

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

The MSRB is filing a proposed rule change concerning market emergencies consisting of an Interpretation of its Rule G-17, on conduct of municipal securities activities and an amendment to its Rule A-4, on meetings of the Board.

The text of the proposed rule change follows. Italics indicate proposed additions.

Rule G-17. Conduct of Municipal Securities Activities

Interpretation of Rule G-17—Effecting Transactions During Market Emergency

It is inconsistent with the principles of fair dealing embodied in Rule G-17 for a broker, dealer or municipal securities dealer to effect transactions in municipal securities during a market emergency. For purposes of this interpretation, a market emergency is any situation causing a substantial failure in any of the systems necessary for clearance, settlement, confirmation, payment, or delivery of transactions in municipal securities or in other systems necessary for the prompt execution and consummation of municipal securities transactions or the fair and accurate pricing of municipal securities. In determining whether such a market emergency exists, a broker, dealer or municipal securities dealer shall rely upon the issuance of official announcements by the MSRB concerning market emergencies, which shall be issued after consultation with the Securities and Exchange Commission. Official announcements by the MSRB on market emergencies will be communicated to brokers, dealers and municipal securities dealers through news outlets commonly used in the municipal securities industry, by posting on the MSRB's World Wide Web site at www.msrb.org, and by transmittal of the announcement to the electronic mail addresses provided to the MSRB by brokers, dealers and municipal securities dealers under Rule G-40. Such official announcements will include information on the nature of the market emergency and affected systems, the nature and scope of transactions affected, and the status of the market emergency and its expected duration, if that is known.

Rule A-4. Meetings of the Board

(a) through (d) No Change.

(e) *Special Meetings on Market Emergencies. Notwithstanding anything in these rules to the contrary, the following procedures govern special*

meetings to act on market emergencies: (i) notice of special telephone conference call meeting on a market emergency shall be sent to all Board members by the Executive Director, or in the absence of the Executive Director, by his or her designee: (A) as soon as possible after credible information is received suggesting the existence of a market emergency, and (B) during the existence of a declared market emergency, within 24 hours of a request by any Board member; (ii) notice of a special meeting on a market emergency, including a description of the proposed Board action and instructions for joining the conference call, shall be given by telephone and by e-mail to all Board members; (iii) the Executive Director, or his or her designee, shall consult with the Commission on the emergency situation prior to a special meeting on a market emergency, if possible; (iv) the quorum requirement for a special meeting on a market emergency shall be five members and there shall be no requirement that at least one public representative, one broker-dealer representative and one bank representative be present; and (v) any action taken at such a meeting shall be by a majority vote of Board members attending the meeting and shall be limited to declaring a market emergency or ending a declared market emergency. For purposes of this paragraph (e), the meaning of the term "market emergency" shall be as defined in "Notice of Interpretation of Rule G-17—Effecting Transactions During Market Emergency," dated _____.

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

In its filing with the SEC, the MSRB 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 text of these statements may be examined at the places specified in Item IV below. The MSRB has prepared summaries, set forth in Section A, B, and C below, of the most significant aspects of such statements.

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

(1) Purpose

After the events of September 11, 2001, staff of the Commission and the MSRB met to discuss how the municipal securities market functioned in the aftermath of the attacks on the

World Trade Center. On September 11, and in the days following, MSRB monitored the municipal securities market through its contacts with dealers, clearing corporations and information providers.

Although the effect on lower Manhattan was severe, because the municipal securities market is decentralized, the municipal securities market as a whole was not affected to the same degree as securities exchanges physically located near the disaster. On September 11, some trading in municipal securities occurred, albeit a very limited amount. Based on transactions reported to the MSRB's Transaction Reporting System, trade volume reached 8,244 trades by September 13 and 17,941 trades by September 17. On September 19 and 20 transaction volume reached 23,996 and 26,155 trades respectively. Prior to September 11, in a typical day, 27,000 transactions were processed.

Aside from dealer operations in Manhattan, in general, the infrastructure and systems necessary for processing transactions in the municipal securities market functioned in the days after September 11. Clearance and settlement systems for municipal securities transactions provided by Depository Trust and Clearing Corporation (DTCC) remained operational, although telecommunications problems in Manhattan did affect the ability of dealers in that area to exchange data with DTCC. The problems with clearing bank functions that disrupted the government securities market did not substantially affect the municipal securities market.

Despite the resilience of municipal securities market systems and infrastructure on September 11, there remains a concern about what might have happened if the situation had been different. Had systems or infrastructure critical to the municipal securities market been disabled by the disaster, no legal or regulatory mechanism existed to temporarily halt trading. For example, any problems with central clearance and settlement systems are of an immediate concern, since the accumulation of unsettled trades, particularly in a volatile or chaotic market, presents risks to all segments of the market. Commission staff accordingly have asked MSRB to consider rulemaking to provide a procedure for a trading halt should a market emergency disable critical market systems or infrastructure in the future.

The proposed rule change would provide such a procedure. Should a similar situation occur in the future, MSRB would review conditions in the