters and two of its District Offices.

History of Program

In June 1994, the Board filed a proposed rule change to require that dealers report inter-dealer transactions and to operate a facility to report transaction information.⁵ This filing described the computer system that would obtain inter-dealer trading data from dealers and the Board's plan ultimately to include institutional and retail customer transactions in the system, with the goal of making available transaction information that is both comprehensive and contemporaneous. In 1994 the Board stated its plan to implement the Program in four phases.⁶

Phase I—Inter-dealer transaction reporting, in which dealers would use NSCC's comparison system as the reporting vehicle.

Phase II—Institutional customer transaction reporting, in which dealers would use the clearance and settlement system as the transaction reporting mechanism for those trades. Since dealers already use this system to clear most of their transactions with institutional customers, it was thought that this technique would provide a relatively quick and easy means to add institutional customer data to the Program. Time-of-trade reporting for inter-dealer and institutional customer trades also would be added in this phase.

Phase III—Retail customer transaction reporting. Because retail customer transactions are not currently reported by dealers to any central location, such reporting would have to be accomplished by dealers modifying their own trade processing systems to generate files of customer trades that could be transmitted to a new, customized computer system at a central site.

Phase IV—More contemporaneous trade reporting. Phases I–III would require dealer reporting of data by the end of trade date, with public dissemination on the next day.

Phase IV of the Program would be a mechanism to accomplish more contemporaneous reporting of data to the Board and to the public.

The Commission in November 1994 approved the proposed rule change for reporting inter-dealer transactions. Phase I Daily Reports went into production in January 1995. Two

program modifications in Phase I were implemented over the next 18 months. A requirement to report the identity of the executing dealers in inter-dealer transactions (as opposed to only identifying the clearing dealers) became effective July 9, 1995⁷ and a requirement to report the time of execution of inter-dealer transactions became effective July 1, 1996.⁸

Revised Strategy for Obtaining Customer Transaction Data

In preparation for adding institutional customer transaction data in Phase II, during the summer of 1995 the Board conducted a thorough review of institutional customer trade data being submitted by dealers to the centralized clearance and settlement system for institutional customer trades.⁹ The review found that various aspects of this data made it unsuitable for transparency and surveillance support purposes. In general, the standards desired for timeliness, accuracy and completeness of trade data for transparency and market surveillance purposes were not met by the data flowing through the clearance and settlement system. The procedures for submitting, resubmitting and canceling trades are geared toward purposes of clearance and settlement, e.g., if the customer's account number is unknown, dealers must delay submitting the trade to the clearance and settlement system until it is known. Dealers also must cancel and resubmit trade reports to the clearance system to correct settlement-related information, such as name or identification number of the customer's agent. A number of procedures and practices employed by dealers for submitting information to the clearance and settlement system appeared to be acceptable for that

⁷ See Securities Exchange Act Release No. 35988 (July 18, 1995). The initial 1995 proposed rule change included a requirement to report executing dealer identities but did not specify which identification symbol was to be used. Some dealers have used NSCC clearing numbers, others NASD executing broker symbols, and others *ad hoc* symbols which they created themselves. Subsequent experience has shown that one identifier—the NASD executing broker symbol—is the most appropriate identifier for purposes of the Program. This is discussed below, under "Dealer Reporting Requirements."

⁸ See Securities Exchange Act Release No. 37116 (April 16, 1996). The time-of-trade data is currently being stored in the database and in the near future will be made available on the surveillance screens.

⁹ The centralized clearance system that dealers currently are required to use to help clear and settle institutional customer trades under rule G-15(d) is operated by the Depository Trust Company (DTC), and is generally known as the Institutional Delivery (ID) System. The ID System produces confirmations and acknowledgements of institutional trades and is linked to the automated system for book-entry settlement.

purpose but would have hindered the purposes of transaction reporting.¹⁰

The ability of the Board and the industry to overcome the problems with the use of clearance and settlement data for transaction reporting would have required changes in the clearance and settlement system and substantial changes in internal dealer systems and procedures that feed trade data to the clearance and settlement system. This would have been a costly and time-consuming project and, at its conclusion, it would immediately have been necessary to solve similar problems in collecting retail transaction data. The Board decided instead to combine institutional customer transactions with the planned retail trade reporting component of the Program so that retail and institutional customer transactions could be collected using a single mechanism designed specifically to accommodate the purposes of transaction reporting. This new plan, and the recognition of the full extent of changes that would need to be made by dealers to their operations, also necessitated a delay in the previously announced date for implementing institutional and retail transaction reporting.¹¹

The Customer Transaction Reporting Program

Overview. Under the Board's revised approach, included in the proposed rule change, each dealer that effects transactions with customers would generate a file of certain required information about its customer transactions, in a specified format, and would transmit the file electronically to the MSRB by midnight of each trading day. The Board expects that most dealers will modify existing internal processing systems to produce the file required by the proposed rule change. This approach will be less costly to

¹⁰ The Board's review found that dealers submit a substantial portion of institutional trades to the clearance and settlement system after trade date, because of unknown customer account numbers, unknown settlement dates, and other reasons. The relatively high cancellation rate of submissions also creates questions about accuracy of the data available on trade date. Only a small fraction of dealer-submitted trade information is acknowledged as correct by the customer or its agent by the end of trade date. Of the remaining data, some is later acknowledged but a substantial portion is not acknowledged before settlement occurs. For those trades not acknowledged by customers on trade date, it is not possible, on the morning of the day after trade date (T+1), to distinguish between those transactions that were submitted with correct price and quantity and those which were not.

¹¹ Initially the Board had anticipated that retail customer transactions would be added to the Program by the end of 1996. Under the revised plan, this function would be delayed to January 1, 1998.

⁵ See Securities Exchange Act Release No. 34458 (July 28, 1994) at 3.

⁶ See "Reporting Inter-Dealer Transactions to the Board: Rule G-14," *MSRB Reports*, Vol. 14, No. 5, (December 1994) at 3–6.

dealers than if the Board were to mandate the use of an independent transaction reporting system with stand-alone terminals that would have to be acquired by dealers and operated by dealer staff.

The dealer could use any available method to transmit the specified file to the Board's system. Most dealers are expected to use existing telecommunications links with NSCC for this purpose, but, alternatively, dealers with low volumes of customer trades may dial-in to the Board's system and upload the file by modem.

The Board plans to build a subsystem of the Transaction Reporting System for accepting customer transaction information. The resulting Customer Transaction Reporting Subsystem ("CTRS") would encompass the system originally planned for retail transactions, but will process institutional customer transaction data as well. Therefore, dealers will have consistent operational requirements for reporting both retail and institutional customer transactions.

Trade Information to be Reported. Dealers would report approximately a dozen data items about each customer trade. These items, and their purpose in the customer transaction reporting subsystem, are as follows:

CUSIP Number. The number assigned by the CUSIP Service Bureau to identify the security. Other identification numbers will be considered errors. This item is needed for transparency and surveillance purposes.¹² Format: 9 alphanumeric characters.

Trade Date. The date the trade was executed. This item is needed for transparency and surveillance purposes and to determine compliance with the Board's rule G-14 requirement that the trade be reported on trade date. Format: 8 digits, CCYYMMDD.

Time of Trade Execution. The time of day, stated as Eastern time to the nearest minute, at which the trade was executed. This item is needed for surveillance purposes. Format: 4 digits, HHMM, Military format.

Dealer Identifier. The executing broker symbol, assigned by the NASD, that identifies the executing dealer. The dealer identity is needed for surveillance purposes. Format: 4 letters, e.g., ABCD.

Buy/Sell Indicator. An indicator of the dealer's capacity as buyer or seller in the transaction. This item is needed

for surveillance purposes. Format: "B" or "S".

Par Value Traded. The par value, in dollars, of the securities in the transaction. The maturity value of zero coupon securities will be given if it differs from the par value. Par value is needed for transparency and surveillance purposes. Format: 9 digit integer.

Dollar Price. The price of the security, in dollars per hundred dollars par value. Dollar price will be reported to the CTRS *excluding* any commission; the CTRS will include the commission (a separate item, described below) in dollar prices as shown in the Daily Reports. If the dollar price cannot be computed precisely because the settlement date of a "when-issued" transaction is unknown, the CTRS will estimate the dollar price based upon the reported yield and an estimated settlement date (see below). Dollar price is needed for transparency and surveillance purposes. Format: 9 digits plus explicit decimal point, e.g., 100.123456 or 098.765432. The decimal point may "float," e.g., both 00099.5000 and 99.5000000 are valid.

Yield. The yield of the transaction, in percent, as reported on the confirmation. Yield will not be required on transactions in municipal variable-rate or collateralized mortgage obligations. Yield will be used to validate dollar price. Format: 8 digits plus explicit decimal point. Units are per cent, e.g., 03.500000 denotes 3.5%.

Dealer's Capacity and, if Agent, Commission Charged. The dealer's capacity indicates whether the dealer acted as agent or principal toward the customer. It is needed for surveillance purposes. Commission, if any, will be stated as dollars per hundred dollars par value, and is needed for computing the net price including commission. Format "A" or "P". Commission: 7 digits plus explicit decimal, e.g., 00.05000.

Settlement Date. The date the transaction is due to settle. The dealer must provide the settlement date if it is known. If the settlement date for an issue in "when-issued" status is not known at the time the trade information is reported, the CTRS will estimate it as 20 business days after the first trade in the issue, until the actual settlement date for the issue is determined. This item will be used to validate the consistency of dollar price and yield as reported. Format: 8 digits, CCYYMMDD.

Dealer's Control Number for Transaction. An identifier, assigned by the executing dealer, sufficient to identify the transaction from among the dealer's other transactions. Dealers may use any coding method, provided that

no two transactions done by a dealer within a three-year period have the same control number. This item is needed for surveillance purposes (so that submissions can be associated with entries in the dealer's record-keeping system) and for data management (so that a dealer may identify a transaction to be revised after it is first reported to the CTRS). Format: 20 alphanumeric characters.

Cancel/Amend Code and Previous Record Reference. An indicator of whether the dealer is reporting an update to data previously reported about a transaction, and, if necessary, the dealer's control number for the transaction whose data is to be updated. Cancel/Amend code format: "F": First report of this transaction to the MSRB. "C": Cancel the record of the trade identified by the dealer's control number. "A": Amend the record of the trade identified by the dealer's control number. "V": Verification that a record of a transaction containing possible errors is correct.

Use of Intermediaries. An important feature of the Program is a provision for dealers to submit customer transaction data to the Board through an intermediary that could handle the technical details of preparing files in the specified format and/or the function of transmitting correctly formatted files to the CTRS. For example, clearing dealers (dealers that submit transactions for clearance and settlement on behalf of other dealers) could report transactions on behalf of the dealers for whom they clear. Clearing dealers themselves may use service bureaus (firms offering confirmation or other processing services) to collect, format and transmit data to the Board. By using the same telecommunication links for CTRS data as for clearing data, the expense to dealers of customer transaction reporting would be minimized.

The Submission Process. Dealers or intermediaries will perform two steps in submitting customer trade data to the Board. First, they will prepare a file containing the necessary information in the physical format specified by the Board. Second, they will transmit the file to the CTRS.

The dealer may extract the necessary information from its record-keeping or automated confirmation systems, or may key in the data to a program designed specifically to create a file in the correct format. For dealers who wish to key in data on a personal computer, data entry and editing software will be made available by the Board. It is expected that only dealers with low volumes of trades will use this method, since higher-volume dealers already store

¹² Items needed for transparency purposes will appear on the public Daily Report. Items needed for surveillance purposes will be stored the Board's surveillance database and used by the enforcement agencies for audit trail construction and other enforcement purposes.

most of the required trade data in existing computer systems and are expected to adapt those systems for reporting purposes rather than manually re-enter the data into another system.

For file transmission, the Board expects most dealers to use intermediaries, as discussed above. Existing links between dealers and NSCC are expected to be used to transmit most files.¹³ If a dealer does not wish to use a intermediary to transmit files to the Board, the dealer will be able to upload files directly to the CTRS from a personal computer. The Board will make telecommunications software available for uploading files, which will run on the dealer's computer under Microsoft Windows. To upload files by dialing in, a dealer will need a modem and any version of Windows supported by Microsoft Corporation. The Board expects this option to be utilized only by lower-volume dealers because most high-volume dealers are already linked with NSCC. The CTRS is being designed initially with sufficient capacity for up to 100 dial-in submissions per day, although fewer are expected.

Errors and corrections. The system will send messages to dealers, by facsimile, acknowledging receipt of a day's file and identifying records that appear to be in error or questionable. (The system also will make available an electronic copy of the receipt and error message file, which the dealer may optionally download to its computer if it prefers.) Dealers will submit corrections using a method similar to that for reporting trades. A dealer may also "cancel" a trade, that is, inform the system that a trade previously reported did not occur or was cancelled by the parties. Dealers will report only changes relevant to the Board's transaction reporting purposes, for example, a change in the price or par value of a trade.

Dealer Reporting Requirements

The proposed rule change would require dealers to report their customer transactions to the Board by midnight of trade date. Dealers also would be required to report corrections and cancellations as soon as the need for such change is known. Dealers would be able to make changes to data previously reported for two months after the trade date.

The proposed rule change would also require each dealer to use a NASD four-letter executing broker symbol (e.g.,

"ABCD") to identify itself as the party that effected a transaction. Dealers reporting inter-dealer trades to the Board through NSCC currently are required by rule G-14 to identify the executing brokers (as well as the clearing brokers), but the specific symbol to be used is not specified in rule G-14 procedures. Specifying the use of the NASD executing broker symbol will enable users of the surveillance database to determine the executing dealer unambiguously in all cases. The NASD assigns such symbols, on request, to all dealer firms including bank dealers. A dealer not already assigned such a symbol will be required to obtain one from the NASD. Executing broker symbols are already in wide use by many dealers. Since identification symbols are already needed for the audit trail of inter-dealer transactions and it would improve the functions of the surveillance database for this uniform identifier to be used, the Board requests that this provision become effective 30 days after Commission approval of the proposed rule change.

The requirement to report customer trades would become fully effective January 1, 1998, with a testing requirement, discussed below, effective beginning July 1997.

Proposed Mandatory Testing

Dealers will need to test their own trade processing systems to ensure they can produce files containing the required information in the proper format. Such testing would clarify system input specifications with dealers and ensure that dealers' systems are able to correct erroneous input. Mandatory testing by dealers is the only way to ensure that dealers' systems are ready to submit customer trade data before the reporting requirement becomes effective.

To begin system operations by January 1, 1998, the proposed rule change would require testing with dealers between July and December 1997. Procedures would involve testing first by the dealers with the greatest volume of customer trades, followed by the lower-volume dealers. Each dealer would be required to report all its customer trades, on a test basis, to the Board for a specified time. None of the test submissions would be publicly reported or provided to the enforcement agencies. The Board would inform the dealers of any problems found, and the dealer would re-test its system and reporting procedures within two months of the initial run. The proposed rule change would require dealers to provide the Board with the name of a dealer staff person responsible for testing, and to

participate in a testing program, which would begin in July 1997. The Board plans to test first with larger submitters, giving consideration to the test readiness of individuals firms.

The Daily Report

All transactions in municipal securities will be recorded in the surveillance database. The Daily Report, however, will not include price data on every transaction, since it reports on those issues that were traded most frequently during the previous day. As noted above, currently the Daily Report includes summary information on those securities which were traded four or more times the previous business day. Including customer trades will substantially increase the number of issues trading above this "reporting threshold." It is impossible at this time, however, to predict quantitatively the effect on the Daily Report of including retail customer trades, since there is no existing source of comprehensive retail transaction information in the industry. The Board is requesting and has begun receiving samples of customer trade data from certain dealers, on a voluntary basis, and has begun to measure the frequency with which issues are traded, trade sizes, and other factors needed to structure the Daily Report to include customer transaction data. The Board plans to determine the reporting threshold and other formatting aspects of the Daily Report by mid-1997 and will describe it in an additional proposed rule change, to be filed before system operations begin.¹⁴

Customer Transaction Data as a Measure of Dealers' Market Participation

The Board currently levies four types of fees that are generally applicable to dealers. Rule A-12 provides for a \$100 initial fee paid once by a dealer when it enters the municipal securities business. Rule A-14 provides for an annual fee of \$200 from each dealer that conducts municipal securities business during the year. Rule A-13 provides for an underwriting fee based on the par value of a dealer's participation in primary offerings of municipal securities, and for a transaction fee based on the par value of a dealer's transactions reported to the Board. The transaction fee is currently .0005 per cent (one-half cent per \$1,000) of the total par value of inter-dealer sales of municipal securities, since the current

¹³ The Board currently is in discussion with NSCC and it appears that NSCC will offer telecommunications services to dealers for customer transaction reporting.

¹⁴ The planned proposed rule change will also specify the fee for subscriptions to the Daily Report, along with any Program modifications found to be necessary.

reporting requirement applies only to inter-dealer trades.

The Board's goal in allocating fees among dealers is to reflect as accurately as possible each dealer's involvement in the municipal securities market. The Board believes underwriting activity and inter-dealer transaction volume currently are the best available and auditable means upon which to base fees, but the Board has noted that these measures of dealer activity do not track every important activity in the market.¹⁵ When customer transaction data becomes available, the Board will consider revising the basis of the transaction fee to include all trades in municipal securities, not just the inter-dealer transactions as under the current transaction fee structure.

B. Statutory Basis

The Board has proposed the rule change pursuant to Section 15B(b)(2)(C) of the Act, which requires, in pertinent part, that the Board'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 * * * 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. * * *

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

The Board does not believe that the proposed rule change will impose any burden on competition in that it applies equally to all dealers in municipal securities.

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

The 1995 Request for Comments

The Board published a notice in February 1995,¹⁶ requesting comment on the institutional customer transaction phase of the Program and proposing that, to produce the Daily Report in this phase, institutional customer and inter-dealer transactions would be reviewed together to identify those issues in which four or more transactions occurred on a given day.

Once these frequently traded issues were identified, the prices for all transactions in the issue would be reviewed to determine the high and low prices, which would be reported on the next day. An "average price" would be computed based upon all transactions in that issue involving par values between \$100,000 and \$1 million, if any. In response, six comment letters were received from the following:

A.G. Edwards & Sons, Inc. ("Edwards")¹⁷
Goldman, Sachs & Co. ("Goldman")¹⁸
Kemper Securities, Inc. ("Kemper")¹⁹
The Public Securities Association ("PSA 1995")²⁰
The Regional Municipal Operations Association ("RMOA")²¹
Applied Financial Management, Inc. ("Applied Financial")²²

The Board described its revised plan to implement reporting of both institutional and retail customer transactions in a January 1996 notice in which preliminary technical specifications were also proposed for comment.²³ In response, three comment letters were received from the following:

The Public Securities Association ("PSA 1996")²⁴
The Regional Municipal Operations Association ("RMOA 1996")²⁵ and Zia Corporation ("Zia")²⁶

Discussion of Comments

Use of Institutional Transaction Data from the Clearance and Settlement System. One commentator²⁷ stated its preference that the Board use

¹⁷ Letter from Douglas L. Kelly, Vice President, A.G. Edwards & Sons, Inc. to Larry M. Lawrence, Policy and Technology Advisor, MSRB (May 30, 1995).

¹⁸ Letter from Edward C. Briscotti, Vice President, Goldman, Sachs & Co., to Judith A. Somerville, Uniform Practice Specialist, MSRB (May 31, 1995).

¹⁹ Letter from Kathleen M. Burns, Municipal Bond Dept., Kemper Securities, Inc., to Hal Johnson, Deputy General Counsel, MSRB (August 22, 1995).

²⁰ Letter from Joseph W. Sack, Senior Vice President, Public Securities Association ("PSA 1995") to Larry M. Lawrence (June 2, 1995).

²¹ Letter from Bruce L. Vernon, Regional Municipal Operations Association ("RMOA 1995") to Judith Somerville (June 13, 1995).

²² Letter from Ron Moore, Senior Market Analyst, applied Financial Management, Inc. ("Applied Financial") to Larry M. Lawrence (undated).

²³ "Reporting Customer Transactions in Municipal Securities: Rule G-14," *MSRB Reports*, Vol. 16, No. 1 (January 1996) at 15-18, and "Customer Transaction Reporting: Proposed Technical Specifications and Request for Comment," *Ibid.* at 19-22.

²⁴ Letter from George Brakatselos, Vice President, Public Securities Association, to Larry M. Lawrence (May 2, 1996).

²⁵ Letter from Executive Committee of the Regional Municipal Operations Association to Harold Johnson (March 22, 1996).

²⁶ Letter from Glenn Burnett, President, Zia Corporation to Larry M. Lawrence (July 2, 1996).

²⁷ RMOA 1996

institutional trade data reported by dealers to the clearance and settlement system (referred to in its letter as the Depository Trust Company's ("DTC") Institutional Delivery [ID] System). Another commentator²⁸ recommended that the DTC develop a program for reporting retail customer transaction data. A commentator²⁹ suggested that the Board focus on reporting institutional customer transactions because they are "much more illustrative of the activities of the municipal market" than are retail transactions.

Although the Board had hoped to use clearance and settlement data for institutional customer transaction reporting, after a careful review the Board found that various aspects of the clearance and settlement system data make it unsuitable for transparency purposes.³⁰ Regarding the suggestion that the Program should focus on institutional, rather than retail, customer transactions, the Board notes the retail transactions are a necessary and integral part of the Program, both for disclosing prices in the Daily Report and for constructing the comprehensive audit trail.

The Daily Report. The Board received a variety of suggestions for changing the Daily Report. Some commentators³¹ suggested reporting individual transactions, while others³² suggested combining data from all trades falling within a given par value range.

The Board does not intend to raise the threshold of four or more trades a day for Daily Report purposes. At this time, however, it is impossible to predict how the inclusion of retail customer data will affect the Daily Report, since retail transactions are not available to conduct a simulation. The system is being designed to have the capability to produce the Daily Report in various formats, based upon alternative criteria, so that this decision can be made when more information is available. As noticed above, the Board has deferred a decision on the Daily Report criteria until next year, by which time sample customer trade data, provided voluntarily to the Board by several dealers for study, can be analyzed. The Board, at that time, will reconsider all of the comments received on the structure of the Daily Report.

²⁸ Goldman

²⁹ RMOA 1995

³⁰ See above and see also "Reporting Customer Transactions in Municipal Securities: Rule G-14," *MSRB Reports*, Vol. 16, No. 1 (January 1996), at 16 and footnote 6.)

³¹ Kemper, Zia and Applied Financial

³² PSA 1995, PSA 1996

¹⁵ See Securities Exchange Act Release No. 36492 (November 20, 1995) at 4-5 and "Revisions to Board Fee Assessments: Rules A-13, A-14 and G-14," *MSRB Reports*, Vol. 16, No. 1 (January 1996) at 29.

¹⁶ "Transaction Reporting Program for Municipal Securities: Phase II," *MSRB Reports*, Vol. 15, No. 1 (April 1995) at 11-15.

Transactions to be Reported. The Board's 1996 request for comment asked whether transactions in certain types of municipal securities should be excluded from reporting. The securities that might be excluded are those that may require special processing by dealer systems, e.g., variable-rate securities, collateralized mortgage obligations, securities prepaying principal and securities trading "flat." One commentator³³ stated that all municipal transactions should be included in the scope of transactions reported, except those in securities that are ineligible for CUSIP number assignment. The proposed rule change would require dealers to report customer transactions in all securities eligible for CUSIP number assignment. The Board notes, however, that it may be impossible, at least initially, to calculate meaningful and reliable dollar prices from yield for some of these instruments with non-standard payment structures. Thus, although the separate trade information will go into the surveillance database for audit trail purposes, some transactions in municipal securities with non-standard payment or call features may not be included as part of the Daily Report.

Data Items to be Reported by Dealers. One commentator³⁴ stated its belief that there is no need for data items in addition to those in the request for comment. The Board has determined that, with one exception, the data items proposed in the January 1996 notice are sufficient for processing customer transaction data and has included those items in the proposed rule change.³⁵

Estimating the Settlement Date. Transactions involving the distribution of new issue securities sometimes are effected before the first settlement date is determined. Often the parties to such "when-issued" transactions agree on the yield of the transaction when effecting the trade, and calculate the corresponding dollar price after the settlement date is determined. The proposed rule change would require the reporting of such transactions on trade date. The system is designed to estimate the dollar price for next-day reporting based upon the reported yield and an estimated settlement date. The 1996 request for comment asked whether the dealer or the Board should estimate the settlement date, and a commentator³⁶

proposed the date should be estimated by the Board. Accordingly, the Board will estimate the settlement date as the date of first trade plus 20 business days.

Information about Calls or Pre-refunded Securities. One commentator³⁷ suggested that the Board require the dealer to report whether the security was priced to call or was known to be pre-refunded, in order to be sure the dealer took such information into account. The planned system is designed to verify the reported dollar price and yield by recalculating the dollar price from the reported yield, using data about the security obtained from one or more securities information vendors. The calculations should be the same if issue information used by the Board and the dealer is the same. If the system's recalculated price indicates there may be erroneous input caused by typographical errors, the dealer will be informed and the transaction will not be included in the Daily Report. Therefore, it is unnecessary to request call or pre-refunding information from the dealer as part of trade input.

Program Costs and "Open Systems" Approach. One commentator³⁸ expressed concern that the Board remain sensitive to the cost to dealers of reporting customer transactions. This commentator also commended the Board for taking the "open system" approach to provide flexibility to dealers and intermediaries in configuring their reporting systems.

The Board notes that the system design and approach to the Transaction Reporting Program are intended to minimize long-term resource commitments from dealers. Instead of requiring dealers to lease a terminal from the Board and hire personnel to input transactions, the program is designed so that dealers can generate nightly files of trade data from their existing trade processing systems. In addition, NSCC has stated its willingness to allow dealers to utilize existing telecommunications links as the means for transmitting these files to the Board. The Board, as well as dealers, will benefit from dealers using existing links with NSCC, since the Board's system then will need less hardware and staff to support dial-in submissions.

Standardized Format for Vendor Reports. A commentator³⁹ posited that the Board may desire to have uniformity among transaction reports distributed by information vendors, and recommended that the Board impose standards for vendor-produced "Official MSRB Daily

Reports." The Board desires to provide maximum flexibility for value-added vendors to reformat the public transaction information to meet the needs of the marketplace, and does not intend to define an "official" report format for redistribution of data obtained via its Daily Report Service.

V. 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 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 such proposed rule change, or

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

VI. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549. 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 principal offices. All submissions should refer to File No. SR-MSRB-96-10 and should be submitted by November 20, 1996.

For the Commission by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland,

Deputy Secretary.

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³³ PSA 1996

³⁴ PSA 1996.

³⁵ The exception is the "cancel/amend code," an indicator whether the dealer is reporting a change to data previously reported about a transaction. This indicator was not specified in the 1996 notice, but is logically necessary to enable the dealer to correct erroneous reports made to the Board.

³⁶ PSA 1996.

³⁷ Zia.

³⁸ PSA 1996.

³⁹ Applied Financial.