

Rule G-47: Time of Trade Disclosure

(a)(i) No broker, dealer, or municipal securities dealer shall sell a municipal security to a customer, or purchase a municipal security from a customer, whether unsolicited or recommended, and whether in a primary offering or secondary market transaction, without disclosing to the customer, orally or in writing, at or prior to the time of trade, all material information known about the transaction, as well as material information about the security that is reasonably accessible to the market.

(ii) Notwithstanding section (a)(i) above, material information is not required to be disclosed to the customer if, pursuant to the dealer's policies and procedures regarding insider trading and related securities laws, such information is intentionally withheld from the dealer's registered representatives who are engaged in sales to and purchases from a customer.

(b) Definitions

- (i) No change.
- (ii) “Material information”: Information is considered to be material if there is a substantial likelihood that the information would be considered important [or significant] by a reasonable investor in making an investment decision.
- (iii) No change.

Supplementary Material**.01 Manner and Scope of Disclosure**

- a. The disclosure obligation includes a duty to give a customer a complete description of the security, including a description of the features that likely would be considered important [significant] by a reasonable investor, and facts that are material to assessing the potential risks of the investment.
- b. - d. No change.

.02 No change.

.03 Disclosure obligations in specific scenarios. The following examples describe information that may be material in specific scenarios and require time of trade disclosures to a customer. This list is not exhaustive and other information may be material to a customer in these and other scenarios.

- a. - h. No change.

i. **Bonds that prepay principal.** The fact that the security prepays principal (e.g. factor bonds to which a factor reflecting a prior partial distribution is applied to determine interest payments and principal amount) and the amount of unpaid principal that will be delivered on the transaction.

j. - o. No change.

p. **Market discount.** The fact that a municipal security bears market discount and that all or a portion of the investor's investment return represented by accretion of the market discount might be taxable as ordinary income.

q. **Zero coupon bonds or stepped coupon bonds.** The special characteristics of zero coupon bonds or stepped coupon bonds and, with respect to stepped coupon securities, the details of the increases to the interest rates.

r. **Yield to worst.** The computed yield required by Rule G-15(a)(i)(A)(5)(c) if different than the yield at which the transaction was effected.

s. **Unavailability of an official statement.** In sales to customers of new issue securities constituting offered municipal securities within the meaning of Rule G-32, the fact that no official statement is available on EMMA or that an official statement is only available from the underwriter.

t. **Whether continuing disclosures may be unavailable.** Whether the issuer or other obligated person has not agreed to make continuing disclosures with respect to the municipal security as contemplated under Securities Exchange Act Rule 15c2-12 that will be available on EMMA.

Time of Trade Disclosures in Inter-Dealer Transactions

For inter-dealer transactions, there is no specific requirement for brokers, dealers or municipal securities dealers (individually and collectively, "dealers") to disclose all material facts to another dealer at time of trade. A selling dealer is not generally charged with the responsibility to ensure that the purchasing dealer knows all relevant features of the municipal securities being offered for sale. The selling dealer may rely, at least to a reasonable extent, on the fact that the purchasing dealer is also a professional and will satisfy their need for information prior to entering into a contract for the municipal securities.

The items of information that professionals in an inter-dealer transaction must exchange at or prior to the time of trade are governed by principles of contract law and essentially are those items necessary adequately to describe the municipal security that is the subject of the contract. As a general matter, these items of information do not encompass all material facts, but should be sufficient to distinguish the municipal security from other similar issues. The Board has interpreted Rule G-17 to require dealers to treat other dealers fairly and to hold them to the

prevailing ethical standards of the industry. The rule also prohibits dealers from knowingly misdescribing municipal securities to another dealer. As a result, it is possible that non-disclosure of an unusual feature might constitute an unfair practice and thus become a violation of Rule G-17 even in an inter-dealer transaction.

For example, with respect to bonds that prepay principal, non-disclosure of the fact that a bond prepays principal could be a violation of Rule G-17. This would be especially true if the information about the prepayment feature is not accessible to the market and is intentionally withheld by the selling dealer. Whether or not non-disclosure constitutes an unfair practice in a specific case would depend upon the individual facts of the case. However, to avoid trade disputes and settlement delays in inter-dealer transactions, it generally is in dealers' interest to reach specific agreement on the existence of any prepayment feature and the amount of unpaid principal that will be delivered.

[Time of Trade Disclosure—Disclosure of Market Discount

Overview

MSRB Rule G-47, on time of trade disclosure, requires brokers, dealers and municipal securities dealers (collectively, “dealers”) to disclose to their customers, at or prior to the time of trade, all material information known about the transaction, as well as material information about the municipal security that is reasonably accessible to the market. The MSRB has previously provided interpretive guidance, now codified in supplementary material to Rule G-47, on specific types of information that is material where specific scenarios occur and requires time of trade disclosure. Rule G-47, however, emphasizes that this list of specific disclosures is not exhaustive, and that other information may be material to a customer and required to be disclosed. The MSRB is publishing this notice to state its interpretation that the fact that a municipal security bears market discount is material information that must be disclosed to a customer under Rule G-47.

Market Discount

When a municipal security is acquired in the secondary market for less than par value, the security may have “market discount.” The amount of market discount is equal to the excess, if any, of the stated redemption price at maturity over the basis of the security immediately after its purchase by the investor. Market discount occurs when the value of a municipal security declines after its issue date—which often may occur due to a rise in interest rates. The fact that a municipal security bears market discount may significantly affect its tax treatment. Under federal tax law, for bonds purchased after April 30, 1993, the market discount is taxed at the investor’s ordinary income tax rate, rather than the capital gains rate.¹

[¹ Tax treatment and the amount of market discount and original issue discount (if any) are determined in accordance with the provisions of the Internal Revenue Code and the rules and regulations of the Internal Revenue Service.]

Original Issue Discount Bonds. Market discount is calculated differently for original issue discount (OID) bonds. An OID bond is a bond that was sold at the time of issue at a price that included an original issue discount. The original issue discount is the amount by which the bond's stated redemption price at maturity exceeded its public offering price at the time of its original issuance and, for a tax-exempt municipal security, is generally treated as tax-exempt interest.²

Market discount exists for an OID bond when the bond is acquired in the secondary market for less than its revised or adjusted issue price. The revised or adjusted issue price for an OID bond is equal to the bond's original issue price plus the accrued OID up to the date of purchase. The amount of market discount is equal to the excess, if any, of the revised issue price over the basis of the bond immediately after its purchase by the investor.

De Minimis Rule. Bonds with a *de minimis* amount of market discount are subject to more favorable tax treatment than bonds with a non-*de minimis* amount of market discount. Under the *de minimis* rule, if the amount of market discount is less than one-fourth of 1% (.0025) of the stated redemption price of the bond multiplied by the number of complete years from the date of purchase to the date of maturity, the market discount is *de minimis* and is generally taxed as a capital gain, rather than ordinary income.

Market Discount Disclosure at or Prior to the Time of Trade

As noted, Rule G-47 requires dealers to disclose to their customers, at or prior to the time of trade, "all material information known about the transaction, as well as material information about the security that is reasonably accessible to the market."³ This disclosure obligation applies whether the transaction is unsolicited or recommended, and whether it is a primary offering or secondary market transaction. Information is considered to be material under Rule G-47 if there is a substantial likelihood that the information would be considered important or significant by a reasonable investor in making an investment decision. The MSRB has previously stated, and codified as supplementary material to Rule G-47, that the fact that a municipal security bears an original issue discount is material information that dealers are obligated to disclose, because it may affect the tax treatment of the security.⁴ Significantly, in explaining this interpretation of the

[² For more information about original issue discount bonds, see MSRB, About Original Issue Discount Bonds, available at: <https://www.msrb.org/msrb1/pdfs/Original-Issue-Discount-Bonds.pdf>.]

[³ MSRB Rule G-47(a). However, under MSRB Rule G-48, on transactions with sophisticated municipal market professionals, a dealer is relieved of the obligation to disclose to a sophisticated municipal market professional or SMMP material information that is reasonably accessible to the market. See Rule G-48(a). Accordingly, dealers do not have an obligation to disclose to SMMPs the existence of market discount.]

[⁴ See MSRB Rule G-47, Supplementary Material .03(f); see also Interpretive Reminder Notice Regarding Rule G-17, on Disclosure of Material Facts—Disclosure of Original

Board's rules, the MSRB noted that appropriate disclosure of a security's original issue discount feature should assist customers in computing the market discount or premium on their transaction. The MSRB also noted its concern that, absent adequate disclosure of a security's original issue discount status, an investor might not be aware that all or a portion of his or her investment return represented by accretion of the discount is tax-exempt, and might therefore, for example, sell the security at an inappropriately low price (*i.e.*, a price not reflecting the tax-exempt portion of the discount).

Similarly, the MSRB is concerned that, absent adequate disclosure that a security has market discount, an investor might not be aware that all or a portion of his or her investment return represented by accretion of the market discount is taxable as ordinary income, and therefore might, for example, purchase the securities at an inappropriately high price (*i.e.*, a price not reflecting the potentially higher tax rate applicable to the discount). The existence of market discount may impact an investor's decision to purchase or sell an affected bond or determination of what price to pay or accept for such bond. As a result, the MSRB believes that the fact that a security has market discount is material information that is required to be disclosed to a customer under Rule G-47 at or prior to the time of trade.]

[Confirmation, Delivery and Reclamation of Interchangeable Securities

In March 1988, the Securities and Exchange Commission approved amendments to rules G-12 and G-15 concerning municipal securities that may be issued in bearer or registered form (interchangeable securities).¹ These amendments will become effective for transactions executed on or after September 18, 1988. The amendments revise rules G-12(e) and G-15(c) to allow inter-dealer and customer deliveries of interchangeable securities to be either in bearer or registered form, ending the presumption in favor of bearer certificates for such deliveries. The amendments also delete the provision in rule G-12(g) that allows an inter-dealer delivery of interchangeable securities to be reclaimed within one day if the delivery is in registered form. In addition, the amendments remove the provisions in rules G-12(c) and G-15(a) that require dealers to disclose on inter-dealer and customer confirmations that securities are in registered form.

The Board has received inquiries on several matters concerning the amendments and is providing the following clarifications and interpretive guidance.

Deliveries of Interchangeable Securities

Issue Discount Bonds (January 5, 2005); Rules G-12 and G-15, Comments Requested on Draft Amendments on Original Issue Discount Securities, *MSRB Reports*, Vol. 4, No. 6 (May 1994) at 7.]

[¹ See SEC Release No. 34-25489 (March 18, 1988); *MSRB Reports* Vol. 8, no. 2 (March 1988), at 3.]

Several dealers have asked whether the amendments apply to securities that can be converted from bearer to registered form, but that cannot then be converted back to bearer form. These securities are "interchangeable securities" because they originally were issuable in either bearer or registered form. Therefore, under the amendments, physical deliveries of these certificates may be made in either bearer or registered form, unless a contrary agreement has been made by the parties to the transaction.²

The Board also has been asked whether a mixed delivery of bearer and registered certificates is permissible under the amendments. Since the amendments provide that either bearer or registered certificates are acceptable for physical deliveries, a delivery consisting of bearer and registered certificates also is an acceptable delivery under the amendments.

Fees for Conversion

Transfer agents for some interchangeable securities charge fees for conversion of registered certificates to bearer form. Dealers should be aware that these fees can be substantial and, in some cases, may be prohibitively expensive. Dealers, therefore, should ascertain the amount of the fee prior to agreeing to deliver bearer certificates. A dealer may pass on the costs of converting registered securities to bearer form to its customer. In such a case, the dealer must disclose the amount of the conversion fee to the customer at or prior to the time of trade, and the customer must agree to pay it.³ In addition, rule G-15(a)(iii)(J)* requires that the dealer note such an agreement (including the amount of the conversion fee) on the confirmation.⁴ The conversion fee, however, should not be included in the price when calculating the yield shown on the confirmation.⁵ In collecting this fee, the dealer merely would be passing on the costs imposed

[² The amendments should substantially reduce delays in physical deliveries that result because of dealer questions about whether specific certificates should be in bearer form. This efficiency would be impossible if these "one-way" interchangeable securities were excluded from the amendments since dealers would be required to determine, for each physical delivery of registered securities, whether the securities are "one-way" interchangeable securities.]

[³ Rule G-17, on fair dealing, requires dealers to disclose all material facts about a transaction to a customer at or before the time of trade. In many cases, the conversion fee is as much as \$15 for each bearer certificate. The Board also has been made aware of some cases in which the transfer agent must obtain new printing plates or print new bearer certificates to effect a conversion. The conversion costs then may be in excess of several hundred or a thousand dollars. Therefore, it is important that the customer be aware of the amount of the conversion costs prior to agreeing to pay for them.]

[⁴ This rule requires that, in addition to any other information required on the confirmation, the dealer must include "such other information as may be necessary to ensure that the parties agree on the details of the transaction."]

[⁵ Rule G-15(a)(i)(I) [currently codified at rule G-15(a)(i)(A)(5)] requires the yield of a customer transaction to be shown on the confirmation.]

by a third party, voluntarily assumed by the customer, relating to the form in which the securities are held. The conversion fee thus is not a necessary or intrinsic cost of the transaction for purposes of yield calculation.⁶

Continued Application of the Board's Automated Clearance Rules

The Board's automated clearance rules, rules G-12(f) and G-15(d), require book-entry settlements of certain inter-dealer and customer transactions.⁷ The amendments on interchangeable securities address only physical deliveries of certificates and, therefore, apply solely to transactions that are not required to be settled by book-entry under the automated clearance rules.

When a physical delivery is permitted under Board rules (*e.g.*, because the securities are not depository eligible), dealers may agree at the time of trade on the form of certificates to be delivered. When such an agreement is made, this special condition must be included on the confirmation, as required by rules G-12(c)(vi)(I) and G-15(a)(iii)(J).^{8*} Dealers, however, may not enter into an agreement providing for a physical delivery when book-entry settlement is required under the automated clearance rules, as this would result in a violation of the automated clearance rules.⁹

Need for Education of Customers on Benefits of Registered Securities

Dealers should begin planning as soon as possible any internal or operational changes that may be needed to comply with the amendments. The Depository Trust Company (DTC) has announced plans for a full-scale program of converting interchangeable securities now held in

[⁶ Some customers, for example, may ask dealers to convert registered securities to bearer form even though the customers also may be willing to accept registered certificates if this is more economical.]

[⁷ Rule G-12(f)(ii) requires book-entry settlement of an inter-dealer municipal securities transaction if both dealers (or their clearing agents for the transaction) are members of a depository making the securities eligible and the transaction is compared through a registered securities clearing agency. Rule G-15(d)(iii) requires book-entry settlement of a customer transaction if the dealer grants delivery versus payment or receipt versus payment privileges on the transaction and both the dealer and the customer (or the clearing agents for the transaction) are members of a depository making the securities eligible.]

[⁸ These rules require that, in addition to the other information required on inter-dealer and customer confirmation, confirmations must include "such other information as may be necessary to ensure that the parties agree to the details of the transaction."]

[⁹ Of course, dealers may withdraw physical certificates from a depository once a book-entry delivery is accepted.]

bearer form to registered form beginning on September 18, 1988.¹⁰ When possible, DTC plans to retain a small supply of bearer certificates in interchangeable issues to accommodate withdrawal requests for bearer certificates.¹¹ The general effect of the amendments and DTC's policy, however, will make it difficult for dealers, in certain cases, to ensure that their customers will receive bearer certificates. Dealers should educate customers who now prefer bearer certificates on the call notification and interest payment benefits offered by registered certificates and dealer safekeeping and advise them when it is unlikely that bearer certificates can be obtained in a particular transaction. Dealers safekeeping municipal securities through DTC on behalf of such customers also may wish to review with those customers DTC's new arrangements for interchangeable securities.]

[Application of Board Rules to Transactions in Municipal Securities Subject to Secondary Market Insurance or Other Credit Enhancement Features

It has come to the Board's attention that insurance companies are offering to insure whole maturities of issues of municipal securities outstanding in the secondary market. The Board understands that municipal securities professionals must apply for the insurance which, once issued, will remain in effect for the life of the security. The Board further understands that other credit enhancement devices also may be developed for secondary market issues.

The Board wishes to remind the industry of the application of rule G-17, the Board's fair dealing rule, in connection with transactions with customers in securities that are subject to secondary market insurance or other credit enhancement devices or in securities for which arrangements for such insurance or device have been initiated.¹ The Board is of the view that facts, for example, that a security has been insured or arrangements for insurance have been initiated, that will affect the market price of the security are material and must be disclosed to a customer at or before execution of a transaction in the security. In addition, the Board believes that a dealer should

[¹⁰ DTC expects this conversion process to take approximately two years. Midwest Securities Trust Company and The Philadelphia Depository Trust Company have not yet announced their plans with regard to interchangeable securities.]

[¹¹ DTC Notice to Participants on Plans for Comprehensive Conversion of Interchangeable Municipal Bonds to the Registered Form (August 10, 1988).]

[* [Currently codified at rule G-15(a)(i)(A)(8)]]

[¹ Rule G-17 provides:

In the conduct of its municipal securities business, each broker, dealer, and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.]

advise a customer if evidence of insurance or other credit enhancement feature must be attached to the security for effective transference of the insurance or device.²

The Board also wishes to remind the industry that under rule G-13, concerning quotations, all quotations relating to municipal securities made by a dealer must be based on the dealer's best judgment of the fair market value of the securities at the time the quotation is made. Offers to buy securities that are insured or otherwise have a credit enhancement feature, or for which arrangements for insurance or other credit enhancement have been initiated, must comply with rule G-13. Similarly, the prices at which these securities are purchased or sold by a municipal securities dealer must be fair and reasonable to its customers under Board rule G-30 on prices and commissions.]

[Notice Concerning Securities that Prepay Principal

The Board has become aware of several issues of municipal securities that prepay principal to the bondholders over the life of the issue. These securities are issued with a face value that equals the total principal amount of the securities. However, as the prepayment of principal to bondholders occurs over time, the "unpaid principal" associated with a given quantity of the securities become an increasingly lower percentage of the face amount. The Board believes that there is a possibility of confusion in transactions involving such securities, since most dealers and customers are accustomed to municipal securities in which the face amount always equals the principal amount that will be paid at maturity.

Because of the somewhat unusual nature of the securities, the Board believes that dealers should be alert to their disclosure responsibilities. For customer transactions, rule G-17 requires that the dealer disclose to its customer, at or prior to the time of trade, all material facts with respect to the proposed transaction. Because the prepayment of principal is a material feature of these securities, dealers must ensure that the customer knows that securities prepay principal. The dealer also must inform the customer of the amount of unpaid principal that will be delivered on the transaction.

For inter-dealer transactions, there is no specific requirement for a dealer to disclose all material facts to another dealer at time of trade. A selling dealer is not generally charged with the responsibility to ensure that the purchasing dealer knows all relevant features of the securities being offered for sale. The selling dealer may rely, at least to a reasonable extent, on the fact that the purchasing dealer is also a professional and will satisfy his need for information prior to entering into a contract for the securities. Nevertheless, it is possible that non-disclosure of an unusual feature such as principal prepayment might constitute an unfair practice and thus become a violation of rule G-17 even in an inter-dealer transaction. This would be especially true if the information about the prepayment feature is not accessible to the market and is

[² The Board has adopted amendments to rule G-15 which, among other things, require that deliveries to customers of insured securities be accompanied by some evidence of the insurance.]

intentionally withheld by the selling dealer. Whether or not non-disclosure constitutes an unfair practice in a specific case would depend upon the individual facts of the case. However, to avoid trade disputes and settlement delays in inter-dealer transactions, it generally is in dealers' interest to reach specific agreement on the existence of any prepayment feature and the amount of unpaid principal that will be delivered.]

[Disclosure of Pricing: Calculating the Dollar Price of Partially Prerefunded Bonds

Disclosure of pricing: calculating the dollar price of partially prerefunded bonds. This is in response to your March 21, 1986 letter concerning the application of Board rules to the description of municipal securities provided at or prior to the time of trade and the application of rules G-12(c) and G-15(a) on calculating the dollar price of partially prerefunded bonds with mandatory sinking fund calls.

You describe an issue, due 10/1/13. Mandatory sinking fund calls for this issue begin 10/1/05 and end 10/1/13. Recently, a partial refunding took place which prerefunds the 2011, 2012 and 2013 mandatory sinking fund requirements totalling \$11,195,000 (which is 43.6% of the issue) to 10/1/94 at 102. The certificate numbers for the partial prerefunding will not be chosen until 30 days prior to the prerefunded date. Thus, a large percentage of the bonds are prerefunded and all the bonds will be redeemed by 10/1/10 because the 2011, 2012, and 2013 maturities no longer exist.

You note that the bonds should be described as partially prerefunded to 10/1/94 with a 10/1/10 maturity. Also, you state that the price of these securities should be calculated to the cheapest call, in this case, the partial prerefunded date of 10/1/94 at 102. You add that there is a 9½ point difference in price between calculating to maturity and to the partially prerefunded date.

You note that the descriptions you have seen on various brokers' wires do not accurately describe these securities and a purchaser of these bonds would not know what they bought if the purchase was based on current descriptions. You ask the Board to address the description and calculation problems posed by this issue.

Your letter was referred to a Committee of the Board which has responsibility for interpreting the Board's fair practice rules. That Committee has authorized this response.

Board rule G-17 provides that

In the conduct of its municipal securities business, each broker, dealer, and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.

In regard to inter-dealer transactions, the items of information that professionals must exchange at or prior to the time of trade are governed by principles of contract law and essentially are those items necessary adequately to describe the security that is the subject of the contract. As a

general matter, these items of information do not encompass all material facts, but should be sufficient to distinguish the security from other similar issues. The Board has interpreted rule G-17 to require dealers to treat other dealers fairly and to hold them to the prevailing ethical standards of the industry.¹ The rule also prohibits dealers from knowingly misdescribing securities to another dealer.²

Board rules G-12(c) and G-15(a) require that

where a transaction is effected on a yield basis, the dollar price shall be calculated to the lowest of price to call, price to par option, or price to maturity ...

In addition, for customer confirmations, rule G-15(a) requires that

for transactions effected on the basis of dollar price, ... the lowest of the resulting yield to call, yield to par option, or yield to maturity shall be shown....

These provisions also require, in cases in which the resulting dollar price or yield shown on the confirmation is calculated to call or par option, that this must be stated and the call or option date and price used in the calculation must be shown. The Board has determined that, for purposes of making this computation, only "in-whole" calls should be used.³ This requirement reflects the longstanding practice of the municipal securities industry that a price calculated to an "in-part" call, for example, a partial prerefunding date, is not adequate because, depending on the probability of the call provision being exercised and the portion of the issue subject to the call provision, the effective yield based on the price to a partial prerefunding date may not bear any relation to the likely return on the investment.

These provisions of Rules G-12(c) and G-15(a) apply, however, only when the parties have not specified that the bonds are priced to a specific call date. In some circumstances, the parties to a particular transaction may agree that the transaction is effected on the basis of a yield to a particular date, *e.g.*, a partial prerefunding date, and that the dollar price will be computed in this fashion. If that is the case, the yield to this agreed upon date must be included on confirmations

[¹ In addition, the Board has interpreted this rule to require that, in connection with the purchase from or sale of a municipal security to a customer, at or before execution of the transaction, a dealer must disclose all material facts concerning the transaction which could affect the customer's investment decision, including a complete description of the security, and not omit any material facts which would render other statements misleading.]

[² While the Board does not have any specific disclosure requirements applicable to dealers at the time of trade, a dealer is free to disclose any unique aspect of an issue. For example, in the issue described above, a dealer may decide to disclose the "effective" maturity date of 2010, as well as the stated maturity date of 2013.]

[³ *See* [Rule G-15 Interpretation - Notice Concerning Pricing to Call], December 10, 1980 ... at ¶ 3571.]

as the yield at which the transaction was effected and the resulting dollar price computed to that date, together with a statement that it is a "yield to [date]." In an August 1979 interpretive notice on pricing of callable securities, the Board stated that, under rule G-30, a dealer pricing securities sold to a customer on the basis of a yield to a specified call feature should take into account the possibility that the call feature may not be exercised.⁴

Accordingly, the price to be paid by the customer should reflect this possibility, and the resulting yield to maturity should bear a reasonable relationship to yields on securities of similar quality and maturity. Failure to price securities in such a manner may constitute a violation of rule G-30 since the price may not be "fair and reasonable" in the event the call feature is not exercised. The Board also noted that the fact that a customer in these circumstances may realize a yield in excess of the yield at which the transaction was effected does not relieve a municipal securities dealer of its responsibilities under rule G-30.

Accordingly, the calculation of the dollar price of a transaction in the securities you describe, unless the parties have agreed otherwise, should be made to the lowest of price to the first in-whole call, par option, or maturity. While the partial prerefunding effectively redeems the issue by 10/1/10, the stated maturity of the bond is 10/1/13 and, subject to the parties agreeing to price to 10/1/10, the stated maturity date should be used.]

[Description Provided at or Prior to the Time of Trade

Description provided at or prior to the time of trade. This is in response to your February 27, 1986 letter and our prior telephone conversation concerning the application of Board rules to the description of municipal securities exchanged at or prior to the time of trade. You note that it is becoming more and more common in the municipal securities secondary market for sellers, both dealers and customers, to provide only a "limited description" and CUSIP number for bonds being sold. Recently you were asked by a customer to bid on \$4 million of bonds and were given the coupon, maturity date, and issuer. When you asked for more information, you were given the CUSIP number. You then bid on and purchased the bonds. After the bonds were confirmed, you discovered that the bonds were callable and that, when these bonds first came to market, they were priced to the call. You state that the seller was aware that the bonds were callable.

Your letter was referred to a Committee of the Board which has responsibility for interpreting the Board's fair practice rules. That Committee has authorized this response.

Board rule G-17 provides that

In the conduct of its municipal securities business, each broker, dealer, and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice. (emphasis added)

⁴ See [Rule G-30 Interpretation - Interpretive Notice on Pricing of Callable Securities] August 10, 1979 ... at ¶ 3646.]

The Board has interpreted this rule to require that, in connection with the purchase from or sale of a municipal security to a customer, at or before execution of the transaction, a dealer must disclose all material facts concerning the transaction which could affect the customer's investment decision and not omit any material facts which would render other statements misleading. The fact that a municipal security may be redeemed in-whole, in-part, or in extraordinary circumstances prior to maturity is essential to a customer's investment decision and is one of the facts a dealer must disclose.

I note from our telephone conversation that you ask whether Board rules specify what information a customer must disclose to a dealer at the time it solicits bids to buy municipal securities. Customers are not subject to the Board's rules, and no specific disclosure rules would apply to customers beyond the application of the anti-fraud provisions of the federal securities laws. I note, however, that a municipal securities professional buying securities from a customer should obtain sufficient information about the securities so that it can accurately describe these securities when the dealer reintroduces them into the market.

In regard to inter-dealer transactions, the items of information that professionals must exchange at or prior to the time of trade are governed by principles of contract law and essentially are those items necessary adequately to describe the security that is the subject of the contract. As a general matter, these items of information may not encompass all material facts, but must be sufficient to distinguish the security from other similar issues. The Board has interpreted rule G-17 to require dealers to treat other dealers fairly and to hold them to the prevailing ethical standards of the industry. Also, dealers may not knowingly misdescribe securities to another dealer.]