

MEMORANDUM

TO: Kara Bringard
Office of Congressional Affairs

FROM: Mary N. Simpkins, Senior Special Counsel
Office of Municipal Securities

RE: Important Reforms and Events in the Municipal Market During Chairman
Arthur Levitt's Tenure

DATE: December 22, 2000

1. Reform of the municipal debt markets by eliminating pay-to-play; adoption of MSRB Rules G-37 and G-38

Early in his tenure Chairman Levitt asked municipal market participants to take voluntary measures to end conflict of interest practices such as pay-to-play. Dealers acted voluntarily, and then adopted a ban through their self-regulatory body, the Municipal Securities Rulemaking Board. In April 1994, the MSRB enacted Rule G-37, which prohibits brokers, dealers and municipal securities dealers, municipal finance professionals, political action committees and brokers and dealers from engaging in any negotiated municipal finance business with an issuer for two years after making a political contribution to an official of that issuer. MSRB Rule G-38, adopted in January 1996, requires disclosure of consulting arrangements.

Lawyers had been reluctant to act until a proposal was submitted to the American Bar Association ("ABA") by the Association of the Bar of the City of New York. A negotiated resolution that condemned political campaign contributions made by lawyers to influence the award of municipal securities contracts, called on state authorities to act against pay-to-play, and appointed a one-year task force to study whether additional measures were necessary, was passed by the ABA in August 1997. On February 14, 2000, after four years of controversy, the American Bar Association voted to adopt new ethics Rule 7.6. Rule 7.6 prohibits a lawyer or law firm from accepting government legal engagements or judicial appointments if they make or solicit political contributions for the purpose of obtaining the business or position. State bar groups that write disciplinary rules will decide whether or not to adopt the ABA Standard.

2. Establishment of first Office of Municipal Securities at the Commission

The Office of Municipal Securities ("OMS"), established on March 22, 1995, provides expertise to the Commission and staff, assists on municipal securities enforcement

cases, coordinates disclosure rules and other ongoing municipal regulatory initiatives, and addresses new issues that arise in the municipal area. In addition, the office provides assistance on legislative matters and works directly with issuers, investors, brokers, municipal securities dealers, and other professionals on issues relating to municipal securities. OMS provides expertise to those inside and outside of the Commission on issues concerning the municipal securities markets.

3. Improved price transparency

Chairman Levitt challenged the municipal bond industry to do more to provide comprehensive municipal bond price data to investors. The Municipal Securities Rulemaking Board began providing daily summary reports of interdealer municipal bond trades in 1995, and expanded the reports to include customer-trading data in 1998. The Bond Market Association now posts MSRB municipal bond trading reports on its Internet site (www.investinginbonds.com) for municipal bonds that trade four or more times on the reported day. Each daily report typically includes about 1000 issues out of the 1.4 million issues that are outstanding.

On October 10, 2000 the Securities and Exchange Commission approved a change to MSRB Rule G-14 that will institute a service to provide historical information on all transactions in municipal securities. The Comprehensive Transaction Report will be made available on a delayed (historical) basis, once a month, covering the previous month's trading. The MSRB is establishing a fee of \$2,000 for an annual subscription to the service.

As experience is gained with reporting of all transactions on a delayed basis, the MSRB will evaluate how best to expand price reporting in subsequent steps. As the MSRB previously has noted, its goal is ultimately to provide comprehensive and contemporaneous transaction reports to the market.

4. Adoption of Amendment to Rule 15c2-12, which requires issuers to contractually commit to bondholders that they will provide ongoing disclosure

Rule 15c2-12 was amended in 1994 to include certain continuing disclosure requirements. An underwriter subject to the rule may not purchase or sell municipal securities unless the issuer of those securities, or an obligated person for whom financial or operating data is presented in the final official statement, has undertaken in a written agreement to provide certain ongoing annual financial information. The information is filed with each nationally recognized municipal securities information repository, or NRMSIR, and to the appropriate state information depository, or SID, if any.

The rule also requires that notice of eleven events, if material, be filed with each NRMSIR or the MSRB and the appropriate, SID, if any. In addition, the rule requires notice to each NRMSIR or to the MSRB and appropriate SID, if any, notice of a failure of any person to

provided the required annual financial information on or before the date specified in the written agreement.

Three important releases were published by the Commission in 1994: an interpretive release regarding disclosure obligations in the municipal securities market (Release No. 34-33741), the proposing release for amendments to Rule 15c2-12 (Release No. 34-33742), and the adopting release for amendments to Rule 15c2-12 (Release No. 34-34961). Copies of these releases are attached.

5. Increased Enforcement Activity in the Municipal Market; Orange County, California; Historic “Yield-Burning” Settlements

Since 1994, the Commission has brought at least 17 injunctive proceedings and 74 administrative proceedings involving municipal market participants. The SEC has brought enforcement actions against more than 40 issuers of municipal securities and issuer officials for faulty disclosure in the last five years.

In early 1996, the Commission announced the most significant enforcement proceeding against an issuer of municipal securities in the Commission’s sixty-year history. The Commission settled its enforcement proceedings with the County and the County Board of Supervisors, as well as the former County Treasurer and Assistant Treasurer for misleading disclosure, including failure to reveal the risks associated with investing in the pools and certain facts affecting the tax status of the notes. The Commission also issued a Report of Investigation (“21A Report”) critical of the conduct of the members of the Board of Supervisors. The Commission also settled proceedings with the financial advisor, bond counsel and underwriter in those cases. The Commission also initiated proceedings against several communities in California that issued notes to invest in the pool, alleging failure to disclose the purpose of the borrowing and risks associated with the investment.

In April 2000, the Commission announced that it had brought and settled civil administrative fraud charges against 10 Wall Street and regional brokerage firms for overcharging municipalities for government securities in a practice commonly known as “yield burning.” The settlements were part of a global resolution of all yield-burning claims with a total of 17 brokerage firms by the SEC, NASD Regulation, Inc., the United States Attorney for the Southern District of New York, and the Department of the Treasury. This global resolution requires the firms to pay a total of more than \$120 million to the United States Treasury. Those payments will preserve the tax-exempt status of more than 3,600 separate issues of municipal bonds. In addition municipalities will receive directly more than \$18 million. The payments made by the firms in the global resolution are the largest settlement in any municipal securities case, and among the largest ever paid in any SEC settlement. (Together with previously and subsequently settled yield-burning actions, over 30 brokerage firms have paid almost \$200 million in connection with over 3,700 tax-exempt issues.)

6. Compendium of municipal securities cases

In April 1999, the Office of Municipal Securities prepared a compendium of all the significant municipal securities cases. A copy of this compendium is attached. We are currently preparing a supplement.

7. Outreach program to educate municipal issuers

In 1999, the Office of Municipal Securities began a series of municipal training sessions in different parts of the country to educate municipal issuers about their responsibilities under the securities laws when they issue municipal bonds. This outreach program is targeted toward smaller, less sophisticated issuers. The first session was held in Mississippi as part of the Mississippi Municipal Association's annual meeting in June 1999. Many of these presentations have been joint presentations with officials from the Internal Revenue Service. The program is continuing.

8. Commencement of SEC Municipal Market Roundtables

In October 1999, the Office of Municipal Securities held the First Annual Municipal Market Roundtable, and held a second roundtable in October 2000. The roundtables included three or four panels, with a cross section of the industry on each, including issuers, counsel, financial advisers, underwriters and investors. Panelists discussed a variety of concerns to participants in the municipal marketplace.

Attachments:

MSRB Rule G-37
MSRB Rule G-38
Rule 15c2-12

Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others (Interpretive Release Regarding Disclosure Obligations in the Municipal Securities Market), Securities Exchange Act Release No. 33741 (March 9, 1994), 59 Fed. Reg. 12748 (March 17, 1994).

Municipal Securities Disclosure (Proposing Release for Amendments to Rule 15c2-12), Securities Exchange Act Release No. 33742 (March 9, 1994), 59 Fed. Reg. 12759 (March 17, 1994).

Municipal Securities Disclosure (Adopting Release for Amendments to Rule 15c2-12),
Securities Exchange Act Release No. 34961 (November 10, 1994), 59 Fed. Reg. 59590
(November 17, 1994).

Compendium of Municipal Securities Cases, April 1999
Transcript of First Annual Municipal Market Roundtable
Agenda of Second Annual Municipal Market Roundtable