

2008

ANNUAL REVIEW



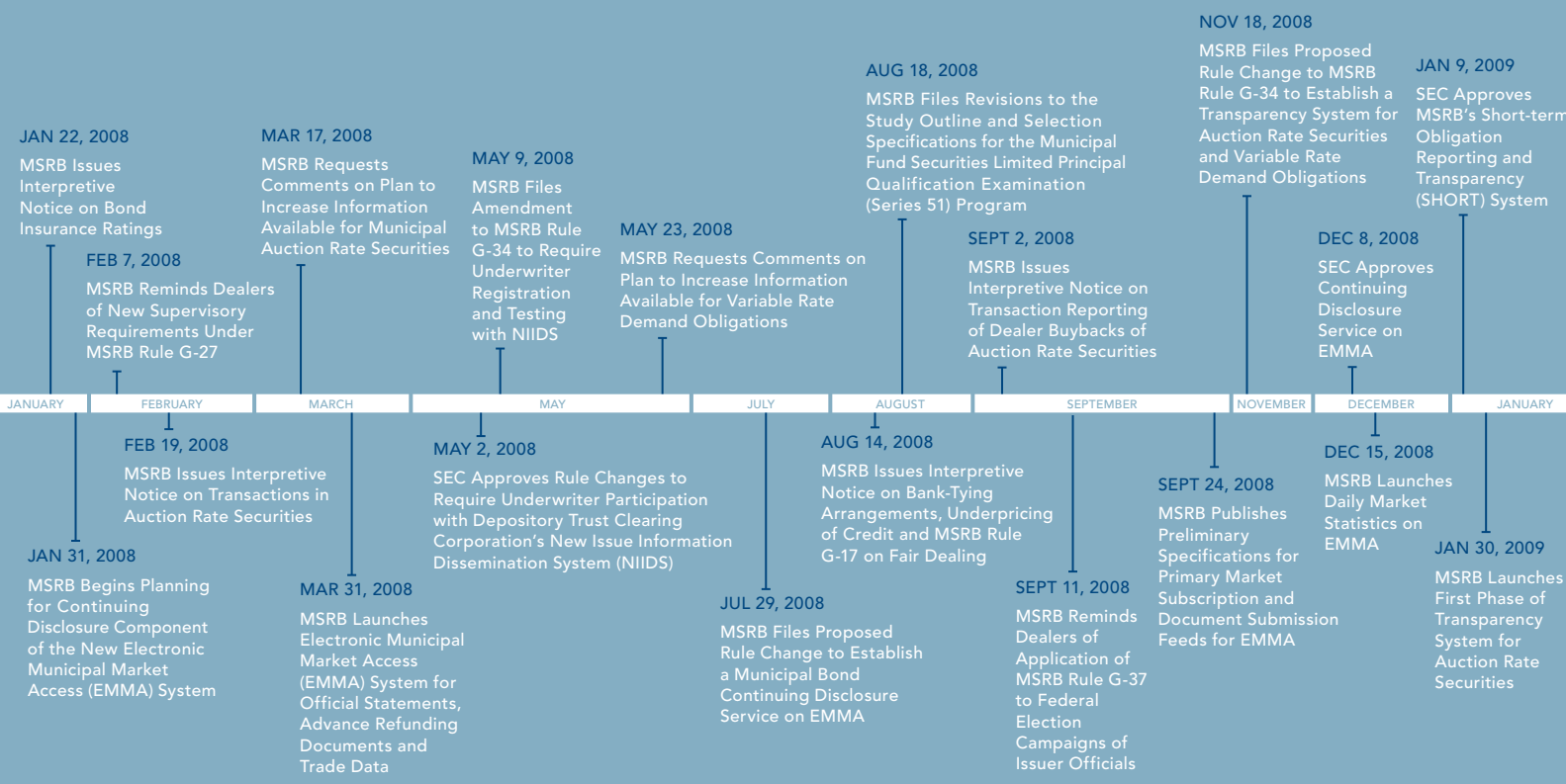
MSRB

Municipal Securities
Rulemaking Board



Highlights of MSRB Rulemaking and Information System Activities

(JAN 2008–JAN 2009)



About the MSRB

MUNICIPAL SECURITIES RULEMAKING BOARD

The Municipal Securities Rulemaking Board (MSRB) was established in 1975 by Congress to develop rules regulating securities firms and banks involved in underwriting, trading and selling municipal securities. The MSRB also operates information systems, including the Electronic Municipal Market Access (EMMA) system, designed to promote transparency and access to municipal bond information. The MSRB also conducts extensive outreach and education. The MSRB is composed of members from the municipal securities dealer community and the public, and is charged with protecting investors and promoting a fair and efficient market. The MSRB is a self-regulatory organization that is subject to oversight by the Securities and Exchange Commission.

Letter from the Chair



Ronald A. Stack

The municipal bond market—indeed modern financial markets generally—have over the last year encountered the kind of upheaval that comes once in a generation. The financial market dislocation that occurred on Wall Street has rippled out to Main Street and beyond, severely affecting most every individual, corporation, institution and government that borrows or invests money.

The municipal securities market, so fundamental to financing our nation's infrastructure, was swept up in the turmoil and subjected to repeated blows: the collapse of the monoline bond insurers and the subsequent downgrade of thousands of municipal bond issues; the paralysis of the auction rate market and a virtual freeze on liquidity in the credit markets; the seizing up of liquidity at the short end of the market; and then, the virtual exodus of institutional investors from the market.

Municipal bonds are the principal way in which state and local governments finance critical public-purpose projects such as roads, bridges, hospitals, airports and even drinking water facilities. The series of events that hammered the market in 2008 came at a particularly difficult time as the nation's infrastructure needs have reached a critical point.

At the same time, state and local governments are facing unprecedented budget crises, putting tremendous pressure on their capital needs. We are hopeful that states and the federal government quickly find solutions to the municipal market's capital-raising challenges. The MSRB has worked to educate policymakers and Congress about possible approaches for assistance, and we continue to offer our expertise wherever needed.

Despite the challenges, new municipal bonds are managing to come to market and trading continues in the secondary market. And investors, as always, are protected by the rules, standards and market transparency provided by the MSRB.

Over the last year, we enhanced and strengthened our tools for protecting investors in ways small and large. As a rulemaking body, we naturally focus closely on the rules of the road for broker-dealers and banks, including rules covering customer protection, market integrity, professionalism and market efficiency. But we have also established information services and provided education to market participants in furtherance of our investor protection mandate.

To further enhance rules-based customer protection in the current market environment, the MSRB moved quickly to provide important guidance to dealers on their fair practice and disclosure duties to customers in the face of bond insurers' rating downgrades that affected thousands and thousands of outstanding issues, and again as

the auction rate market ground to a standstill.

We emphasized the duty to ensure that customers are informed of the material facts about their transactions in light of the market changes, to make recommendations that are suitable taking into account such changed facts, and to ensure that pricing of transactions properly reflects the new facts about the securities. Later, as conversions from auction rate programs to other variable rate programs took off, the MSRB reminded the industry of federal bank-tying prohibitions that could come into play where a bank-affiliated dealer might directly or indirectly condition the provision of a credit or liquidity facility on the underwriting or remarketing of a bond issue.

During the election season, the MSRB also reminded securities dealers about the strict prohibition on using political contributions to influence the underwriter selection process. And as the new year unfolded, the MSRB's rules, and in particular the MSRB's groundbreaking rule that has preserved the integrity of relationships between broker-dealers and state and local government issuers by ending the practice of dealers being awarded municipal securities business based on political contributions, emerged as a potential model for unregulated participants in the municipal market.

Meanwhile, we have focused on our ambitious program to move the municipal market to a real-time, all-electronic standard for disseminating disclosure documents, trade prices and other

information. When this effort is completed this year, our market will establish a standard whereby investors and the general public have immediate electronic access to all offering documents for municipal bonds.

The vehicle for providing this information—and much more—to investors is the MSRB's Electronic Municipal Market Access website, or EMMA, which we proudly launched as a pilot program in 2008 at www.emma.msrb.org. This first-of-its kind website provides free on-line access to all official statements for municipal bonds since 1990, as well as current real-time trade data and historical trade data since 2005. For those unfamiliar with the municipal market, the advent of immediate—and free—access to disclosure documents for municipal bonds is a quantum leap forward for investors, particularly retail investors who traditionally have not been able to readily obtain these documents and current trade information.

In December 2008 the MSRB received approval from the Securities and Exchange Commission to expand EMMA to provide ongoing information from municipal bond issuers beginning in July 2009. These important “continuing disclosures” will be included as part of EMMA's integrated display of documents and trade prices provided

for each municipal security, allowing investors to access comprehensive information about municipal bonds in a single location and at no cost. EMMA also provides daily market statistics, an education center and other investor resources.

Beginning in January 2009, the MSRB has been disseminating through EMMA up-to-date interest rate information for municipal auction rate securities. For the first time investors have a free centralized venue to find this vital information. In the coming months, EMMA will incorporate additional key market data on municipal auction rate securities as well as variable rate demand obligations so investors—indeed all market participants—can fairly and adequately assess transactions in these securities. Disclosure and transparency in the municipal market have never been more critical and the MSRB is meeting that need.

In addition to the expansion of EMMA, the Board has launched a comprehensive review of the MSRB's general rules that govern dealers to ensure that they continue to be consistent with our statutory mandate and appropriately address existing and emerging products, practices and participants in the municipal securities market. This is a critical undertaking in light of the

events of last year, and our analysis will help guide our rulemaking efforts as we evaluate the market as a whole.

The MSRB also is calling on Congress, the Administration and fellow regulators to consider a regulatory scheme that covers unregulated participants in the municipal market providing advice to state and local government issuers. The MSRB is limited by its statute to overseeing the broker-dealer community, and we urge policy and lawmakers to evaluate all parties that do business in the market and regulate them as appropriate.

I am deeply grateful to be charged with the responsibility of guiding the Board during this tumultuous time. My fellow Board members and I are committed to ensuring that the MSRB fulfills its mandate to protect investors in every sector of the market. And we look forward to working with policymakers, lawmakers and the Administration to craft additional rules and develop additional information products needed to preserve the integrity, efficiency and fairness of the municipal market.



Ronald A. Stack

Chair, Municipal Securities Rulemaking Board

MUNICIPAL SECURITIES RULEMAKING BOARD 2008-2009

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Chair, MSRB
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Term ends 9/30/10



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Securities Corporation
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Term ends 9/30/09



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*President and
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Term ends 9/30/11



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Managing Director
Stifel Nicolaus & Co., Inc
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Term ends 9/30/09



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Senior Vice President
Duncan-Williams, Inc.
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Term ends 9/30/10



JOHN W. YOUNG II
Managing Director
Samuel A. Ramirez & Co. Inc.
New York, NY
Term ends 9/30/11

Rulemaking Activity

Over the last year, the MSRB put in place new rules and published interpretive guidance that focused on ensuring investor protection and promoting market transparency. All MSRB rules and rule amendments were approved by the Securities and Exchange Commission, an imprimatur that gives the rules the force of law.

NEW ISSUE DISCLOSURE

In 2008 the MSRB implemented rules that require bond underwriters to submit comprehensive information about new bond issues to a central information utility so it can be distributed to market participants before trading begins. Underwriter participation in the New Issue Information Dissemination System (NIIDS), operated by the Depository Trust

and Clearing Corporation, speeds and broadens dissemination of new issue information so that trade matching, price reporting and trade confirmation distribution can be completed more quickly, efficiently and accurately. The new rules also require underwriters to set and disseminate a “time of first execution” on most new issues, which gives market participants time to access necessary information in preparation for trade reporting prior to beginning trade executions in the issue.

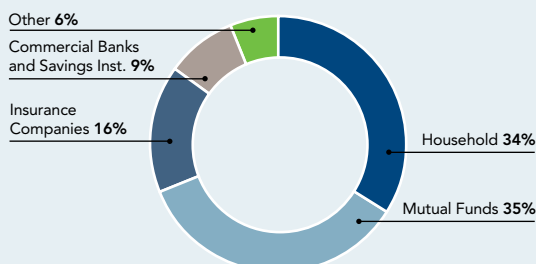
The MSRB rule change proposal to require underwriter participation with NIIDS was approved by the SEC May 2008. Before the

NIIDS centralizes information collection on new municipal bond issues, and improves timeliness and accuracy of new issue trade reporting.

MUNICIPAL SECURITIES INVESTORS

As of September 2008, more than two-thirds of the \$2.67 trillion outstanding municipal bonds were owned by individual investors either through their own brokerage accounts or mutual funds. The proportion of retail investors is significantly higher than in the early 1980s when individuals accounted for just a third of the municipal bond market. Other municipal bond investors include insurance companies and banks, whose presence in the market has declined since the early 1980s.

HOLDERS OF MUNICIPAL SECURITIES OUTSTANDING
As of September 2008



Total: \$2,669.0 Billion
Source: Federal Reserve Flow of Funds, December 2008

September 2008 NIIDS implementation date, the MSRB worked with DTCC to register underwriters with the new system and to train them in its use.

SHORT-TERM OBLIGATION TRANSPARENCY

Another key MSRB rulemaking initiative in 2008 focused on increasing transparency for municipal auction rate securities and municipal variable rate demand obligations. The MSRB filed a proposal with the SEC in November 2008 to require broker-dealers to report market information about these short-term municipal securities to the MSRB and to establish a system for disseminating the information to the public for free.

The SEC approved the MSRB's Short-term Obligation Rate Transparency (SHORT) system in January 2009 and municipal securities dealers began reporting interest rate and descriptive information about municipal auction rate securities at the end of that month. This information is made available for free on EMMA, the Electronic Municipal Market Access

website. Reporting requirements for variable rate demand obligations go into effect April 1, 2009, at which time rate reset and related information also will be made available for free on EMMA.

Throughout 2009, the MSRB will be implementing additional phases of SHORT to provide the market with a more complete picture of these types of transactions. SHORT will be expanded to collect bidding information on auction rate securities to provide the market with insight into the depth and nature of the market for an auction rate security as one indicator of its liquidity.

GENERAL RULES REVIEW

In the fall of 2008, the MSRB initiated a proactive review of its "G," or general, rules to ensure investor protection in a rapidly evolving market. The MSRB recognizes that financial markets are dynamic and periodic assessment of existing rules is required to maintain a relevant regulatory structure. The events of 2008 make this undertaking even more important.

The MSRB is developing additional phases of SHORT during 2009 to provide market participants with increased information about municipal auction rate securities and variable rate demand obligations.

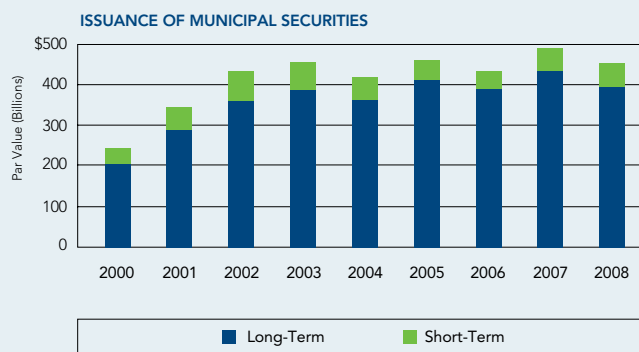
ADDITIONAL RULEMAKING

The MSRB completed a range of other regulatory changes in 2008. These changes are described below.

- Revisions to MSRB's Municipal Fund Securities Limited Principal Qualification Examination Series 51 program became effective in November 2008. The changes reflect developments in the 529 college savings plan market and were designed to ensure that professionals supervising dealer activities in this area have a thorough understanding of the application of MSRB rules to this product.
- Amendments to MSRB Rule G-27 on dealer supervision were implemented in February 2008. The changes harmonized many of the MSRB's supervisory requirements with those of the Financial Industry Regulatory Authority while also tailoring certain provisions to address the unique characteristics of the municipal securities market.
- An amendment to MSRB Rule G-8 on recordkeeping that removes certain recordkeeping requirements due to the modernization of the Form G-40 submission process went into effect on March 21, 2008.
- Amendments to MSRB Rules A-3 and A-4 relating to the nomination and election of members of the MSRB's Board of Directors and to meetings of the Board became effective on March 5, 2008. The changes were designed to promote diversity in Board membership and to permit the Board to respond more rapidly and efficiently to emergent issues.
- Amendments to MSRB Rule G-11 on new issue syndicate practices, and Rule G-12, on uniform practice, consolidated a number of syndicate practice provisions.

MUNICIPAL SECURITIES ISSUANCE

Due in large measure to the financial markets turmoil in the second half of 2008, overall issuance of municipal securities fell by 7% in 2008 to \$453 billion from \$488 billion in 2007, when issuance hit a record high. Over the last four years, new municipal securities coming to market have averaged \$458 billion per year. The municipal securities market includes all securities issued by state and local governments and their political subdivisions. More than 50,000 entities issue municipal bonds, including states, cities and counties, as well as airport authorities, housing finance authorities, educational institutions, and other public entities authorized to issue securities under state law. As of December 31, 2008, approximately 1.3 million municipal securities were outstanding with a total face value of more than \$2.67 trillion.



Source: Thomson Reuters

Regulatory Guidance

Throughout the year, the MSRB published a number of interpretive guidance notices and reminders to dealers of specific obligations under MSRB rules. Such regulatory guidance played an important role during 2008 as market developments unfolded that related to municipal market rules covering many dealer activities.

JANUARY 2008

In light of the widespread credit downgrades of bond insurance companies and their prominence in the municipal securities market, the MSRB reminded dealers of investor protection rules affecting transactions in insured municipal securities.

FEBRUARY 2008

Amidst the volatility in municipal auction rate securities, the MSRB provided guidance to dealers on the application of MSRB investor protection rules when effecting transactions in auction rate securities, particularly those rules on fair practice and suitability of recommendations.

AUGUST 2008

Following increased demand for liquidity facilities in the municipal securities market as many issuers sought to convert their auction rate securities to variable rate demand obligations, the MSRB became concerned about the potential for bank-tying activities whereby the availability or terms of loans or other credit products are conditional on the purchase of certain other products and services. The MSRB took the opportunity to remind dealers that it is illegal for banks to tie credit and debt underwriting from the bank or any of its affiliates.

SEPTEMBER 2008

During the election season, the MSRB reminded dealers that Rule G-37 on political contributions applies to issuer officials who campaign for any federal office. The MSRB also reminded dealers to be aware of the Rule G-37 issues involving indirect rule violations and contributions to non-dealer associated political action committees and payments to political parties.

MSRB regulatory guidance reinforces and interprets existing MSRB rules to help municipal securities dealers understand their requirements and obligations.

Information Systems and Market Transparency

EMMA MAKES HISTORY

During 2008, the MSRB began providing municipal bond investors with important disclosure and transparency information about municipal securities that historically had been difficult to access, particularly for individual investors. This historic achievement, executed through the launch of the MSRB's Electronic Municipal Market Access (EMMA) system in March 2008, cannot be overstated. The MSRB's success at overcoming barriers for investors to accessing municipal market information has resulted in a fundamentally changed market in which issuer disclosures and daily prices paid for municipal bonds are freely and immediately available to anyone at www.emma.msrb.org. Never before could ordinary investors obtain this kind of data in a centralized location and electronic format like their institutional counterparts. Today, all investors can easily access municipal bond official statements, advance refunding documents, interest rate information on auction rate securities, and real-time and historic trade data for all municipal bonds.

MARKET STATISTICS

In December 2008, the MSRB began publishing daily market statistics on EMMA that for the first time provide individual investors with free access, on a daily basis, to municipal market trading trends. Investors can now view snapshots of daily trade data

based on municipal security characteristics such as size, sector, maturity and source of repayment. The addition of these daily statistics is the first in a series of initiatives by the MSRB to provide investors with more extensive data on municipal bonds to help them better understand the market.

MUNICIPAL SECURITIES TRADING

During the period 2005–2008, an average of 36,000 transactions in municipal securities was reported to the MSRB each business day, resulting in par values averaging about \$23.2 billion per day. In 2008, daily average trading volume decreased to \$19.4 billion. The municipal securities market is an over-the-counter, dealer market. There are no central exchanges, specialists, or formal market maker designations. Approximately 2,000 securities firms and banks are authorized to act as brokers and dealers in municipal securities. During a given year, approximately 1,430 dealers report transactions in municipal securities to the MSRB under its price transparency program.



ARS AND VRDO TRANSPARENCY

In January 2009, the MSRB began collecting—and posting for public access on EMMA—interest rate and descriptive information for municipal auction rate securities (ARS). This is the first time such information has been readily available to the public. The MSRB will make similar interest rate information on variable rate demand obligations (VRDO) available beginning April 1, 2009, and follow that with the collection and dissemination of bidding information for ARS as well as documents for both ARS and VRDO.

CONTINUING DISCLOSURES

Beginning July 1, 2009, investors will have access to even more municipal bond disclosure information when EMMA makes available continuing disclosures about existing bonds. These documents, such as annual financial statements and

material event notices, are another important way for investors to evaluate the credit quality of individual securities trading in the secondary market.

REAL-TIME TRANSACTION REPORTING SYSTEM

During 2008, the MSRB refined and improved its collection of municipal bond transaction data from dealers. Enhancements to the MSRB's Real-Time Transaction Reporting System (RTRS) included the addition of a new report that provides trade information to correspondent dealers and parallels information that existing reports provide to clearing dealers.

MSRB GATEWAY

In 2008, the MSRB launched the first phase of the MSRB Gateway, a single secure access point for all MSRB applications. Dealers, enforcement agencies and information subscribers that use MSRB applications can now access these programs more efficiently and in a centralized way. The first phase, implemented in October 2008, provides centralized access to MSRB Forms G-40 and G-37 and to RTRS Web, the website for MSRB's transaction reporting system. MSRB primary contacts can create and manage user accounts and appoint account administrators on MSRB Gateway. Phase I also gave dealers the ability to electronically designate agents to submit primary market documents on their behalf.

The EMMA website provides free access to municipal bond offering documents, real-time and historic trade prices for municipal securities, and interest rate and auction results for municipal auction rate securities.

During 2008, the MSRB held industry-wide and individual meetings with many groups involved in the municipal securities market to work together on areas of mutual concern and to explain the MSRB's mission and activities.

MSRB ROUNDTABLE

In January 2008, the MSRB held its annual MSRB Roundtable, an important information-gathering event that brings together representatives from more than a dozen organizations, including the Government Accounting Standards Board, the Government Finance Officers Association, the Investment Company Institute, the National Association of Bond Lawyers, the National Association of State Auditors, Controllers and Treasurers, the National Association of State Treasurers, the Regional Bond Dealers Association (RBDA) and the Securities Industry & Financial Markets Association (SIFMA).

ADVISORY GROUP MEETINGS

The MSRB also met multiple times throughout the year with its Issuer and Investor Advisory Groups, made up of more than 20 industry representatives from the municipal issuer and investment communities. Other regular industry meetings included those with dealer members of RBDA and SIFMA.

COMPLIANCE TRAINING

Each year, the MSRB conducts training for dealer legal and compliance officials on new and existing information systems. In 2008,

the MSRB held its semi-annual compliance seminars in Chicago and New York City, and held additional seminars in Dallas, Chicago and New York to review testing and implementation of the Depository Trust and Clearing Corporation's New Issue Information Dissemination System (NIIDS). The MSRB also held a phone-in workshop on NIIDS and educational conference calls on the requirements of the Real-Time Transaction Reporting System.

The MSRB also held multiple webinars for dealers as part of MSRB's annual training on RTRS, as well as for MSRB Gateway and NIIDS.

529 COLLEGE SAVINGS PLANS

The MSRB hosted two regional compliance seminars regarding the MSRB rules applicable to the sale of 529 college savings plans. Held in Washington, D.C. and Chicago, Ill., these market outreach and educational sessions focused on compliance issues and recent MSRB initiatives relevant to the marketing of 529 college savings plans.

ENFORCEMENT TRAINING

The MSRB also provided updates and training for the agencies that enforce MSRB rules in the use of

transaction information in broker-dealer examinations and market surveillance. MSRB staff also met on a regular basis last year with the SEC and securities firm and bank regulators to keep them informed of MSRB activities.

MARKET LEADERSHIP

During 2008, the MSRB stepped up its outreach to federal lawmakers and policymakers and to help educate them about challenges facing the municipal market in the wake of the collapse of the broader financial and credit markets. The MSRB provided its municipal market expertise and data in meetings with President Obama's Transition Team, the Federal Reserve, the Department of the Treasury and Capitol Hill staffers. Early in January 2009, the MSRB recommended expanding federal municipal bond regulation to cover unregulated intermediaries such as financial advisors, swap advisors and investment brokers. The MSRB also provided Congress with specific recommendations in this area, including that the MSRB is the appropriate regulatory body to regulate these investment professionals.

MSRB SENIOR MANAGEMENT

Lynnette Kelly Hotchkiss, *Executive Director*

Harold L. Johnson, *Deputy Executive Director*

Ernesto A. Lanza, *General Counsel*

Janet Eakes, *Chief Operating Officer*

Melanie S. Richardson, *Chief Financial Officer*

Jennifer A. Galloway, *Chief Communications Officer*

As a self-regulatory organization, the MSRB's operations are financed solely through fees and assessments on securities firms and bank dealers engaged in the municipal securities business. Please click here <http://www.msrb.org/msrb1/pdfs/MSRBAuditReport2008.pdf>.

The MSRB writes rules for municipal securities dealers, operates information systems that support market transparency and disclosure,

and provides market leadership, outreach and education for the municipal market—each with the goal of furthering investor protection. This investor protection mandate is reflected in the MSRB's free public website for investors called EMMA, located at www.emma.msrb.org.

MSRB's day-to-day operations are handled by a 70-member staff based in Alexandria, Virginia.

**Municipal Securities Rulemaking Board**

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