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Why SIFMA, BDA Want Shorter Dealer Closeout Timeframes.

WASHINGTON – Dealer groups are urging the Municipal Securities Rulemaking Board to cut in half a proposed requirement that would mandate municipal securities transactions to be closed out within 20 days of settlement.

The change to a 20-day closeout requirement from the current 90-day recommendation under the MSRB Rule G-12 on uniform disclosure would lessen the effect of interdealer transaction failures on the market, the MSRB has said. The self-regulator filed the proposed change for approval with the Securities and Exchange Commission on May 11.

Mike Nicholas, Bond Dealers of America's chief executive officer, and Leslie Norwood, associate general counsel and co-head of munis for the Securities Industry and Financial Markets Association, agreed with the MSRB's reasoning for shortening the closeout timeframe.

However, they said in comment letters to the SEC that they believe the mandatory close-out deadline should be shortened to no later than 10 calendar days after settlement. The groups are also proposing that there be a caveat allowing a dealer to extend that deadline another 10 days, for a total of 20 days, if the dealer gets the consent of the buyer.

"We feel it is better for all market participants, the dealers as well as the investors, if failed transactions get settled sooner rather than later," Norwood said. SIFMA believes the majority of dealers would close out the transactions within the 10-day window because "the exemption to go another 10 days is not a slam dunk where it is just something that the dealer opts into," she added.

The MSRB originally proposed amending the rule to require transactions are closed out no later than 30 days after settlement. SIFMA responded similarly to that proposal, recommending the period be cut to 15 days with the possibility of an extra 15 days if the buyer consents. The MSRB chose against the 15-day timeframe because it said it was concerned small dealers would be overburdened by a shorter timeline and because it wanted to give all dealers the same fixed timeframe.

Norwood, in her most recent comment letter, said that after extensive discussions with SIMFA's broad range of broker-dealer members, the group feels the MSRB's concerns are not warranted.

The MSRB is also seeking rule changes that would allow the purchasing dealer to start close-out procedures within three business days of the settlement date, a change from the current 10-business day window. Additionally, the proposal would change the earliest day for execution to four days after electronic notification instead of the rule's current 11 days after notice by telephone.

While the time period for close-outs would be significantly shortened, the three interdealer options for remedying a failed transaction would remain the same through the transition. The purchasing dealer could choose a "buy-in" and go to the open market to purchase the securities. It could also choose to accept securities from the selling dealer that are similar to the originally purchased securities in a number of areas. Lastly, the purchasing dealer could require the seller to repurchase the securities along with payment of accrued interest and the burden of any change in market price

or yield.

In addition to their recommendations about the closeout timeframe, BDA and SIFMA also asked the MSRB to provide further guidance as to how the MSRB's multiple changes would work in practice.

SIFMA brought up an issue it had noted in past comments, saying it would be "extremely helpful" to know whether a dealer should have the authority to close out a position by returning it to the seller when a customer with a self-directed account won't agree to do so. Dealers aren't allowed to use their discretion when working with self-directed accounts, SIFMA said, though the MSRB does have the ability to mandate dealers act as well as the ability to provide regulatory relief.

BDA is asking for further clarification on the closeout process for accounts transferred to a dealer through the Automated Customer Account Transfer Service (ACATS). The system facilitates the transfer of securities from one trading account to another at a different brokerage firm or bank.

Nicholas wrote that the timeframe under the G-12 amendment would work for ACATS, though he said ACATS transfers are based on a "validation" date as opposed to a "settlement" date. Fail transfers can additionally be closed out by a fail reversal if the receiving firm cannot buy-in the security due to a lack of market availability, but the portion of G-12 that would be amended doesn't mention fail reversals as a closeout process, he wrote.

Dealers would have a 90-calendar day grace period after the MSRB's rule change is approved to resolve all outstanding dealer fails.

The Bond Buyer

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