MSRB
Municipal Securities
Rulemaking Board

Proposed Application of MSRB Rule G-17 to Underwriters of Municipal Securities*

With the passage of the Dodd-Frank Act, the MSRB was expressly directed by Congress to protect municipal entities. Accordingly, the MSRB is proposing to provide additional interpretive guidance that addresses how Rule G-17 applies to dealers in the municipal securities activities described below.

Scope of Notice

As clarified by the Amendment, the Notice would concern the duties of underwriters to municipal entity issuers of municipal securities ("issuers"). It would not address the duties of underwriters to obligated persons. The Notice would not apply to selling group members and, unless otherwise specified, the Notice would apply only to negotiated underwritings and not to competitive underwritings.

Role of the Underwriter/Conflicts of Interest

The Amendment would add a new section to the Notice, which would provide for robust disclosure by an underwriter as to its role, its compensation, and actual or potential material conflicts of interest. The disclosure would build on the disclosure already required by the Rule G-23 interpretive notice approved by the Commission in May of this year.[1] Certain of the required disclosures could be made by a syndicate manager on behalf of other syndicate members. The Notice would also prohibit an underwriter from recommending that the issuer not retain a municipal advisor.

The required disclosures would generally be required to be made at the time the underwriter is engaged to provide underwriting services and to be made to an official of the issuer with the power to bind the issuer by contract with the underwriter. The disclosure concerning the arm's-length nature of the underwriter-issuer relationship would continue to be required to be made at the earliest stages of the underwriter-issuer relationship, as required by the Rule G-23 interpretive notice. In the case of disclosures triggered by recommendations as to particular financings, as under the original proposed rule change, the disclosures would be required to be provided in sufficient time before the execution of a contract with the underwriter to allow the official to evaluate the recommendation. The disclosures required in the Notice under "Role of the Underwriter/Conflicts of Interest/Other Conflicts Disclosures" were included in the original proposed rule change. Pursuant to the Amendment, they would simply be included in the list of required disclosures, so that underwriters reviewing the Notice would only need to look to one place to see all the required conflicts disclosures. The underwriter would be required to

* Pending approval from the Securities and Exchange Commission (SEC)

[1] See SEC Release No. 34-64564, File No. SR-MSRB-2011-03 (May 27, 2011).

attempt to obtain the written acknowledgement of the issuer to the required disclosures and, if the issuer would not provide such acknowledgement, to document that fact.

Representations to Issuers

The Notice would provide that all representations made by underwriters to issuers of municipal securities in connection with municipal securities underwritings (e.g., issue price certificates and responses to requests for proposals), whether written or oral, must be truthful and accurate and may not misrepresent or omit material facts.

Required Disclosures to Issuers

As clarified by the Amendment, the Notice would provide that an underwriter of a negotiated issue that recommends a complex municipal securities transaction or product (e.g., a variable rate demand obligation with a swap) to an issuer has an obligation under Rule G-17 to disclose all financial material risks (e.g., in the case of a swap, market, credit, operational, and liquidity risks) known to the underwriter and reasonably foreseeable at the time of the disclosure, financial characteristics (e.g., the material economic terms of the swap, the material terms relating to the operation of the swap, and the material rights and obligations of the parties during the term of the swap), incentives, and conflicts of interest (e.g., payments received from a swap provider) regarding the transaction or product. Underwriters would also be required to inform the issuer that there might be accounting, legal, and other risks associated with a swap and that the issuer should consult with other professionals concerning such risks. Such disclosure would be required to be sufficient to allow the issuer to assess the magnitude of its potential exposure as a result of the complex municipal securities financing. Disclosures concerning swaps would also be required to be made only as to the swaps recommended by underwriters. If an issuer decided to accept the recommendation of a swap provider other than the underwriter, the underwriter would have no disclosure obligation with regard to that other provider's swap.

In the case of routine financing structures, underwriters would be required to disclose the material aspects of the structures if the issuer personnel did not otherwise have knowledge or experience with respect to such structures. The Amendment would clarify that any disclosures required to be made with respect to routine financings would be based on the underwriter's "reasonable belief" that issuer personnel lack knowledge or experience with such structures and be linked to whether the underwriter had recommended the routine financing.

The disclosures would be required to be made in writing to an official of the issuer whom the underwriter reasonably believed had the authority to bind the issuer by contract with the underwriter (i) in sufficient time before the execution of a contract with the underwriter to allow the official to evaluate the recommendation and (ii) in a manner designed to make clear to such official the subject matter of such disclosures and their implications for the issuer. If the underwriter did not reasonably believe that the official to whom the disclosures were addressed was capable of independently evaluating the disclosures, the underwriter would be required to make additional efforts reasonably designed to inform the official or its employees or agent.[2]

[2] Section 4s(h)(5) of the Commodity Exchange Act requires that a swap dealer with a special entity client (including states, local governments, and public pension funds) must have a reasonable basis to believe that the special entity has an independent

Underwriter Duties in Connection with Issuer Disclosure Documents

The Notice would provide that a dealer's duty to have a reasonable basis for the representations it makes, and other material information it provides, to an issuer and to ensure that such representations and information are accurate and not misleading, as described above, extends to representations and information provided by the underwriter in connection with the preparation by the issuer of its disclosure documents (e.g., cash flows).

New Issue Pricing and Underwriter Compensation

The Notice would provide that the duty of fair dealing under Rule G-17 includes an implied representation that the price an underwriter pays to an issuer is fair and reasonable, taking into consideration all relevant factors, including the best judgment of the underwriter as to the fair market value of the issue at the time it is priced. The Notice distinguishes the fair pricing duties of competitive underwriters (submission of bona fide bid based on dealer's best judgment of fair market value of securities) and negotiated underwriters (duty to negotiate in good faith). The Notice would provide that, in certain cases and depending upon the specific facts and circumstances of the offering, the underwriter's compensation for the new issue (including both direct compensation paid by the issuer and other separate payments or credits received by the underwriter from the issuer or any other party in connection with the underwriting) may be so disproportionate to the nature of the underwriting and related services performed, as to constitute an unfair practice that is a violation of Rule G-17.

Conflicts of Interest

The Notice would require disclosure by an underwriter of potential conflicts of interest, including the existence of third-party payments, values, or credits made or received, profit-sharing arrangements with investors, and the issuance or purchase of credit default swaps for which the underlying reference is the issuer whose securities the dealer is underwriting or an obligation of that issuer. The Amendment would clarify that the provisions of the Notice concerning disclosures of third-party payments and credit default swaps would require disclosure of the existence of third-party payments, but not the amount, and that particular transactions in credit default swaps would not be required to be disclosed under the Notice. These disclosures would draw the attention of issuers to such payments and credit default swap activity, and the issuers could choose to request more information from the underwriters.

Retail Order Periods

The Notice would remind underwriters not to disregard the issuers' rules for retail order periods by, among other things, accepting or placing orders that do not satisfy issuers' definitions of "retail."

Dealer Payments to Issuers

Finally, the Notice would remind underwriters that certain lavish gifts and entertainment, such as those made in conjunction with rating agency trips, might be a violation of Rule G-17, as well as Rule G-20.

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representative that has sufficient knowledge to evaluate the transaction and its risks, as well as the pricing and appropriateness of the transaction. Section 15F(h)(5) of the Exchange Act imposes the same requirements with respect to security-based swaps.



(b) The MSRB believes that the proposed rule change is consistent with Section 15B(b)(2) of the Securities Exchange Act ("Exchange Act"), which provides that:

> The Board shall propose and adopt rules to effect the purposes of this title with respect to transactions in municipal securities effected by brokers, dealers, and municipal securities dealers and advice provided to or on behalf of municipal entities or obligated persons by brokers, dealers, municipal securities dealers, and municipal advisors with respect to municipal financial products, the issuance of municipal securities, and solicitations of municipal entities or obligated persons undertaken by brokers, dealers, municipal securities dealers, and municipal advisors.

Section 15B(b)(2)(C) of the Exchange Act, provides that the rules of the MSRB shall:

> 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, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities and municipal financial products, to remove impediments to and perfect the mechanism of a free and open market in municipal securities and municipal financial products, and, in general, to protect investors, municipal entities, obligated persons, and the public interest.



MSRB NOTICE 2011-52 (SEPTEMBER 12, 2011)

POTENTIAL APPLICABILITY OF MSRB RULES TO CERTAIN "DIRECT PURCHASES" AND "BANK LOANS"

Introduction

The Municipal Securities Rulemaking Board ("MSRB") is aware that many state and local governments have turned to private placements of their municipal securities with banks (sometimes referred to as "direct purchases") and bank loans as an alternative to public offerings of municipal securities. In many cases, this shift is attributable to the pending expirations of letters of credits and standby bond purchase agreements providing liquidity for variable rate demand obligations ("VRDOs"). In other cases, these private placements and bank loans have taken the place of temporary cash flow borrowings previously accomplished with revenue anticipation notes ("RANs").

The MSRB has received a number of inquiries regarding the potential applicability of MSRB rules or other federal securities laws or regulations to direct purchases of municipal securities or bank loans placed in these contexts. As the MSRB has previously observed, private placements of municipal securities are subject to MSRB rules and other federal securities laws applicable to transactions in municipal securities.[1] In response to these recent inquiries, the MSRB is publishing this notice to alert municipal market participants that, under existing legal principles described below, certain financings that are called "bank loans" may, in fact, be municipal securities. If that is the case, and parties regulated by the MSRB[2] play a role in such financings, those parties may inadvertently violate MSRB rules, as well as other federal securities laws.

Securities Regulation of "Direct Purchases" and "Bank Loans"

If a broker-dealer serves as a placement agent for a "direct purchase" by a bank of municipal securities or as a placement agent for a "bank loan" that is, in fact, a municipal security, the broker-dealer is subject to all MSRB rules, as well as other federal securities laws. This is the case even if the broker-dealer is an affiliate of such bank or a separately identifiable department or division of the bank.[3] For example, as agent, a broker-dealer may effect a direct purchase of VRDOs by its bank affiliate followed by a restructuring of such VRDOs. In some cases, that restructuring may be so significant that it amounts to a primary offering of municipal securities.[4] In such a case, depending upon the broker-dealer's involvement in the purchase and restructuring, the broker-dealer may be obligated under MSRB Rule G-32 to report the restructured transaction to the MSRB. The same would be true of a broker-dealer that places a "bank loan" that is, in substance, a municipal security.

This obligation to report such a primary offering exists even though Rule G-32 does not require that copies of private placement memoranda be delivered to the MSRB. The reporting of such primary offerings serves important investor protection and market efficiency functions by ensuring that market information systems are able to properly record and disseminate to the marketplace information regarding any subsequent trading in such municipal securities or any continuing disclosures relating to such securities (including disclosures provided voluntarily for securities not subject to the continuing disclosure provisions of Exchange Act Rule 15c2-12). It also provides the enforcement agencies with an audit trail for purposes of their enforcement of MSRB rules and other federal securities laws. Furthermore, the

reporting of the baseline Rule G-32 information for such transactions alerts investors in other securities of the issuer to the existence of issuer debt that might be on a parity with, or senior to, their own holdings.

Among the other MSRB rules that might apply to a broker-dealer placing a bank financing that is a municipal security are: Rule A-13 (requiring broker-dealers to pay assessments on underwritings and placements of municipal securities), Rule G-3 (requiring broker-dealers engaged in municipal securities activities to pass qualifying examinations), Rule G-14 (requiring broker-dealers to report purchases and sales of municipal securities, including agency trades), Rule G-17 (imposing a duty of fair dealing on broker-dealers and municipal advisors in the conduct of their municipal securities and municipal advisory activities), Rule G-34 (requiring broker-dealers to obtain CUSIP numbers for municipal securities issues), and Rule G-37 (banning broker-dealers from engaging in municipal securities business for two years following non-*de minimis* political contributions to certain "issuer officials").

A municipal advisor that advises a state or local government issuer on whether to enter into a "bank loan" that is, in fact, a municipal security, or on a "direct purchase" by a bank of the issuer's securities followed by a restructuring of the securities that is considered a primary offering, is subject to the rules of the MSRB concerning municipal advisors. For example, a municipal advisor to a state or local government on a direct purchase and restructuring of VRDOs could be considered to provide advice on the issuance of municipal securities if such restructuring amounts to a primary offering. Such a municipal advisor would be subject to a federal fiduciary duty to the issuer under Section 15(c)(1) of the Exchange Act. The municipal advisor would, therefore, be required to act in the best interests of the issuer and advise the issuer of any risks associated with the transaction. The same would be true of a municipal advisor that advised a state or local government issuer on whether to enter into a transaction that, while called a "bank loan," is, in fact, a municipal security. The MSRB notes that Standard & Poor's has issued a report that highlights the risks such financings may pose for state and local governments, including repayment risks and the risk of cross-default on other obligations.[5]

"Bank Loans;" the *Reves* Case

Municipal securities that are purchased by banks and subsequently restructured do not lose their character as municipal securities. However, when banks make "loans" to state and local governments, even if only to provide a source of funds for those governments to purchase their own securities, whether such "loans" will be considered securities can be a difficult question.

Many loans are evidenced by notes. Section 3(a)(10) of the Exchange Act includes "notes" within the definition of "security." The principal legal authority on the distinction between a note that is a security from one that is not is the U.S. Supreme Court case of *Reves v. Ernst & Young, Inc.*[6] A note is presumed to be a security under the Supreme Court's opinion in *Reves* unless it is of a type specifically identified as a non-security.

The types of non-security notes identified in *Reves* include notes delivered in a consumer financing, notes secured by a mortgage on a home; short-term notes secured by a lien on a small business or its assets, short-term notes evidenced by accounts receivable, notes evidencing "character" loans to bank customers, notes formalizing open account debts incurred in the ordinary course of business, and notes evidencing loans from commercial banks for ordinary operations.[7]

A note that is not among the list identified in *Reves* is a security unless it bears a

"strong family resemblance" to the non-security notes identified in the opinion.[8] *Reves* established a four-part family resemblance test to determine whether a note is a security, which is composed of the following factors: (i) the motivations of the buyer and seller; (ii) the plan of distribution; (iii) the reasonable expectations of the investing public; and (iv) the existence of an alternate regulatory regime.[9] If a note fails the family resemblance test, it is deemed a security.

As to the first factor -- the motivations of the buyer and the seller -- the Supreme Court said that, if the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the instrument is likely to be a "security." On the other hand, if the note is exchanged to facilitate the purchase and sale of a minor asset or consumer good, to correct for the seller's cash-flow difficulties, or to advance some other commercial or consumer purpose, the note is less sensibly described as a "security."[10]

As to the second factor -- the plan of distribution -- the Supreme Court said the question is whether the note is an instrument in which there is "common trading for speculation or investment."[11]

As to the third factor -- the reasonable expectations of the investing public -- the Supreme Court said that it might consider instruments to be "securities" on the basis of public expectations, even where an economic analysis of the circumstances of the particular transaction might suggest that the instruments are not "securities" as used in that transaction.[12]

As to the fourth factor -- the existence of another regulatory scheme that significantly reduces the risk of the instrument, thereby rendering application of the securities laws unnecessary -- the Supreme Court said it would consider whether the notes would escape federal regulation entirely if the securities laws were held not to apply.[13]

Application of the *Reves* Factors to "Bank Loans"

Certain characteristics of some bank financings evidenced by notes may be indicative of securities, using the factors enumerated by the Supreme Court in *Reves*. An analysis of different bank financings may produce different results, depending upon the facts and circumstances. While the *Reves* case is the leading case on whether a note is a loan or a security, other court decisions and Securities and Exchange Commission ("SEC") guidance have also addressed the question. Dealers and municipal advisors that play a role in bank financings evidenced by notes should consult with their counsel on whether the financings are securities or loans, because whether the financing is called a "loan" is not necessarily dispositive of whether the financing is a loan or a security, and the consequences of failing to analyze such financings properly may be significant.

The SEC and the courts, and not the MSRB, ultimately have the authority to interpret the meaning of the term "security" for purposes of the federal securities laws. Because this notice is only an advisory, the MSRB has not filed it with the SEC for approval, and no inference should be drawn that the SEC or its staff has approved its publication. In issuing this notice, the MSRB intends to make dealers and municipal advisors aware that some financing instruments might be municipal securities. While the MSRB's intent is to draw attention to the factors to consider in determining whether an instrument is a security, the MSRB draws no legal conclusions regarding any individual instrument. Dealers and municipal advisors should consult with their legal counsel about the analysis of whether an individual instrument is a security.

The MSRB will continue to monitor evolving market practices and to consider the securities law implications of such changing practices. Although market participants must take primary responsibility for understanding the specific legal consequences of any transaction in which they participate, the MSRB will seek to provide further educational alerts as appropriate and to discuss with other regulatory authorities potential clarifications of their applicable rules and regulations in the context of such new market practices.

September 12, 2011

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[1] *See* MSRB Notice 2011-37 (August 3, 2011).

[2] Pursuant to Section 15B of the Securities Exchange Act of 1934 (the "Exchange Act"), the MSRB regulates brokers, dealers, and municipal securities dealers ("broker-dealers") engaged in municipal securities activities and municipal advisors engaged in municipal advisory activities.

[3] As defined in MSRB Rule G-1.

[4] Under MSRB Rule G-32(d)(viii), the term "primary offering" means "an offering defined in Securities Exchange Act Rule 15c2-12(f)(7), including but not limited to any remarketing of municipal securities that constitutes a primary offering as such subsection (f)(7) may be interpreted from time to time by the Commission." Exchange Act Rule 15c2-12(f)(7) provides that:

> The term "primary offering" means an offering of municipal securities directly or indirectly by or on behalf of an issuer of such securities, including any remarketing of municipal securities
>
> (i) That is accompanied by a change in the authorized denomination of such securities from $100,000 or more to less than $100,000, or
>
> (ii) That is accompanied by a change in the period during which such securities may be tendered to an issuer of such securities or its designated agent for redemption or purchase from a period of nine months or less to a period of more than nine months.

[5] Standard & Poor's, "The Appeal of Alternative Financing Is Not Without Risk for Municipal Issuers," (May 17, 2011).

[6] 494 U.S. 56 (1990).

[7] *Id.* at 65.

[8] *Id.* at 64-65.

[9] *Id.* at 66-67.

[10] *Id*. at 66.

[11] *Id*.

[12] *Id*. at 66-67.

[13] *Id*. at 67.

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MSRB to Delay Municipal Advisor Rule Proposals

Date: September 12, 2011

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MSRB TO DELAY MUNICIPAL ADVISOR RULE PROPOSALS

Alexandria , VA – The Municipal Securities Rulemaking Board (MSRB) today announced that it is delaying its municipal advisor rule proposals currently before the Securities and Exchange Commission (SEC).

Since being given regulatory jurisdiction over municipal advisors on October 1, 2010, the MSRB has been seeking to provide clarity to the municipal advisors registered under the SEC's temporary registration rule by advancing a core set of rules. However, given substantial concern regarding the timing of a permanent municipal advisor definition, the MSRB is delaying its proposed rules on fiduciary duty, pay to play, fair dealing, supervision, gifts and assessments until the SEC adopts a permanent definition under the Securities Exchange Act of 1934.

The MSRB has a statutory mandate under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) to protect municipal entities and regulate municipal advisors. The MSRB has sought to fulfill its Congressional mandate by soliciting broad input, issuing draft rules, seeking public comment and proposing core municipal advisor rules. Before the MSRB proposed its rules, it took into account the potential breadth of the definition of municipal advisor under the SEC proposal. However, the MSRB is concerned that because the definition has not been finalized, some firms and individuals will not participate in the SEC comment process on the MSRB proposals.

"We want to make sure that all potential municipal advisors are on notice that they could be affected by our rule proposals and have an opportunity to participate fully in the SEC comment process," said MSRB Executive Director Lynnette Kelly Hotchkiss.

The MSRB's rulemaking process for municipal advisors will continue. Once municipal professionals have certainty from the SEC regarding who is covered by the MSRB rules, the MSRB's rule proposals will be resubmitted to the SEC for approval.

The MSRB will act promptly once the SEC finalizes its definition of municipal advisor to ensure that there is a fair and level playing field for all municipal professionals and that the MSRB promotes issuer protection through the elimination of pay to play and establishing rules of conduct.

"We are committed to fulfilling our Dodd-Frank responsibilities through careful and deliberate rulemaking," Hotchkiss said. "We will continue to carry out this work to ensure that municipal advisors have clear guidance about their obligations under federal law."

The Municipal Securities Rulemaking Board (MSRB) protects investors, issuers of municipal securities and entities whose credit stands behind municipal securities, and public pension plans by promoting a fair and efficient municipal market. The MSRB fulfills this mission by regulating securities firms, banks and municipal advisors that engage in municipal securities and advisory activities. To further protect market participants, the MSRB promotes disclosure and market transparency through its Electronic Municipal Market Access (EMMA) website, provides education and conducts extensive outreach. The MSRB has operated under Congressional mandate with oversight by the Securities and Exchange Commission since 1975.

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MSRB NOTICE 2011-51 (SEPTEMBER 12, 2011)

MSRB WITHDRAWS PENDING MUNICIPAL ADVISOR RULE PROPOSALS

On September 9, 2011, the Municipal Securities Rulemaking Board (MSRB) withdrew the following municipal advisor rule proposals, which were pending with the Securities and Exchange Commission (SEC):

- SR-MSRB-2011-08 (July 26, 2011) (Proposed New Rule A-11, on Municipal Advisor Assessments, and New Form A-11-Interim);
- SR-MSRB-2011-10 (August 16, 2011) (Proposed Rule Change Consisting of Amendments to Rule G-20, on Gifts and Gratuities, Rule G-8, on Books and Records, and Rule G-9, on Preservation of Records, and to Clarify that Certain Interpretations by FINRA and NASD Would Be Applicable to Municipal Advisors);
- SR-MSRB-2011-12 (August 19, 2011) (Proposed Rule Change Consisting of Proposed New Rule G-42, on Political Contributions and Prohibitions on Municipal Advisory Activities; Proposed Amendments to Rules G-8, on Books and Records, G-9, on Preservation of Records, and G-37, on Political Contributions and Prohibitions on Municipal Securities Business; Proposed Form G-37/G-42 and Form G-37x/G-42x; and a Proposed Restatement of a Rule G-37 Interpretive Notice);
- SR-MSRB-2011-14 (August 23, 2011) (Proposed Rule Change Consisting of Proposed Rule G-36, on Fiduciary Duty of Municipal Advisors, and a Proposed Interpretive Notice Concerning the Application of Proposed Rule G-36 to Municipal Advisors); and
- SR-MSRB-2011-15 (August 24, 2011) (Proposed Interpretive Notice Concerning the Application of Rule G-17, on Conduct of Municipal Securities and Municipal Advisory Activities, to Municipal Advisors).

SR-MSRB-2011-13 (August 22, 2011) (Proposed Rule Change Consisting of Proposed New Rule G-44, on Supervision of Municipal Advisory Activities, Along with Related Proposed Amendments to Rule G-8, on Books and Records, and Rule G-9, on Preservation of Records) was already undergoing revision and will not be refiled at this time.

Upon the SEC's adoption of a permanent definition of the term "municipal advisor" under the Securities Exchange Act of 1934, the MSRB plans to resubmit these rule proposals.

September 9, 2011

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MSRB Fact Sheet



The MSRB protects the public interest by fostering a fair and efficient municipal market. The MSRB regulates the municipal securities dealers and municipal advisors that act as market intermediaries between issuers and investors, and promotes market disclosure and transparency through its Electronic Municipal Market Access (EMMA) website.

The MSRB and Municipal Market Integrity

All Americans, even if they don't realize it, benefit from municipal bonds. Schools, hospitals and highways are just some of our nation's infrastructure projects made possible by municipal bonds. Interestingly, it is the American public that largely provides municipalities the money to build and maintain the country's infrastructure. Individual investors own about two-thirds of the nearly $3.7 trillion in outstanding municipal securities, either directly or through mutual funds.

Maintaining the integrity of this large, public-purpose market is the responsibility of the MSRB, created by Congress in 1975 to oversee the municipal market.

EMMA and Municipal Market Transparency

The municipal market may be more transparent than you think. Users of the MSRB's free EMMA website, at **emma.msrb.org**, can access hundreds of thousands of disclosure documents, which include important information about the terms of a bond and about the issuer that can be used to evaluate the benefits and risks associated with investing. Issuers can also track the trading of their bonds and compare the terms of their offerings with other issuers.



emma.msrb.org

EMMA displays real-time trade data for 1.5 million outstanding municipal bonds, allowing EMMA users to track the trading activity of particular bonds and evaluate the market as a whole.

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FACT SHEET

EMMA®

THE OFFICIAL SOURCE FOR MUNICIPAL DISCLOSURES AND DATA

What Is EMMA?

The Electronic Municipal Market Access (EMMA) website, at **emma.msrb.org**, is a centralized online database that provides free public access to official disclosure documents associated with municipal bonds issued in the United States. EMMA also provides real-time trade data for approximately 1.5 million outstanding municipal bonds and current interest rates for auction rate securities and variable rate demand obligations. EMMA is operated by the Municipal Securities Rulemaking Board (MSRB), the self-regulatory organization that oversees the municipal market.

How Does EMMA Help Investors and Issuers?

EMMA provides transparency of information for investors in the $3.7 trillion municipal market and makes it easy for them to access information that can inform and enhance investment decisions. Municipal bond issuers use EMMA to submit disclosure documents. Issuers can learn about their own or comparable municipal securities. EMMA provides real-time trade data for each security, which allows investors and issuers to view the pricing of bonds in the secondary market and compare securities to each other.

What Municipal Bond Information Does the EMMA System Provide?

- Official statements and advance-refunding documents
- Continuing disclosure documents
- Real-time and historical trade data
- Interest rate resets and other data and documents for variable rate securities
- Preliminary official statements and notices of sale, in some cases
- Daily market statistics

What Other Information Is Available on EMMA?

EMMA also provides snapshots of daily trade data based on security size, sector, maturity and source of repayment, educational material about bonds and their associated documents, and a glossary of municipal bond terms.

Who Uses EMMA?

Investors and other municipal market participants interested in accessing information about the municipal securities market utilize the resources available on EMMA. Financial professionals also benefit from the information on EMMA, which assists them in evaluating various securities. In addition, members of the public, government officials and the media can view valuable municipal market documents on EMMA. All information on EMMA is available free of charge.



emma.msrb.org

How Often Is Information on EMMA Updated?

The MSRB collects and posts new information on EMMA every few minutes, including municipal bond-related documents and data about thousands of municipal bond trades. This continuous posting of information on EMMA keeps it a valuable and up-to-date database of documents and data available for researching the municipal bond market.

Finding Documents on EMMA

The easiest way to search for an official statement or continuing disclosure document on EMMA is to enter the CUSIP number associated with the security. Documents and data can also be found by entering a description of the bond issue, the state, maturity date or date of issuance into the site's search feature.

What Are Email Alerts?

Investors and others can sign up to receive an email alert when new disclosure documents for individual municipal securities are posted on EMMA. Each time a document is submitted for a particular security, EMMA will send an alert to anyone who has signed up to receive notification.

Upcoming Changes to EMMA

In fall 2011, the MSRB will make available on EMMA credit rating information for municipal securities. Ratings will be provided by one or more Nationally Recognized Statistical Rating Organizations (NRSROs). These ratings will assist investors in evaluating the general creditworthiness of a particular bond issuance.

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Six Things to Know When Issuing Municipal Bonds

State and local governments rely on the municipal securities market to raise money to finance projects for their citizens. Issuing bonds, whether done once a decade or many times a year, generally requires municipal governments to hire financial professionals to help.

The Municipal Securities Rulemaking Board (MSRB) plays an important role in defining the relationship that municipal governments have with financial professionals. It also plays a role in helping state and local governments communicate with investors. These activities are closely linked to how much it costs a state or local government to borrow money.

This document will explain six key things for state and local governments to know about issuing municipal bonds.

MSRB registration is required for underwriters and financial advisors.

When a state or local government issues a bond, an underwriter may help bring the bonds to market. A state or local government may also hire a municipal advisor, sometimes called a financial advisor, to provide advice before and during the issuance of a bond. Both underwriters and financial advisors are required to be registered with the MSRB and are subject to MSRB rules. State or local government issuers can check if their underwriters and municipal advisors are registered by visiting the MSRB's website, at **www.msrb.org** and clicking on the "Municipal Bond Market" tab. To view rules that apply to underwriters and municipal advisors, go to the "Rules" section of the MSRB's website.

Underwriters and municipal advisors can request a Certificate of Current MSRB Registration from the MSRB to provide to state and local government clients who request written verification.



Underwriters and municipal advisors must provide accurate information related to the sale of bonds.

State and local governments should expect a high level of professional conduct from both underwriters and municipal advisors. These financial professionals are required by federal law to act in ways that ensure state and local governments are not taken advantage of, defrauded or otherwise treated unfairly. MSRB rules require both underwriters and municipal advisors to deal fairly with state or local government issuers. These financial professionals are required to provide accurate information when giving advice or information related to the sale of bonds. They also cannot omit important information that is relevant for decision-making.

Underwriters must deal fairly with state or local government issuers in connection with all aspects of the underwriting of their municipal securities. This includes honoring commitments made to state or local government issuers regarding distribution of the issuer's securities. MSRB rules also prohibit conflicts of interest that can harm state or local government issuers. For example, effective November 27, 2011, underwriters cannot act as a financial advisor to a state and local government issuing a bond, and then become an underwriter on the same transaction.

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Municipal advisors owe a fiduciary duty to their state or local government issuer clients.

State and local government issuers should also know that municipal advisors are required by federal law to act in the best interests of their state and local government clients without regard to their own financial or other interests. This is called a "fiduciary duty." Municipal advisors must not let any financial relationships or interests they have prevent them from acting in the best interests of state or local government issuers that want to raise money at the lowest possible cost. Underwriters do not have a fiduciary duty to their state or local government issuer clients, but they must act fairly and not deceive state or local government issuers.

State and local governments can use different approaches to financing capital projects to borrow at the lowest possible cost.

In a competitive sale, underwriters submit bids to the issuers and the bonds are awarded to the underwriter that offers to pay the issuer the lowest interest cost. In a negotiated transaction, a state or local government issuer hires an underwriter that helps it find investors for the bonds.

During the pricing process, state and local government issuers have the right to assign underwriting liabilities. State and local government issuers are involved in determining which customer orders receive priority and defining what constitutes a retail order. Also, state and local government issuers have the right to determine how the bonds are distributed among investors. Underwriters are required to act in good faith with state and local governments and to honor primary offering practices as defined by the MSRB.

State or local government issuers can use the EMMA system to communicate important information directly to investors.

Issuing bonds also generally requires municipal governments to take certain steps to keep their investors informed, at the time of issuance and afterwards. These steps can reduce the overall cost of borrowing to the state or local government issuer. The MSRB operates the EMMA website as a centralized platform for state and local government issuers to communicate important information about themselves and their securities to municipal bond investors.

In addition to required disclosures, the MSRB allows state and local government issuers to voluntarily submit other categories of investment-related information, such as annual budgets. The MSRB also allows state and local government issuers to submit information about the timing and accounting standard used to prepare the annual financials. It is up to the state or local government issuer to decide whether or not to submit more information than what is minimally required although investors report that issuers with strong disclosure practices receive favorable pricing in the market.

State or local government issuers can use EMMA to track bond trading.

After a bond is issued, state and local government issuers will be able to easily track their bonds on EMMA by entering a CUSIP number or state or local government issuer name and selecting the "Trade Activity" tab. State or local government issuers can review the trading of their bonds and view the trade data available on EMMA for nearly 1.5 million outstanding bonds. On a typical trading day, the MSRB collects and disseminates information on an average of 40,000 trades.

Click here to view a video of this information.

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FACT SHEET

EMMA®

SIX WAYS TO USE EMMA

Submit continuing disclosure documents.

Pursuant to continuing disclosure agreements, municipal bond issuers and obligated persons must file continuing disclosures and related documents to EMMA. The EMMA system is the only official repository for continuing disclosure documents. Underwriters are required to provide official statements to EMMA on behalf of municipal bond issuers.

Learn about the continuing disclosure available for other bond transactions.

Both continuing disclosures made pursuant to a continuing disclosure agreement and those made voluntarily can be found under the EMMA website's continuing disclosure tab. A visual display of the timing agreed to by issuers for submitting annual financial information can be seen for most bonds issued on or after February 14, 2011.

Communicate other important information directly to investors.

The MSRB operates EMMA as a centralized platform for state and local governments to communicate important information to municipal bond investors and others. The EMMA website is the place to provide key financial disclosures to investors as well as other documents.

On a voluntary basis, issuers can provide:

- Pre-sale documents
- Notices of sale
- Advertisements announcing an upcoming new issue
- Official statements
- Advance refunding documents
- 529 plan disclosure documents
- Quarterly/monthly financial information
- Budgets
- Accounting standard used to prepare annual financials
- Material provided to rating agency or credit/liquidity provider
- Interim/additional financial information/operating data
- Derivative or other similar transaction, and
- Other voluntary information



emma.msrb.org

Track bond trading.

Issuers can easily track their bonds on EMMA by entering a CUSIP number or issuer name and selecting the Trade Activity tab. Issuers can review trading activity of their bonds and view the trade data available on EMMA for nearly 1.5 million outstanding bonds.

Learn about the structure of other bond transactions.

EMMA houses over 250,000 official statements and other primary market documents. These can be found using an issuer's name or a CUSIP number.

Track variable rate demand obligations.

EMMA is the only centralized, comprehensive database of current interest rate resets for variable rate demand obligations (VRDOs). State and local governments can use EMMA to compare the pricing of their VRDOs with other VRDOs.

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EMMA®

SUBMITTING CONTINUING DISCLOSURES TO THE EMMA SYSTEM

Submitting Continuing Disclosure Documents to EMMA

Since July 1, 2009, municipal bond issuers and obligated parties must file continuing disclosures and related documents with the Electronic Municipal Market Access (EMMA) system operated by the Municipal Securities Rulemaking Board (MSRB). These filing requirements are the result of changes made by the Securities and Exchange Commission (SEC) to SEC Rule 15c2-12. The EMMA system is the only official repository for continuing disclosure documents and issuers no longer need to file with multiple repositories.

In addition to being the repository for continuing disclosure documents, the EMMA system, at **emma.msrb.org**, also houses official statements, real-time and historical trade data, interest rates and auction results for auction rate securities, interest rates and liquidity documents for variable rate demand obligations, daily market statistics and educational material about municipal bonds. When issuers and obligors submit continuing disclosure documents to EMMA, they will be displayed on the EMMA website for public viewing and downloading.

Information for Issuers and Obligors

- Consult with their disclosure agent, disclosure counsel, bond counsel, financial advisor or trustee to learn more about their continuing disclosure obligations.
- Review continuing disclosure agreements (CDAs) to understand their obligations.
- Submit continuing disclosure documents to EMMA in word-searchable, PDF format.
- Consider submitting voluntary documents and information to the EMMA system.
- Prepare to register with the MSRB by having the following information available: an email address, organization name, address and phone number.

Information about how issuers and obligors get their EMMA submission accounts confirmed and how to designate agents to submit documents on their behalf can be found online by clicking on the EMMA Dataport tab at **emma.msrb.org**. Please refer to the Manual for Continuing Disclosure Submission.

Steps in Making a Continuing Disclosure Submission

1. **Create an account with MSRB and log in.**
   Go to **www.msrb.org** and go to the section "MSRB for…" and select "Issuers." Select the "Submit to EMMA" link and follow the on-screen instructions. Registration and subsequent secure access to EMMA operate through the MSRB's Gateway system.

2. **Specify the type of disclosure.**
   Submitters should select the type of disclosure they are making — either Financial/Operating Filing or Event Filing.

3. **Specify Rule 15c2-12 or voluntary.**
   Submitters must specify if the disclosure is being made pursuant to SEC Rule 15c2-12 or is an Additional/Voluntary disclosure.

4. **Specify municipal securities or issues.**
   Submitters must specify, or "associate," the securities or issues to which the disclosure relates. EMMA facilitates this by displaying all issues associated with a 6-digit CUSIP number. Submitters can select the relevant CUSIP-9s to which the disclosure relates.

5. **Add contact information.**
   The EMMA website will display at least one contact whom the public can reach to get more information about a disclosure. If a contact name is not entered, EMMA will display the submitter's contact information.

6. **Upload the document file.**
   Documents must be word-searchable PDF files. If the disclosure consists of more than one PDF file, submitters will be able to upload multiple PDF files.

7. **Publish the submission.**
   EMMA will confirm with the submitter that the disclosure is ready for publication.

8. **Save groups of securities and issues to use again.**
   Submitters can create and store a group of CUSIP numbers on EMMA for future use. These groups consist of all the CUSIP numbers associated with the completed disclosure.

9. **Receive an email record of submission from EMMA.**
   After publishing a submission, the submitter will receive an email receipt from EMMA confirming the disclosure has been made.

Click here to view a video on the continuing disclosure submission process.

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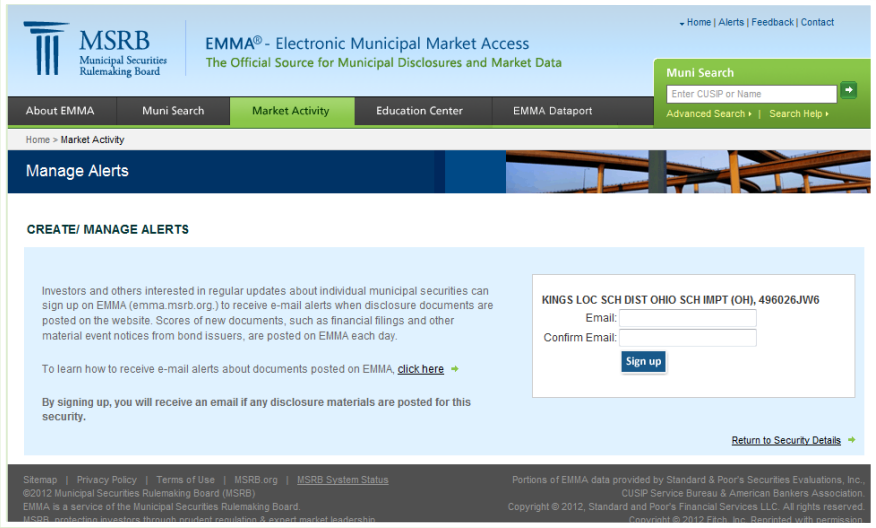
EMMA®

SIGNING UP FOR EMMA SYSTEM ALERTS

Anyone interested in receiving regular updates about individual municipal securities can sign up on the EMMA website to get email alerts when disclosure documents are posted and trades are reported. Many key documents, such as financial filings and other material event notices from bond issuers, are posted on EMMA each day.

Investors and issuers who track particular bonds can receive an email notification every time a new disclosure document is posted for that security as well as at the end of each day that the security trades. To sign up for alerts, go to EMMA, at http://emma.msrb.org, and follow the instructions below.



How to Sign Up for an Alert

- Enter a nine-digit CUSIP number into the "Muni Search" function.
- Click the arrow in the "Muni Search" box to navigate to the "Security Details" page for the bond.
- Click on the "Sign Up for Alerts" button then enter and confirm the email address to which you would like the alert sent.

Completing this process for any nine-digit CUSIP will create automatic delivery of email alerts whenever new documents are posted to the EMMA website associated with the CUSIP number(s) entered.

Manage Alert Preferences

- Follow the link in the email confirming that an alert has been set or select the "Alerts" link at the top of the screen to identify specific types of disclosures on which alerts will be sent.
- Elect to receive an end-of-day trade alert email on days that the security trades.
- Enter a list of CUSIP numbers to sign up for bulk alerts.

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ANNUAL REPORT 2011

MUNICIPAL SECURITIES RULEMAKING BOARD

MSRB
Municipal Securities
Rulemaking Board

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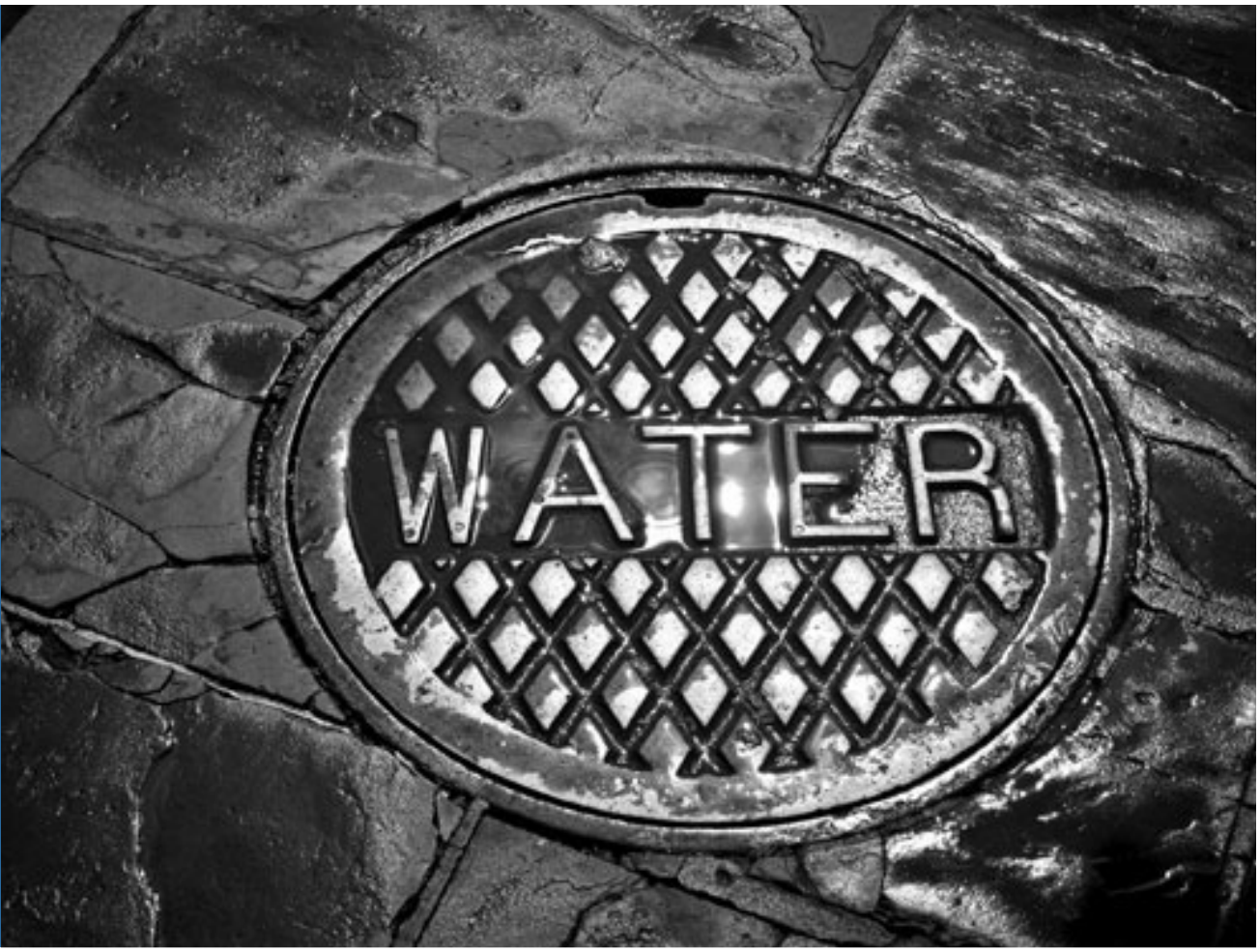


About the MSRB

The Municipal Securities Rulemaking Board (MSRB) protects investors, issuers of municipal securities and entities whose credit stands behind municipal securities and public pension plans by promoting a fair and efficient municipal market. The MSRB fulfills this mission by regulating securities firms, banks and municipal advisors that engage in municipal securities and advisory activities. To further protect market participants, the MSRB promotes disclosure and market transparency through its Electronic Municipal Market Access (EMMA®) website, provides education and conducts extensive outreach. The MSRB has operated under Congressional mandate since 1975.

The MSRB Board of Directors is composed of 21 members, including members of the public, municipal securities dealers and municipal advisors, and is a self-regulatory organization subject to oversight by the Securities and Exchange Commission. Members of the MSRB meet throughout the year to make policy decisions, approve rule-making, enhance information systems and review developments in the municipal securities market. The operations of the MSRB are primarily funded through assessments on dealers and municipal advisors. A professional staff in Alexandria, Virginia manages the MSRB's day-to-day operations.

LETTER FROM THE CHAIR



Last year represented a historic shift in the regulatory structure of the municipal market. The MSRB transitioned from a regulator of firms that underwrite and trade municipal securities to one with a broader mandate with the authority to also oversee municipal advisors.

This change has been accompanied by a shift in the composition of the MSRB Board of Directors from a majority of members representing regulated financial professionals to a majority of members representing the public.

At the same time, market and economic forces weighed considerably on municipal issuance and other activity. We continued to see the impact of the credit crisis that began in 2008 and affected all financial markets.

In August 2011, a major credit rating agency reduced the U.S. sovereign credit rating for the first time in history. This rating change affected some of the state and local government debt linked directly or indirectly to the U.S. sovereign credit rating.

New issuance of municipal bonds declined significantly in 2011 as state and local governments faced difficult financial decisions, including how to meet obligations associated with pension funds, an important source of retirement income for many former municipal employees.

The MSRB plays an important role in regulating the financial intermediaries in the municipal market and we act, within our jurisdiction, to address issues affecting the municipal market. The MSRB does not control investment outcomes or the value of municipal securities, but it does seek to ensure that the market operates fairly and efficiently.

More than ever, the MSRB recognizes the importance of ensuring investors and state and local governments have the information they need to make informed financial decisions. The MSRB's EMMA website has allowed the public to easily access a wealth of information about municipal bonds—for free. It has also transformed the way state and local government issuers communicate important information to investors.

As Chair of the MSRB, I believe it is important to discuss our initiatives with market participants to generate as much feedback as possible to help us make appropriate regulatory decisions. Robust and open discourse undoubtedly produces the best possible outcomes for the market.

I look forward to continuing to work with market participants to promote the fairness and efficiency of this vital market.



Alan Polsky
Chair, Fiscal Year 2012

IN 2011, THE MSRB INITIATED IMPORTANT SAFEGUARDS FOR MUNICIPAL ENTITIES AND INVESTORS.

LETTER FROM THE EXECUTIVE DIRECTOR

As an organization, the MSRB strives day in and day out to ensure the fair and efficient operation of the municipal market. The MSRB helps to ensure that state and local governments and investors are not defrauded or otherwise treated unfairly by market intermediaries working on their behalf.

Doing so requires a coordinated effort guided by a Board of Directors with the authority both to write rules for regulated entities and oversee the operations of the MSRB. This Annual Report outlines the work of the MSRB during fiscal year 2011 on behalf of investors and municipal entities.

In 2011, the MSRB initiated important safeguards for state and local governments that issue bonds—including rulemaking efforts related to the obligations of municipal securities dealers and municipal advisors. We also addressed conflicts of interest associated with financial advisor and underwriter role-switching during municipal bond transactions. These regulations will strengthen the foundation for issuer protection.

The MSRB continues to focus on investor protection and we promoted fair pricing for individual investors in the secondary market in 2011.

The MSRB remains committed to improving market transparency.

During 2011 we made numerous enhancements to our EMMA website that provide additional information to the market, including expansion of disclosures associated with variable rate demand obligations and additional continuing disclosure information. Just as the calendar year closed, the MSRB began to display credit ratings on EMMA.

Last year, the MSRB also formalized its market leadership function to ensure the organization stays apprised of market activities. The MSRB operates in a unique position at the nexus of market activity and can provide expertise and recommendations on particular issues. The MSRB does not represent or advocate on behalf of any segment of the market but does have the obligation to provide leadership when it believes that doing so will result in a fairer and more efficient market for all participants.

As we head into 2012, the MSRB is positioned to fulfill its mission to protect municipal entities and investors, and serve the market as a whole by ensuring that information is available for all participants to make informed decisions that meet their needs.

Lynnette Kelly

Lynnette Kelly
Executive Director



Market Regulation

MSRB rules, which have the force of federal law, seek to ensure that investors and issuers are treated fairly and that they have information to make informed financial decisions. After careful consideration of alternatives, the MSRB proposes rules that undergo a thorough review process, which includes public comment periods and approval by the Securities and Exchange Commission (SEC), before they are adopted to allow for consideration of the interests of all market participants. The MSRB also issues interpretations of its rules, which also have the force of federal law when approved by the SEC.

The MSRB sets rules for several different types of financial professionals, including municipal securities underwriters. During 2011, the MSRB saw the need to clarify the relationship of an underwriter to its issuer client as a way of protecting the issuer's interests. The MSRB proposed an interpretation of its fair dealing rule that establishes for the first time comprehensive guidance on the professional conduct issuers can expect from their underwriters in terms of representations, disclosures, compensation, new issue pricing and conflicts of interest.

IMPLEMENTING DODD-FRANK

When state and local governments issue new bonds, they often hire municipal advisors, sometimes called financial advisors, to represent their interests. Last year, the MSRB began to lay the foundation for municipal advisor regulation, as called for by Congress in the Dodd-Frank Wall Street Reform and Consumer Protection Act. Under the Dodd-Frank Act, municipal advisors owe a federal fiduciary duty to state and local governments when providing financial advice.

In 2011, the MSRB proposed a series of new rules and related interpretive notices to establish the key principles that would govern the regulation of municipal advisors. The MSRB expects to complete this initial phase of municipal advisor rulemaking in 2012 in conjunction with the SEC's completion of its own pending rule proposal to more clearly delineate the breadth of professionals covered by the Dodd-Frank Act's new regulation of municipal advisors.

The MSRB proposed a new rule and an associated interpretation covering the details of an advisor's fiduciary duty that would require municipal advisors to act in the best interests of their state or local government clients, disclose all material conflicts of interest, not undertake an engagement when an unmanageable conflict exists, and not charge excessive compensation. If approved, it also would require municipal advisors to review reasonably feasible alternatives to proposed products and transactions, and conduct a reasonable inquiry into the facts necessary to support representations made in certificates.

PROHIBITING CONFLICTS OF INTEREST

Prohibiting conflicts of interest on the part of financial professionals that could undermine the integrity of the municipal market is an important aspect of many MSRB regulations. One form of conflict of interest in the municipal market can occur if financial professionals seek to influence the award of business by government officials by making political contributions to those officials or soliciting them on their behalf. This activity can have a negative impact on market fairness and public confidence in elected officials.

The MSRB restricts these so called pay-to-play activities of dealers and last year proposed similar restrictions for municipal advisors. In 2011, the MSRB also proposed amending its rules to limit municipal advisor gift-giving, just as the MSRB's gift rule already does for dealers.

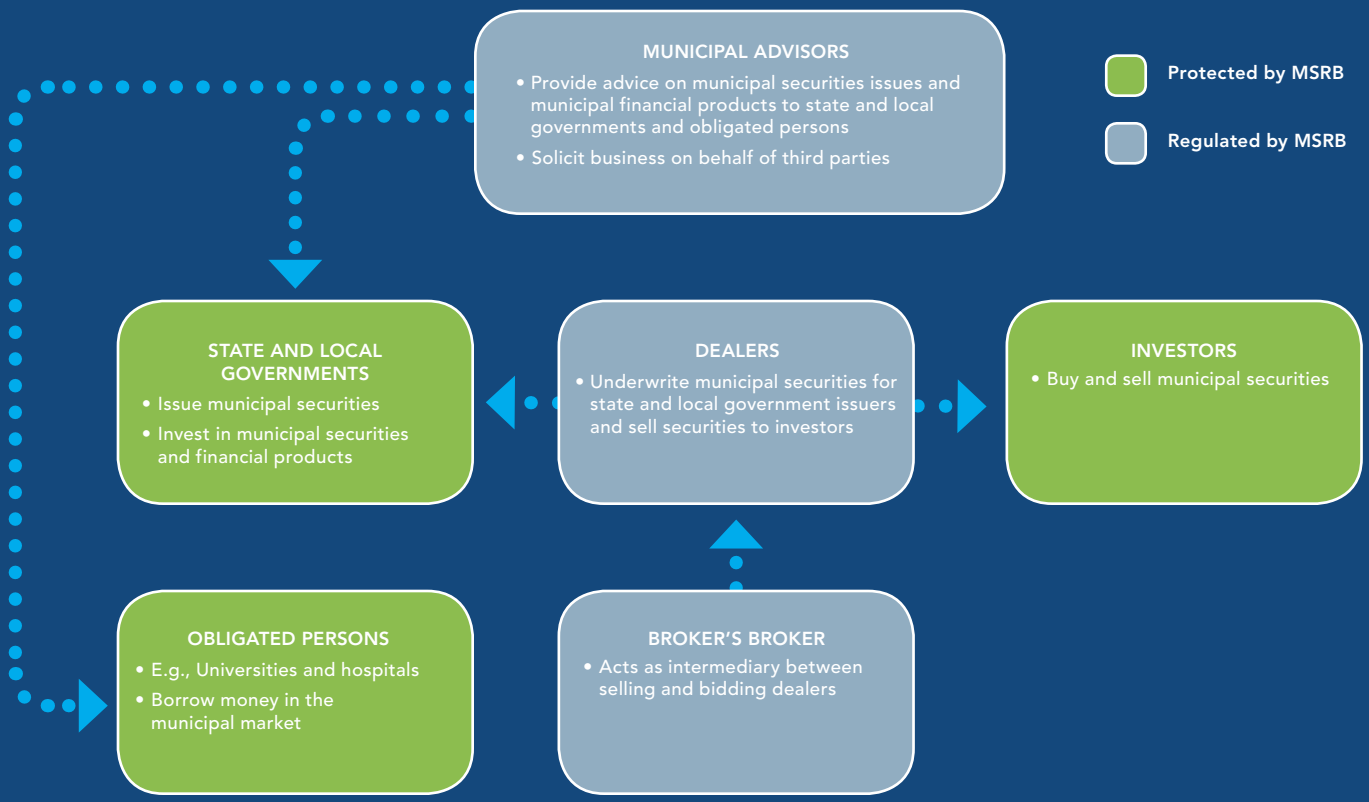
A rule change adopted by the MSRB to address potential conflicts of interests in the municipal securities market went into effect in 2011. The MSRB prohibited the practice of a dealer serving as a financial advisor to a state or local government client in connection with a new issue and then acting as an underwriter on the same transaction.

ESTABLISHING PROFESSIONAL QUALIFICATIONS

It is important that financial professionals in the municipal market have the qualifications necessary to provide their services competently to investors and state and local governments. MSRB rules govern the qualification, classification, disqualification, disciplinary actions and related professional requirements for municipal securities brokers and dealers. During 2011, the MSRB began developing similar qualifications for municipal advisors and is in the process of developing a draft content outline for a qualifying exam.

In 2011, the MSRB also acted to address an important investor protection issue. Brokers that buy and sell municipal securities often use the services of "broker's brokers" to help complete transactions. The conduct of

The MSRB and Municipal Market Regulation



broker's brokers with respect to pricing often is directly linked to the prices individual investors pay in the secondary market for municipal securities. In 2011 the MSRB requested comment on a draft rule that would govern the conduct of broker's brokers.

REGULATORY SUPPORT

The MSRB's market regulation activities include providing enforcement support to the regulatory authorities that enforce MSRB rules, including the SEC, the Financial Industry Regulatory Authority (FINRA) and federal bank regulators. The MSRB meets regularly with these fellow municipal market regulators to discuss proper enforcement of MSRB rules and interpretations as well as to discuss other market issues. The MSRB ensures that data from its information systems are available for enforcement activities and regularly trains regulators on using MSRB data for enforcement purposes. In 2011, the MSRB for the first time entered into an agreement to provide municipal market data to the Internal Revenue Service in connection with its enforcement of tax laws related to municipal securities. The MSRB also amended its rule regarding compliance examinations of broker-dealers and began working closely with FINRA to institute a risk-based method of ensuring that market participants remain in compliance with key MSRB rules.

Market Transparency

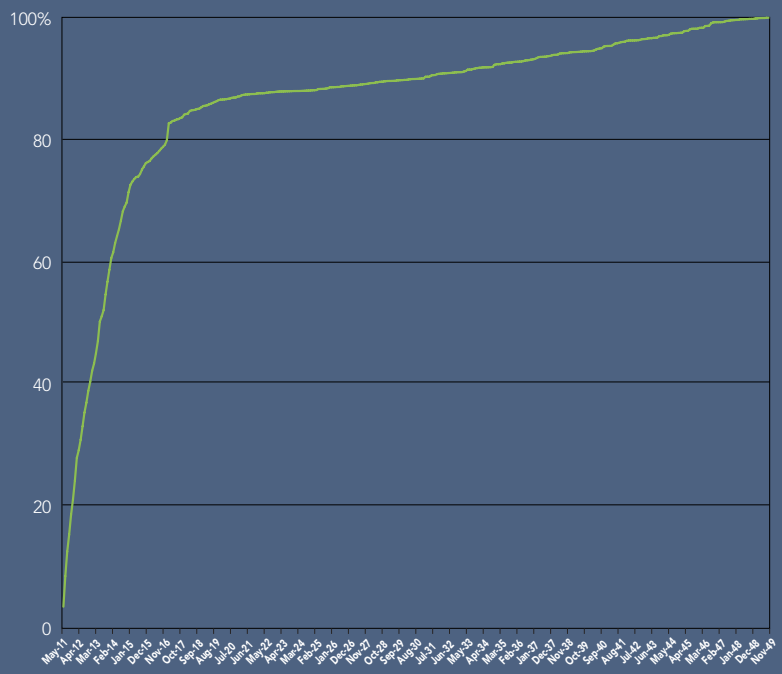


A key way the MSRB protects investors and municipal entities in the municipal market is by making market information as transparent and widely available as possible. By providing free access to municipal bond offering documents, continuing disclosures, trade data, interest rates and other information, investors and others can better understand the terms, characteristics and risks of a particular security. At the same time, the mechanisms of a transparent market allow issuers of municipal securities to provide information to existing and potential investors, and to gain a comprehensive view of the marketplace allowing them to compare their securities with other bonds.

ADDING TRANSPARENCY TO VRDOS

The MSRB's EMMA website provides unprecedented access to municipal bond data and disclosures—for free. In 2011, the MSRB continued its effort to enhance EMMA in ways that reflect changes in the marketplace. With the sharp increase in the expiration of liquidity facilities backing variable rate demand obligations (VRDOs) (see graph), the MSRB began making available to investors for the first time, documents that describe the liquidity features of VRDOs, such as letters of credit and stand-by purchase agreements.

PERCENTAGE OF VRDO PAR OUTSTANDING BY LIQUIDITY FACILITY EXPIRATION DATE



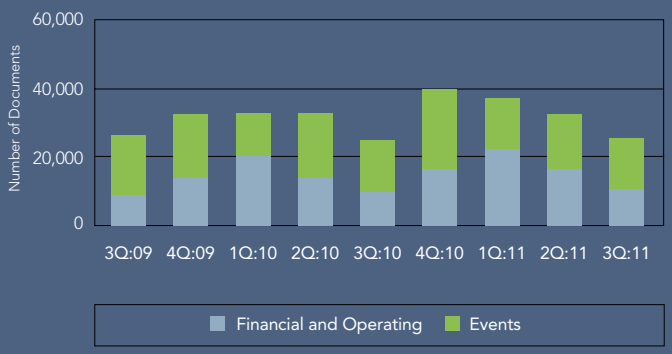
According to a July 2011 MSRB report, approximately 44%, or $142 billion, of liquidity facilities supporting VRDOs are set to expire by the end of 2012. The MSRB now makes documents describing a VRDO's liquidity features available on EMMA.

The MSRB also made additional information about auction rate securities available on EMMA in 2011, including bidding information on auction rate securities and documents describing auction procedures and how interest rates are set. While the market for auction rate securities has entered into a period of prolonged distress in recent years, transparency surrounding auction procedures allows investors who continue to hold auction rate securities and others to better understand important technical aspects of these securities. EMMA also displays a bid-to-cover ratio for each auction rate security.

During fiscal year 2011, the MSRB published a report summarizing key information submitted to the MSRB about VRDOs and ARS from early 2009 through April 2011. During this time,

THE MSRB'S EMMA® WEBSITE PROVIDES UNPRECEDENTED ACCESS TO MUNICIPAL BOND DATA AND DISCLOSURES FOR FREE.

NUMBER OF CONTINUING DISCLOSURES SUBMITTED TO THE MSRB
July 2009–September 2011



The MSRB's EMMA system has been the official repository for continuing disclosure documents since July 1, 2009. These documents provide investors with important financial and event-based information about municipal bonds.

approximately 2.15 million municipal VRDO rate resets and 68,061 ARS rate resets were reported to the MSRB.

In 2011, the MSRB supported more timely dissemination of continuing disclosure information in the marketplace by providing a visual display on EMMA of the date by which issuers of municipal bonds are expected to make annual financial information available so that investors can assess the timeliness of actual disclosures made each year. The MSRB also created a venue for state and local government issuers to indicate to the public on EMMA their commitment to provide their annual financial information on an accelerated basis as well as their adherence to generally accepted accounting principles. The MSRB also began displaying a confirmation from bond underwriters of issues for which the bond issuer has made a commitment to provide ongoing disclosures consistent with federal anti-fraud laws.

CONTINUING DISCLOSURE REPORTING

As part of its mission to educate about the municipal market, the MSRB periodically publishes reports summarizing key data it collects. Last year, the MSRB published its first report analyzing the type and number of continuing disclosure documents for municipal securities available on EMMA. Between July 2009 and June 2011, the MSRB received 258,162 continuing disclosure documents, of which approximately 46 percent constituted financial and operating disclosures and approximately 54 percent constituted event disclosures.

In addition to information displayed on EMMA that is submitted by state and local governments under continuing disclosure agreements, issuers can also voluntarily provide investors with access to key pre-sale documents. The MSRB launched this capability in May 2011 through an EMMA enhancement that displays certain pre-sale information, including preliminary official statements, voluntarily submitted by state and local government issuers.

STUDYING MARKET STRUCTURE

The MSRB also promotes municipal market transparency and a fair and efficient market through the collection and broad dissemination of post-trade municipal securities transaction data. During 2011, the MSRB began an important study reviewing transaction costs, price dispersion and other market data to help the MSRB assess whether the market is operating as efficiently and fairly as possible. The results of this study, expected in 2012, will assist the MSRB in evaluating further potential improvements to pricing mechanisms and liquidity in the market.

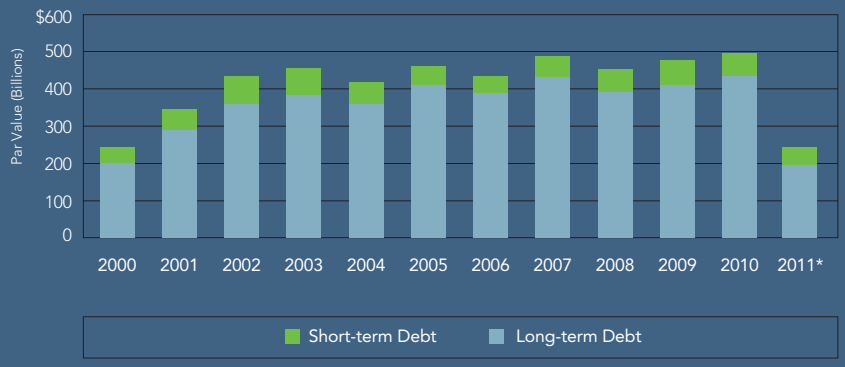
As part of its market transparency operations, the MSRB also collects official statements for municipal securities, which are available on EMMA and provide instantaneous marketwide access to key primary market disclosures. The MSRB also collects disclosures about political contributions made by municipal securities dealers pursuant to the MSRB's precedent-setting pay-to-play rule. These disclosures are accessible to the public on the MSRB's website, at www.msrb.org.

Market Facts



After reaching a record in 2010, municipal bond issuance fell sharply in 2011 through September, and was expected to end the year at the lowest level since 2002.

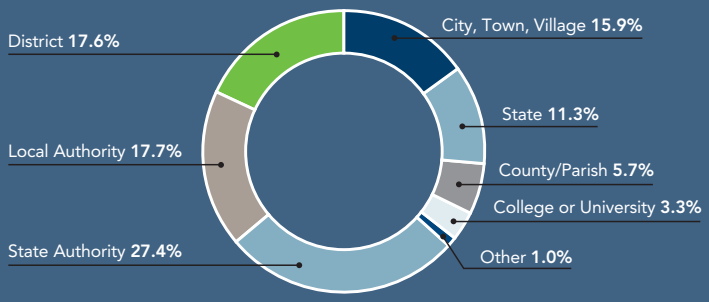
ANNUAL ISSUANCE OF MUNICIPAL SECURITIES
2000–2011*



*As of September 30, 2011
Source: Thomson Reuters

State authorities accounted for the largest share of municipal bond issuance in 2011 through September, and together with local authorities and districts, accounted for nearly two-thirds of overall volume.

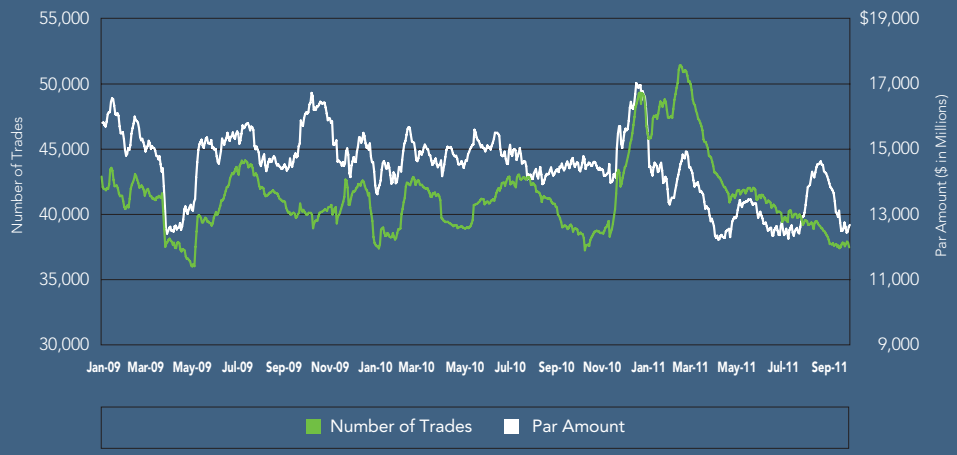
ISSUANCE OF MUNICIPAL SECURITIES BY ISSUER TYPE
2011*



*As of September 30, 2011
Source: Thomson Reuters

Trading activity of municipal bonds remained strong through the first nine months of 2011 and was on pace to surpass 10 million trades for the fourth consecutive year.

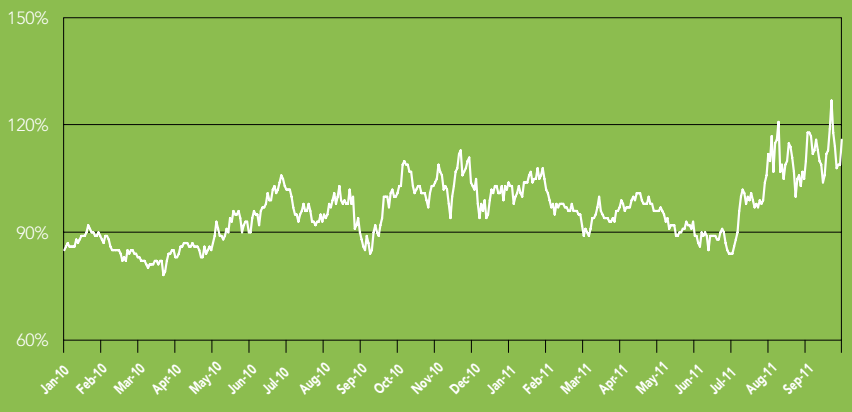
MUNICIPAL TRADING VOLUME
30-Day Trailing Average





Yields on municipal securities as a percentage of U.S. Treasuries spiked in August and September 2011, following the downgrade of the U.S. sovereign credit rating by Standard & Poor's.

MUNICIPAL YIELDS AS A PERCENTAGE OF TREASURY YIELDS
10-Year Maturity
January 2010–September 2011



Source: Bloomberg

Market Leadership



MSRB Executive Director Lynnette Kelly testifies before the U.S. Senate Committee on Banking, Housing and Urban Affairs.

The MSRB stays apprised of events and activities affecting the municipal market and acts within its jurisdiction to address them when needed. Monitoring the market and offering possible solutions helps ensure that MSRB initiatives appropriately address challenges and are relevant to market conditions.

For example, the MSRB often lends expertise to other regulators whose jurisdiction includes aspects of the municipal market, with the goal of providing an important perspective with which to make policy decisions.

During 2011, the MSRB provided the Securities and Exchange Commission (SEC) extensive written comments on its proposed final rule regarding the definition of municipal advisors. The MSRB generally supported the SEC's proposal, but suggested refinements to certain definitions and recommended that members of governing bodies of state and local governments be excluded from the definition of "municipal advisor" since Congress did not intend to regulate municipal entities' internal activities.

During 2011, the MSRB also submitted comments to the SEC on the updating of its guidance on federal laws governing disclosure in the municipal market.

In recent years with the development and expansion of the EMMA website, the MSRB has become a unifying force in what was previously a fragmented disclosure regime. In its letter to the SEC, the MSRB supported greater transparency in the primary market by recommending that the SEC expand disclosure requirements for variable rate demand obligation bonds, which are currently exempt. The MSRB also suggested that the SEC elaborate on the importance of market professionals' disclosure to investors of risk factors and conflicts of interest.

The MSRB also recommended the SEC improve secondary market disclosure by improving compliance by municipal securities issuers and obligated persons with terms of their continuing disclosure agreements. The MSRB suggested requiring issuers and obligated persons to make robust disclosures of previous breaches of continuing disclosure agreements in official statements for new issues of municipal securities.

TESTIFYING BEFORE CONGRESS

In another demonstration of market leadership in 2011, the MSRB was invited to testify in a hearing before the U.S. Senate Committee on Banking, Housing and Urban Affairs to discuss enhanced investor protection after the 2008 financial crisis. MSRB Executive Director Lynnette Kelly told the Committee about recent MSRB rulemaking and transparency initiatives aimed at protecting investors.

During 2011 the MSRB also participated in field hearings conducted by the SEC to discuss the role of self-regulatory organizations in the municipal market and MSRB initiatives to enhance municipal market transparency, specifically in the area of pre-trade price transparency.

On August 5, 2011, one of the most prominent credit rating agencies in the U.S., Standard & Poor's, downgraded the sovereign debt rating of the U.S. In response, the MSRB published guidance related to the application of MSRB investor protection rules. This guidance expressed concern about the treatment of retail investors and warned that any dealer that uses a financial market disruption to manipulate the pricing of municipal securities would be violating federal securities law.

MONITORING BANK PRODUCTS

Recently, state and local governments have begun using bank products as an alternative to traditional financing options. In response, the MSRB issued an advisory covering certain financings called "bank loans" that could, depending on the nature of the transactions, be placements of municipal securities, as well as certain "direct purchases" by banks of issuers' securities that are subsequently restructured so significantly that they may constitute primary offerings of securities. In cases where these bank products involve municipal securities transactions, the MSRB advised that the financial professionals involved are subject to all applicable MSRB rules and other federal securities laws.

Outreach and Education

As a self-regulatory organization, the MSRB relies on municipal market participants and other stakeholders to provide input that informs the rulemaking process. At the same time, the MSRB seeks to ensure that these stakeholders are aware of regulatory developments that may affect them.

As of October 2010, the MSRB assumed expanded jurisdiction to protect municipal entities, which includes state and local government issuers and public pension plans. To strengthen the MSRB's understanding of the issues affecting state and local governments, and to begin to develop a policy-making framework, the MSRB conducted several outreach forums around the country. In 2011, MSRB staff and Board of Directors members met with audiences around the country to help them understand how the MSRB and the market were changing as a result of the Dodd-Frank Act. The MSRB held outreach events in New York, NY, Chicago, IL, Los Angeles, CA, Austin, TX, Atlanta, GA and Denver, CO to discuss the changes and their implications for market participants.

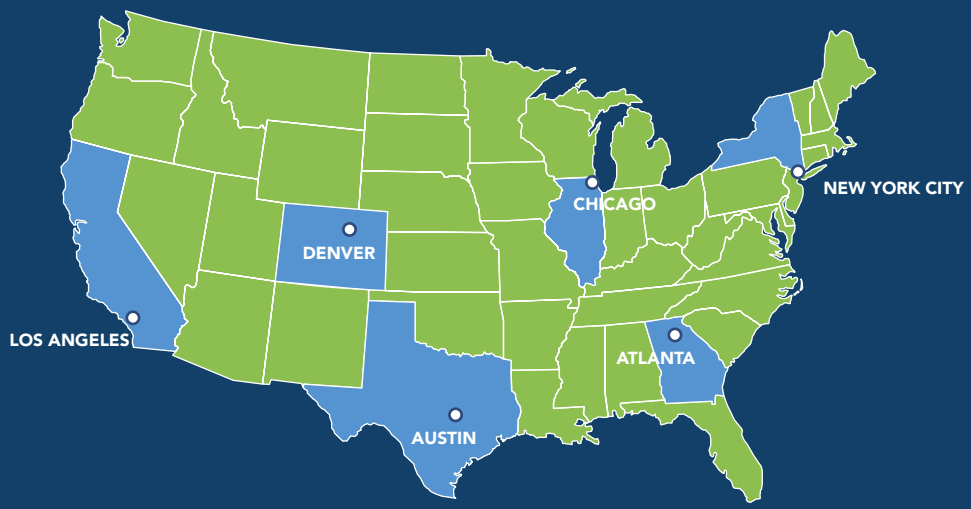
In January 2011, the MSRB hosted a roundtable dedicated to public pension fund issues and also conducted meetings and webinars with state and local government officials to discuss the concerns of issuers in the municipal market.

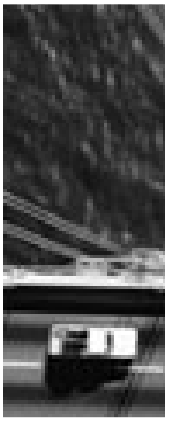
In 2011, the MSRB also co-hosted regulatory and compliance events with the Bond Dealers of America and the Securities Industry and Financial Markets Association. The MSRB participated in these events, along with staff members from the Securities and Exchange Commission, the Internal Revenue Service and the Financial Industry Regulatory Authority.

Late in the year, the MSRB engaged in meetings and discussions with representatives of state and local governments to better understand how the MSRB could provide educational materials for municipal government officials. These discussions contributed to development of an online "toolkit" that provides information to state and local governments related to regulations governing financial professionals, as well as instructions for using the MSRB's EMMA website.

All MSRB education and outreach events resulted in strengthening relationships between the MSRB and municipal market stakeholders, and demonstrated the MSRB's commitment to a fair rulemaking process.

MSRB EDUCATION AND OUTREACH EVENTS
OCTOBER 2010–2011





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2011–2012 MUNICIPAL SECURITIES RULEMAKING BOARD

OFFICERS 2011–2012

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ROBERT A. LAMB
Vice Chair

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and Finance
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Chief Financial Officer
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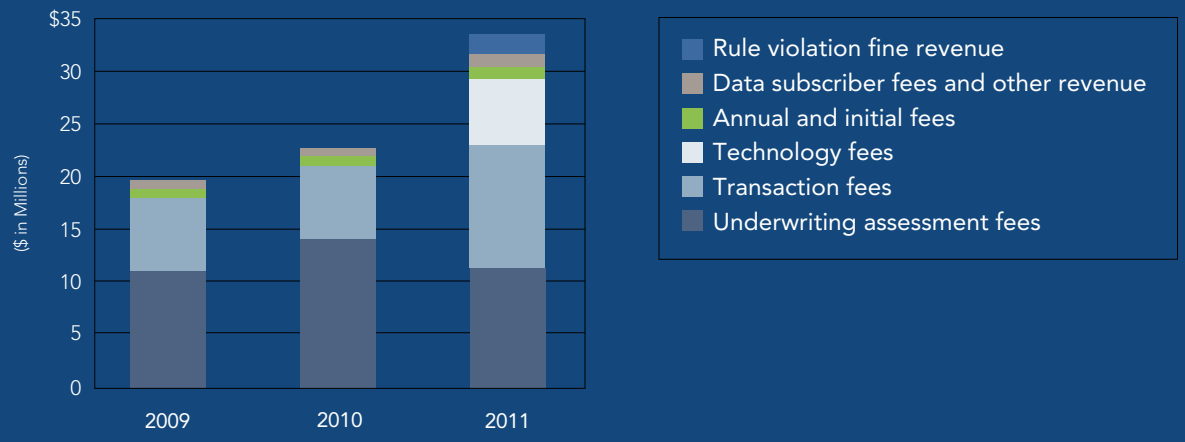
Goldman, Sachs & Co.
New York, New York

Financial Highlights

REVENUE

The MSRB's mission of protecting investors, issuers of municipal securities and public pension plans by promoting a fair and efficient marketplace requires that the organization have stable and sufficient funding. Accordingly, the MSRB has worked to ensure adequate funding aligned with the associated costs of fulfilling this mission and the organization's regulatory mandate, both of which were expanded in 2011 as a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act. In 2011, the MSRB diversified its revenue sources to ensure more balanced and equitable funding. FY 2011 reflects growth in total revenue as a result of targeted efforts to adequately fund operations, coupled with new revenues. Transaction fees paid by municipal securities dealers doubled from $.005 to $.01 per $1,000 par value on January 1, 2011 for most municipal securities sales transactions reported to the MSRB. In addition, technology fees were introduced beginning January 1, 2011, requiring municipal securities dealers to pay a $1.00 per transaction fee for all sales transactions to update, replace, and maintain the MSRB technology systems. The Dodd-Frank Act provides that fines collected by the SEC and/or FINRA for violation of MSRB rules be shared with the MSRB. Accordingly, fine revenue appears for the first time in FY 2011.

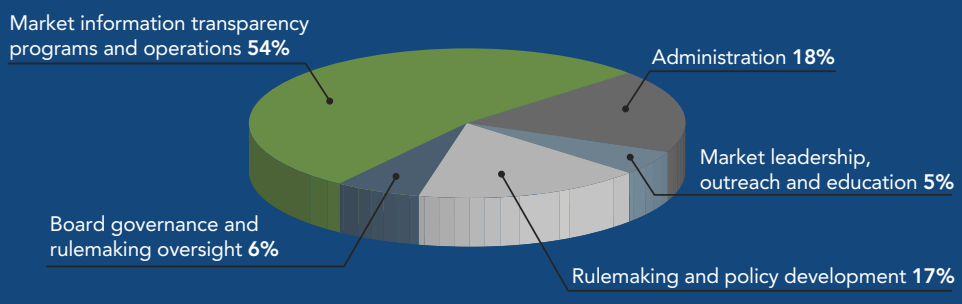
REVENUE



EXPENSES

The MSRB expenses reflect its core mission: rulemaking and policy development; board governance and rulemaking oversight; market information transparency programs and operations; market leadership, outreach and education; and administration. In FY 2011, operating expenses totaled $26,075,879.

EXPENSES





2011 FINANCIAL HIGHLIGHTS

September 30,	**2011**	2010	2009
Statements of Financial Position			
Total Assets	$36,651,410	$29,760,889	$30,777,664
Total Liabilities	3,312,474	3,825,563	4,391,176
Total Net Assets—Unrestricted	33,338,936	25,935,326	26,386,488
Statements of Activities			
Revenue:			
Underwriting assessment fees	11,368,394	13,984,780	10,837,652
Transaction fees	11,348,228	6,940,551	7,150,905
Technology fees	6,280,060	—	—
Annual and initial fees	1,281,200	1,018,821	631,100
Data subscriber fees and other revenue	1,217,774	736,094	1,008,327
Rule violation fine revenue	1,983,833	—	—
Total Revenue	33,479,489	22,680,246	19,627,984
Expenses	26,075,879	23,131,408	21,281,260
Change in Net Assets	$ 7,403,610	$ (451,162)	$ (1,653,276)
Statements of Cash Flows			
Cash Provided from Operating Activities	$ 8,572,169	$ 2,563,789	$ 41,699
Investment in Technology Systems and Other Fixed Assets	$ 4,236,002	$ 3,819,043	$ 5,065,567

Auditor's Letter

Deloitte.

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USA

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Audit Committee of
Municipal Securities Rulemaking Board
Alexandria, Virginia

We have audited the accompanying statements of financial position of Municipal Securities Rulemaking Board (the "Board") as of September 30, 2011, and the related statements of activities and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Board for the year ended September 30, 2010 were audited by other auditors whose report, dated December 2, 2010, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Board's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Board as of September 30, 2011, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte + Touche LLP

December 14, 2011

Member of
Deloitte Touche Tohmatsu

STATEMENTS OF FINANCIAL POSITION

As of September 30,	2011	2010
Assets		
Cash	$ 2,931,963	$ 1,736,866
Accounts receivable—net	6,247,626	3,927,581
Accrued interest receivable	—	72,998
Other assets	440,613	208,804
Investments	19,320,350	16,228,328
Fixed assets—net of accumulated depreciation and amortization of $16,310,663 and $12,782,423 in 2011 and 2010	7,710,858	7,586,312
Total	$36,651,410	$29,760,889
Liabilities and Net Assets		
Accounts payable and accrued liabilities	$ 1,060,418	$ 1,137,604
Accrued vacation payable	549,789	758,728
Deferred rent	1,642,583	1,814,979
Deferred compensation	59,684	114,252
Total liabilities	3,312,474	3,825,563
Undesignated net assets	30,502,641	25,935,326
Designated technology renewal fund	2,836,295	—
Net assets—unrestricted	33,338,936	25,935,326
Total	$36,651,410	$29,760,889

See notes to financial statements.

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

For the years ended September 30,	**2011**	**2010**
Revenue:		
Underwriting assessment fees	$11,368,394	$13,984,780
Transaction fees	11,348,228	6,940,551
Technology fees	6,280,060	—
Rule violation fine revenue	1,983,833	—
Annual and initial fees	1,281,200	1,018,821
Data subscriber fees	1,021,412	509,547
Professional qualifications examination fees	122,520	92,220
Investment return	60,145	92,715
Publications and other income	13,697	41,612
Total Revenue	33,479,489	22,680,246
Expenses:		
Rulemaking and policy development	4,483,383	4,133,981
Board governance and rulemaking oversight	1,631,778	1,625,522
Market information transparency programs and operations	13,907,119	11,858,000
Market leadership, outreach and education	1,367,044	863,495
Administration	4,686,555	4,650,410
Total Expenses	26,075,879	23,131,408
Change in Net Assets	7,403,610	(451,162)
Net Assets—Beginning of year	25,935,326	26,386,488
Net Assets—End of year	$33,338,936	$25,935,326

See notes to financial statements.

STATEMENTS OF CASH FLOWS

For the years ended September 30,	2011	2010
Cash Flows from Operating Activities:		
Change in net assets	$ 7,403,610	$ (451,162)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	4,058,819	3,252,682
Impairment of long-lived assets	37,835	—
Loss on disposal of long-lived assets	14,804	3,980
Net amortization of investment discounts	21,322	187,974
Unrealized loss on investments	27,726	212,133
Bad debt expense	41,073	31,265
Changes in assets and liabilities:		
Accounts receivable	(2,361,117)	(271,191)
Accrued interest receivable	72,998	89,755
Other assets	(231,809)	(23,663)
Accounts payable and accrued liabilities	(77,188)	(472,416)
Accrued vacation payable	(208,940)	52,784
Deferred rent	(172,396)	(92,316)
Deferred compensation	(54,568)	43,964
Net cash provided by operating activities	8,572,169	2,563,789
Cash Flows from Investing Activities:		
Purchases of fixed assets	(4,236,002)	(3,819,043)
Purchases of investments	(30,545,764)	(8,709,421)
Maturities of investments	27,404,694	10,325,000
Net cash used in investing activities	(7,377,072)	(2,203,464)
Cash Flow from Financing Activity—Payments on note payable	—	(97,629)
Net Increase in Cash	1,195,097	262,696
Cash—Beginning of year	1,736,866	1,474,170
Cash—End of year	$ 2,931,963	$ 1,736,866
Supplemental Information:		
Interest paid	$ —	$ 4,920
Taxes paid	$ 14,041	$ 13,739

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

NOTE 1.—NATURE OF OPERATIONS

The Municipal Securities Rulemaking Board (MSRB) was established in 1975 pursuant to authority granted by the Securities Exchange Act of 1934, as amended by the Securities Acts Amendments of 1975, as an independent, self-regulatory organization charged with protecting investors and the public interest by promoting a fair and efficient municipal securities market through rulemaking on the municipal securities activities of broker-dealers and banks. Effective May 17, 1989, the MSRB became incorporated as a not-for-profit, non-stock corporation in the Commonwealth of Virginia. The MSRB also collects and disseminates market information, and operates the Electronic Municipal Market Access (EMMA®) website to promote transparency and widespread access to information.

On October 1, 2010, the MSRB's mission was expanded by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) to protect municipal entities and obligated persons and to undertake rulemaking in connection with the municipal advisory activities of municipal advisors.

NOTE 2.—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The MSRB's financial statements are prepared using the accrual basis of accounting in accordance with the accounting principles generally accepted in the United States of America (GAAP).

Investments

Investments are stated at fair value. Investments consist of United States (U.S.) Treasury notes, government-guaranteed agency securities, and mutual funds. The U.S. Treasury notes had various maturity dates through April 2011. MSRB holds a 457(f) Rabbi Trust that is comprised entirely of mutual funds.

Amortization and accretion of investment premiums and discounts are recorded as a component of investment return.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded at invoiced amounts and do not bear interest. Accounts receivable are reported net of an allowance for doubtful accounts in the statements of financial position. Management's estimate of the allowance for doubtful accounts is based on historical collection experience and ongoing reviews. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

Concentration of Credit Risk

Financial instruments that potentially subject the MSRB to a concentration of credit risk consist principally of cash and accounts receivable. Cash balances at times are in excess of federally insured amounts and, as a result, subject the MSRB to a degree of credit risk. As of September 30, 2011 and 2010, the MSRB's uninsured cash balance amounts to $0 and $1,236,866, respectively. As of January, 2011, the MSRB maintained all cash in a non-interest-bearing account with unlimited FDIC insurance. Accounts receivable consist of fees due from municipal securities brokers and dealers. At times, there are certain significant balances due from regulated entities but the MSRB does not believe it is exposed to any significant credit risk on these balances. Four regulated entities accounted for 37% and 43% of total revenues in fiscal year 2011 and fiscal year 2010, respectively.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are used in accounting for, among other things, realization of accounts receivable, the carrying value of investments, and the impairment of long-lived assets. Actual results could differ from those estimates.

Reclassifications

Certain amounts included in the fiscal year 2010 financial statements have been reclassified to conform to the fiscal year 2011 presentation. Annual fees and initial fees revenue have been combined. To be consistent with fiscal year 2011 allocations of expenses across program services, technology expenses for internal corporate support of $1,258,682 included in Administration in fiscal year 2010 were allocated among the program services benefited.

Fixed Assets

Furniture and fixtures, as well as computer and office equipment, are recorded at cost and are depreciated using the straight-line method over five years and three years, respectively. Leasehold improvements are amortized using the straight-line method over the shorter of the remaining lease period or the estimated useful life of the improvement. Improvements and replacements of fixed assets are capitalized. Maintenance and repairs that do not improve or extend the lives of fixed assets are charged to expense as incurred.

When assets are sold or retired, their cost and related accumulated depreciation are removed from the accounts, and any gain or loss is recognized in the statements of activities and changes in net assets.

Capitalized Software Costs

The MSRB capitalizes certain costs associated with computer software developed or obtained for internal use. The MSRB's policy provides for the capitalization of external direct costs of materials and services, and direct payroll-related costs incurred during the application development stage as well as costs related to upgrades and enhancements to internal use software provided it is probable that these expenditures will result in additional functionality. Costs associated with preliminary project stage activities, training, maintenance, and post implementation stage activities are expensed as incurred.

After all substantial testing and deployment are completed and the software is ready for its intended use, internally developed software costs are amortized using the straight-line method over three years.

Impairment of Long-lived Assets

The MSRB's policy is to review its long-lived assets, such as fixed assets and capitalized software costs, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment, if any, is recognized in the period of identification to the extent the carrying amounts of an asset exceeds the fair value of such asset.

Leases

The MSRB leases office space and certain office equipment under non-cancelable operating leases and may include options that permit renewals for additional periods. Rent abatements and escalations are considered in the determination of straight-line rent expense for operating leases. Lease incentives are recorded as a deferred credit and recognized as a reduction to rent expense on a straight-line basis over the lease term.

Revenue Recognition:

Underwriting Assessment Fees—With the limited exceptions noted below, the underwriting assessment fee is equal to a $0.03 per $1,000 of the face amount of municipal securities, which are purchased by underwriters from an issuer as part of a new issue. Beginning December 1, 2009, the MSRB assessment increased to $0.03 per $1,000 for new issue municipal securities puttable back to the issuer between nine months and two years or with a final stated maturity between nine months and two years which were previously assessed at a rate of $0.01 per $1,000. Additionally, beginning December 1, 2009, the MSRB applied its $0.03 per $1,000 underwriting assessment to previously exempt securities, including those (i) with a par value of less than $1 million; (ii) sold in certain limited offerings or private placements; (iii) that are puttable back to the issuer every nine months or less, such as variable rate demand obligations; and (iv) with a final stated maturity of nine months or less. Currently commercial paper and municipal fund securities are exempt from the assessment.

Revenue from underwriting assessment fees is recognized in the month the underwriter files the offering document with the MSRB.

Transaction Fees—Prior to January 1, 2011, the transaction fee was $0.005 per $1,000 par value of bonds sold and was levied on both customer and interdealer transactions as specified in Board Rule A-13. As described in this rule, certain transactions are exempt from this fee. Effective January 1, 2011, the transaction fees paid by municipal securities dealers increased from $0.005 per $1,000 par value to $0.01 per $1,000 par value.

Transaction fee revenue is recognized as sales transactions are settled. Unbilled receivables consist primarily of September transaction and technology fees revenue billed in October.

Technology Fees—Effective January 1, 2011, the MSRB established a new technology fee on municipal securities trades reported to the MSRB. Municipal securities dealers are required to pay an assessment of $1.00 per transaction for all sales transactions. As further described in Note 12, the MSRB Board has designated the use of the funds generated by these fees to update, maintain, and replace its technology systems.

Technology fee revenue is recognized as sales transactions are settled. Unbilled receivables consist primarily of September transaction and technology fees revenue billed in October.

Rule Violation Fee Revenue—The Dodd-Frank Act provided, as of October 1, 2010, that fines collected by the Securities and Exchange Commission (SEC) for violations of the rules of the MSRB shall be equally divided between the SEC and the MSRB and that one-third of fines collected by the Financial Industry Regulatory Authority (FINRA) allocable to violations of the rules of the MSRB will be paid to the MSRB, although the portion of such fines payable to the MSRB may be modified at the direction of the SEC upon agreement between the MSRB and FINRA. FINRA fine revenue is recorded in the month earned. At September 30, 2011, no SEC fine revenue has accrued to the benefit of the MSRB.

Annual and Initial Fees—With respect to each fiscal year of the MSRB in which a municipal securities broker or dealer conducts business, the broker or dealer is required to pay an annual fee of $500 per Rule A-14. Revenue is recognized when brokers or dealers are billed annually.

Effective October 1, 2010, the Dodd-Frank Act also expanded MSRB's regulatory jurisdiction to cover municipal advisors who advise state and local governments and other municipal entities on municipal financial products and municipal securities. Rule A-14 governing annual fees was amended to include municipal advisors, effective as of November 15, 2010, at which time the MSRB began registering and collecting an annual fee of $500 as part of the registration process for municipal advisors. During fiscal year 2011, municipal advisor annual fee revenue is recognized when received.

The initial fee is a onetime fee of $100, which is to be paid by every municipal securities broker or dealer upon registration with the MSRB under Rule A-12. Rule A-12 was amended to include municipal advisors, effective as of November 15, 2010, at which time the MSRB began collecting the one-time fee of $100 from municipal advisors. Initial fee revenue is recognized when received.

Data Subscriber Fees—The MSRB collects, stores, and provides access to information pertaining to the municipal securities market. The MSRB operates four computer-based information systems that offer data subscription for a fee: an electronic document and data system for the collection, processing, storage, and dissemination of official statements, advance refunding documents, and related data (the EMMA® Primary Market Disclosure System); an electronic document and data system for the collection, processing, storage, and dissemination of continuing disclosure documents and related data from municipal securities issuers, obligated persons, and their agents (the EMMA® Continuing Disclosure System); an electronic data system for the collection, processing, storage, and dissemination of data on all municipal securities transactions for purposes of price transparency and surveillance (the Real Time Transaction Reporting System); and an electronic document and data system for the collection, processing, storage, and dissemination of data on short-term obligation rate reset data and related documents (the Short-term Obligation Rate Transparency System). Information in these systems is sold to subscribers on an annual basis, with the annual subscription fee billed on a quarterly basis and revenue recognized as billed. In addition, the MSRB maintains files for public access of information submitted by municipal securities brokers and dealers in connection with political contributions and municipal securities business under MSRB Rule G-37. Copying fees are levied at the time of use for the reproduction of any documents.

Professional Qualification Examination Fees—New Rule A-16 established an examination fee of $60 assessed on persons taking certain qualification examinations, which became effective on January 4, 2010. These examinations include the Series 51 (Municipal Fund Securities Limited Principal Qualification Examination), Series 52 (Municipal Securities Representative Qualification Examination), and Series 53 (Municipal Securities Principal Qualification Examination). Professional qualification examination fees are recognized in the month the exams are given.

New Accounting Pronouncement

In May 2011, the Financial Accounting Standards Board issued amendments to the guidance pertaining to fair value measurement and disclosure. The amendments create a common definition of fair value for GAAP and International Financial Reporting Standards (IFRS) and align the measurement and disclosure requirements. These amendments provide further guidance on some of the principles for measuring fair value and expand the disclosure requirements specifically for Level 3 fair value measurements. The new requirements are effective for annual periods beginning after December 15, 2011 and will be applied prospectively. The MSRB has determined that the adoption of these new requirements will not have a material impact on its changes in net assets or financial position.

NOTE 3.—INVESTMENTS

Investments as of September 30, 2011 and 2010, consist of the following:

	2011	2010
U.S. Treasury notes	$ —	$ 6,838,004
Government-guaranteed agency securities	19,263,486	9,263,250
Mutual funds	56,864	127,074
	$19,320,350	$16,228,328

Investment return for the years ended September 30, 2011 and 2010, consists of the following:

	2011	2010
Interest and dividends	$ 87,871	$ 304,848
Unrealized losses	(27,726)	(212,133)
	$ 60,145	$ 92,715

NOTE 4.—FAIR VALUE MEASUREMENTS

The carrying amounts of financial instruments, including cash, receivables, accounts payable, and accrued expenses approximate fair value as of September 30, 2011 and 2010 because of the relatively short duration of these instruments.

The MSRB's policy defines fair value, uses a framework for measuring fair value, and provides a fair value hierarchy based on observable inputs.

Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect assumptions that market participants would use in pricing the asset or liability based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the transparency of inputs as follows:

Level 1—Valuation based on quoted prices available in active markets for identical assets or liabilities as of the report date.

Level 2—Valuations based on inputs other than quoted prices included within Level 1, that are observable, either directly or indirectly.

Level 3—Valuations based on significant inputs that are unobservable and reflect management's best estimate of what market participants would use as fair value.

The MSRB considers observable market data to be readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market. The categorization of a financial instrument within the hierarchy is based upon the pricing transparency of the instrument and does not necessarily correspond to the entity's perceived risk of that instrument.

The MSRB's Level 1 investments include mutual funds, and as of September 30, 2010, any U.S. Treasury notes and government-guaranteed agency securities that had trades on the observation date.

The MSRB's Level 2 investments include government-guaranteed agency securities which on September 30, 2010 had no observable trades. For the year ended September 30, 2011, the MSRB determined that it was most appropriate to consider the market for government-guaranteed agency securities as inactive, regardless of observable trades on September 30, 2011. Therefore as of September 30, 2011, all government-guaranteed agency securities are considered Level 2 investments.

The MSRB bases the fair value on pricing obtained from the MSRB's investment broker. The MSRB does not adjust for or apply any additional assumptions or estimates to the pricing information it receives from its broker. The broker's pricing is compared to industry standard data providers (e.g., Bloomberg) for reasonableness. The MSRB considers this the most reliable information available for the valuation of investments.

Investments were recorded at fair value as of September 30, 2011 and 2010, based on the following levels of hierarchy:

2011	Level 1	Level 2	Level 3	Total
Government-guaranteed agency securities	$ —	$19,263,486	$ —	$19,263,486
Mutual funds	56,864	—	—	56,864
	$ 56,864	$19,263,486	$ —	$19,320,350

2010	Level 1	Level 2	Level 3	Total
U.S. Treasury notes	$ 6,838,004	$ —	$ —	$ 6,838,004
Government-guaranteed agency securities	4,263,850	4,999,400	—	9,263,250
Mutual funds	127,074	—	—	127,074
	$11,228,928	$ 4,999,400	$ —	$16,228,328

NOTE 5.—ACCOUNTS RECEIVABLE

Accounts receivable as of September 30, 2011 and 2010, consist of the following:

	2011	2010
Billed accounts receivable	$4,619,887	$3,436,286
Unbilled accounts receivable	1,899,778	726,846
	6,519,665	4,163,132
Less allowance for doubtful accounts	(272,039)	(235,551)
	$6,247,626	$3,927,581

NOTE 6.—FIXED ASSETS

Fixed assets as of September 30, 2011 and 2010, consist of the following:

	2011	2010
Leasehold improvements	$ 1,936,517	$ 1,421,356
Computer and office equipment	2,236,216	2,350,974
Furniture and fixtures	1,662,357	1,418,815
Capitalized software costs	18,186,431	15,177,590
	24,021,521	20,368,735
Less accumulated depreciation and amortization:		
Leasehold improvements	(1,001,730)	(796,229)
Computer and office equipment	(1,500,319)	(1,615,016)
Furniture and fixtures	(1,362,580)	(1,319,282)
Capitalized software costs	(12,446,034)	(9,051,896)
	(16,310,663)	(12,782,423)
	$ 7,710,858	$ 7,586,312

Depreciation and amortization expense during the fiscal years 2011 and 2010 are as follows:

	2011	2010
Depreciation expense	$ 486,077	$ 419,355
Amortization expense for capitalized software cost and leasehold improvements	3,572,742	2,833,327
	$ 4,058,819	$ 3,252,682

Impairment of long-lived assets—Through regular review of long-lived assets, in fiscal year 2011 an estimated impairment loss of $37,835 was recognized.

NOTE 7.—ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of September 30, 2011 and 2010, consist of the following:

	2011	2010
Accounts payable	$ 368,306	$ 686,859
Salaries, taxes, and benefits payable	531,889	264,290
Other accrued expenses	160,223	186,455
	$ 1,060,418	$ 1,137,604

NOTE 8.—NOTE PAYABLE

In May 2009, the MSRB entered into a financing agreement for the purchase of software and annual software support. Payments under this agreement totaled $97,629 for the fiscal year ended September 30, 2010.

The debt was extinguished in May 2010. No notes payable were outstanding as of September 30, 2011 and 2010.

NOTE 9.—COMMITMENTS

Operating Leases

The MSRB leases office space and certain office equipment under operating lease arrangements. In May 2001, the MSRB entered into a lease for office space in Alexandria, Virginia, which will expire in fiscal year 2016. The operating lease agreement for this office space contains provisions for future rent increases. The total amount of rental payments due over the lease term is being charged to rent expense on a straight-line basis over the term of the lease. The difference between rent expense recorded and the amount paid is credited or charged to deferred rent, which is included in the liabilities in the accompanying statements of financial position.

Future minimum lease payments under non-cancelable operating leases are as follows:

Year ending September 30,	
2012	$1,771,344
2013	1,833,336
2014	1,897,512
2015	1,963,920
2016	998,844
Total minimum lease payments	$8,464,956

Total rent expense for office space and equipment for the years ended September 30, 2011 and 2010, was $2,206,315 and $2,226,223, respectively.

Employment Agreements

In accordance with the executive director's employment agreement, a 457(f) deferred compensation plan is maintained. The agreement calls for contributions of $10,000 on September 30, 2010, $50,000 on September 30, 2011, and $55,000 on September 30, 2012. The sum, including all earnings and interest accrued, will be paid on September 30, 2012, or such earlier time as set forth by the agreement. During fiscal year 2011, a previously vested amount of $126,312 was paid to the executive director. The organization maintains a mutual fund where the contributions are invested; this account is reflected as a component of MSRB's investments. As of September 30, 2011 and 2010, the MSRB has recorded a deferred compensation liability of $59,684 and $114,252, respectively.

The MSRB has a contract with its former executive director that calls for medical benefits to be provided to the executive director and his spouse for a term ending on December 2012. As of September 30, 2011 and 2010, MSRB has included a liability related to this benefit of $28,551 and $71,402, respectively, in salaries, taxes, and other benefits payable. In addition to the above agreement, the MSRB entered into separation agreements with other former employees, and as of September 30, 2011 and 2010, the MSRB has recorded a liability related to these agreements of $208,403 and $423, respectively, in salaries, taxes, and other benefits payable.

NOTE 10.—RETIREMENT PLAN

The MSRB has a defined contribution pension plan for all employees. Participation commences upon completion of one month of eligible service as described in the plan document. For all active participants employed on the first day of the calendar quarter, the MSRB makes a quarterly contribution as required by the plan document. These contributions are based on the participants' quarterly compensation for the calendar quarter immediately preceding the first day of the calendar quarter. The contribution percentage ranges from 9% to 12% depending on the length of vested service as scheduled in the plan document. Each employee is fully vested upon being credited with three plan years of

service. Employees may also make voluntary contributions to the plan. The MSRB made contributions to the plan totaling $831,881 and $673,593 for the years ended September 30, 2011 and 2010, respectively.

All administrative expenses of the plan are paid by the MSRB. Administrative expenses total $14,544 and $18,014 for the years ended September 30, 2011 and 2010, respectively.

NOTE 11.—INCOME TAXES

The MSRB is exempt from federal and state taxes on income (other than unrelated business income) under Section 501(c)(6) of the Internal Revenue Code and applicable income tax regulations of the Commonwealth of Virginia. No provision for income taxes has been made as of September 30, 2011 and 2010.

Effective September 30, 2010, the MSRB adopted new guidance that creates a single model to address uncertainty in tax positions and clarified the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in its financial statements. Under the requirements of this guidance, organizations could now be required to record an obligation as the result of tax positions they have historically taken on various tax exposure items. The impact of the adoption of this guidance did not have a material effect on the financial statements of MSRB. Prior to the adoption of this guidance, the determination of when to record a liability for a tax exposure was based on whether a liability was considered probable and reasonably estimable in accordance with guidance concerning recording of contingencies.

NOTE 12.—BOARD-DESIGNATED NET ASSETS

By policy, prior to January 1, 2011, the MSRB maintained sufficient cash and investments at a level not to exceed one-year of expenses. Unrestricted net assets were designated for future capital projects, including technology systems, and to fund reserves for operating expenses.

Beginning January 1, 2011, a board-designated technology renewal fund was established to provide funds for capital expenditures, such as the replacement or acquisition of computer hardware and software. The technology renewal fund is credited with all revenue derived from the technology fee and depleted by technology information capital expenses. With the establishment of the technology renewal fund, the undesignated net assets provide for operating capital in the event of a revenue shortfall or for significant unplanned expenditures.

	2011
Technology fees	$ 6,280,060
Technology capital expenditures	(3,443,765)
Designated technology renewal fund	$ 2,836,295

NOTE 13.—SUBSEQUENT EVENTS

The MSRB evaluated its September 30, 2011, financial statements for subsequent events through December 14, 2011, the date the financial statements were available to be issued. The MSRB is not aware of any subsequent events that would require recognition or disclosure in the financial statements except as disclosed below.

Effective October 1, 2011, the contribution percentages for the defined contribution pension plan were reduced from a range of 9% to 12% to a range of 7% to 9%, depending on the length of vested service as scheduled in the plan document.

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Executive Director

Ernesto A. Lanza
Deputy Executive Director
and Chief Legal Officer

Peg Henry
General Counsel—
Market Regulation

Al Morisato
Chief Operations and
Technology Officer

Ritta McLaughlin
Senior Director,
Market Leadership

Jennifer A. Galloway
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