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Why the MSRB is Shortening its Dealer Closeout Timeframes.

WASHINGTON – The Municipal Securities Rulemaking Board wants to cut in half a proposed requirement to mandate municipal securities transactions be closed out within 20 days of settlement after dealer groups pushed for the shorter timeframe.

The MSRB proposed a move to a 10-day closeout requirement, with the option for a one-time 10-day extension if the buyer of the municipal security consents, in a partial amendment with the Securities and Exchange Commission. The 10-day requirement, which the MSRB proposed on Monday, would join other proposed changes to MSRB Rule G-12 on uniform practice that the MSRB filed with the SEC for approval on May 11.

“Shortening the close-out period from 20 calendar days, as stated in the original proposed rule change, to 10 calendar days will further reduce the risk and cost associated with interdealer [failures],” the MSRB said in its amendment.

The partial amendment mirrors suggested alterations that the Securities Industry and Financial Markets Association and Bond Dealers of America had proposed.

“We emphasize in our [comment] letter and the MSRB states in its amendments that failed transactions don’t get better with age,” said Leslie Norwood, associate general counsel and co-head of munis for SIFMA. “To that end, we are very pleased that the MSRB is taking this step to give investors greater certainty and reduce the risk and cost for regulated broker-dealers.”

John Vahey, director of federal policy for BDA, said BDA’s members “are pretty satisfied with the way the rulemaking is going.”

Under the MSRB’s current Rule G-12, there is no specific time requirement for closeouts, only a recommendation that any dealer that fails to deliver securities to another dealer by the agreed upon settlement date close out those interdealer trade failures within 90 days of the settlement date.

When the MSRB first proposed changing the rule, it recommended there be a requirement that failures be closed out no later than 30 days after settlement. SIFMA responded to that proposal by suggesting the MSRB instead require a closeout within 15 days of settlement with the possibility of an extra 15 days if the buyer consents.

The MSRB then changed its proposal to require a closeout within 20 days after the settlement date, citing both concerns that smaller dealers would be overburdened by a shorter timeline and a desire to ensure all dealers operated under the same, fixed timeline.

SIFMA said the concerns weren’t warranted and again argued the time period was too long. Both SIFMA and BDA then recommended the 10-day timeline with the possibility of a 10-day extension.

The dealer groups also brought up other issues, with SIFMA 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. BDA asked for further clarification on the closeout process for accounts transferred to a dealer through the Automated Customer Account Transfer Service (ACATS). ACATS facilitates the transfer of securities from one trading account to another at a different brokerage firm or bank.

The MSRB said in a footnote in its partial amendment that both concerns are "beyond the scope of the original proposed rule change and current proposed rule change."

In addition to the changes to the timeline for resolving interdealer failures, the MSRB is also asking the SEC to approve proposals 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. The MSRB proposal would also 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.

The MSRB plans to give dealers a 90-day grace period after SEC approval to come into compliance with the changes.

The Bond Buyer

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